Student Debt Weighs on All of Us

By Eugene Steuerle *Thu, Oct 6, 2016*

'If this debt policy additionally discourages risk taking and marriage after education, then all this debt may even reduce investment over time in education, businesses, and homes combined,' writes our guest author, an Urban Institute scholar.

The 2016 presidential election has made student debt a national issue. Two just-released books, one by Sandy Baum and one by Beth Akers and Matt Chingos, have done a great job of identifying the real problems with student debt, while debunking much of the rhetoric that tends to identify wrong problems and come up with wrong solutions. I highly recommend the books, though I am hardly unbiased since Matt and Sandy are colleagues of mine.

By focusing on the real risks associated with the current system, the authors emphasize thatwe must pay attention to who acquires the debt and who benefits from it. For instance, future doctors and lawyers with high returns to postgraduate education acquire some of the highest levels of student debt. Akers and Chingos emphasize that over 40 percent of student debt is held by those in the top 20 percent of the income stratum. Thus, simply eliminating student debt would help the highest income borrowers most.

Sandy Baum focuses on designing proposals that would prevent so many at-risk students from borrowing for programs unlikely to serve them well. She especially discredits proposals that provide the most assistance to those who are actually in the best position to repay their loans. One example of how all this plays out was shown earlier by some other colleagues: blacks as a group, who are less likely to come out of college with a degree, end up with higher average student debt than whites.

Here I wish to address a more macro question: whether this shift toward higher student debt represents just one more way that government has disinvested in the economy. As students accumulated $1.3 trillion in debt, did government make an equivalent increase in investment in what economists often call “human capital”? Or did government simply shift additional burdens onto these students with few or no significant gains in educational achievement nationwide? Or something in between?

When we look at budgets as a whole, both federal and state, it’s quite clear how resources are being shifted. Average tax rates are about where they have been, maybe a touch higher.

Taxpayers may have gotten a break for a while as rates went down a bit and then back up a bit, but that’s not the main story. Both federal and state budgets have adopted huge spending increases for retirement and health care. States have also put a lot more into prisons, while the feds have put much more toward interest costs, though offered a reprieve—if one can call it that—by a weak worldwide economy that has led to low interest rates.

Clearly, a smaller share of revenues and incomes goes for education—not just higher education, but primary and secondary education as well. Almost anything that might qualify as investment, such as infrastructure, has also seen a downturn.

Taking the budget as a whole, therefore, it’s hard to avoid the conclusion that the net effect of federal and state policies, of which student loans become merely one example, has been a disinvestment in the economy as a whole.

This raises an additional issue for those assessing programs by comparing benefits to costs. In the case of student loans, if more borrowing on average increases human capital by more than the value of the loans, we would say it was worthwhile for individuals to take out those loans. Correspondingly, if we were replacing a system with less education and no loans with one that on net created more assets than debt, we would likely conclude that the shift was worthwhile societally, not just individually. However, starting from a society that had financed education more directly, the student loan policy may be a failure.

Put another way, the starting point matters. In this arena and others we usually want government to increase net investment, as well as improving the allocation of funds so as to garner the highest returns on the investment, and we need to figure out the effect across the entire balance sheet of assets and liabilities.

The individual perspective compares the personal increase in assets with the personal increase in borrowing and asks whether enough people come out ahead that society is better off. But if the additional loans don’t finance an increase in education societally, whether because some students don’t attain degrees or others don’t acquire any more education than they would have undertaken anyway, then we must ask what we got for our money.

If this debt policy additionally discourages risk taking and marriage after education, then all this debt may even reduce investment over time in education, businesses, and homes combined. Unfortunately, I think this has been the most likely outcome of recent policy.

Even the creative reforms that Baum, Akers, and Chingos recommend won't restore those past losses, though they may help minimize them in the future.

Whatever your take on this issue, this presidential campaign makes clear that higher education reform very likely will be on the national agenda in the next year or two. The Baum and Akers-Chingos studies should be required reading for anyone undertaking that reform.