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Time to rethink student lending

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To land a good job, get a college degree. This has become a mantra in most American households, and with good reason. Yet while there is no better value than college, paying for it is a daunting challenge for a growing number of families.

College tuitions have doubled over the last decade and there is little relief in sight. Financially strapped state governments are cutting back on funding for higher education in this region and beyond. Like all institutions and families, moreover, colleges and universities are grappling with losses on their investments.

During the housing boom, families tapped their home equity through loans and refinancing to pay at least some of the rising cost of tuition. Many homeowners who are now underwater got there trying to prepare their kids for solid, rewarding careers. But the housing bust left many families with little or no equity, while the tough economy cut into incomes and other savings used to pay tuition.

Thus many find borrowing the only way to afford college, and student lending has surged. Over the last decade, student debt has nearly tripled to a stunning \$1 trillion, more than all credit-card and auto-loan debt combined. Students, and the parents who often cosign their loans, clearly can't manage it; nearly a fourth are not making timely payments.

Students can sometimes defer loan payments until they find jobs. Yet unlike other debt, student loans can't be extinguished in bankruptcy. The law reasons that because borrowers lack income, lenders need protection; otherwise, student loans would be harder to find and/or carry much higher interest rates.

Recent media reports have fanned fears that defaulting student loans will blow up the financial system as subprime mortgages did, but such hysteria is overblown. While student loan debt has ballooned, it is tiny compared with the massive volume of crazy mortgages made during the housing bubble. And unlike those mortgages, student loans haven't been diced and sliced into millions of complex financial securities too complex for credit-rating agencies or investors to understand.

Moreover, the federal government backs more than three-quarters of student loans outstanding. Taxpayers, not the banks, are ultimately on the hook if today's students don't pay back their loans.

The real threat posed by student lending is that it has burdened young people with debt, without making their education more affordable. Since good educational services are in limited supply, more student lending has simply driven up tuitions.

This also threatens our economy's long-term success. Despite all our problems, the U.S. economy remains the world's most productive, and the secret of our success is a highly educated population. It's no accident that Facebook, Twitter, Google, and eBay — recent examples of our economy's ability to innovate — were born here. The key is that we educate our best and brightest.

There is no easy fix to the student-loan problem. The first question is how to help young people afford the education they and the economy need. Congress and the Obama administration are currently debating whether to keep interest rates on one popular type of student loan at 3.4 percent, or let the rate double in July to 6.8 percent. Given our current economic circumstances, it probably makes sense to extend this benefit for another year, but over time the rate subsidy should be phased out. At the end of the day, it only is adding to the cost of tuition, not making college more affordable.

A proposal to forgive some existing student-loan debt isn't a good idea. It would almost surely create a moral hazard problem, as students borrow more in the belief that it, too, will eventually be forgiven. This would eventually add tens or even hundreds of billions of dollars to the nation's debt load.

Instead of using tax money to fund student loans, let's use those resources to hire more professors, build more labs, facilitate e-learning, and fund more internships. The federal government could provide matching grants or low-interest loans to the nation's community colleges, teaming them up with private firms willing to help educate their own future employees. The quid pro quo for business would be input into college curriculums, to ensure that the training meets a real need. The goal should be to increase the supply of higher education, thus making it more affordable so that students in the future don't need as many loans to attend.

College is vital to our children's financial success, and our economy's growth depends on a highly educated workforce, but we need to rethink student lending.

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http://www.philly.com/philly/opinion/20120429_Time_to_rethink_student_lending.html