

THE STUDENT LOAN PROBLEM IN AMERICA:



IT IS NOT ENOUGH TO SAY, "STUDENTS WILL EVENTUALLY RECOVER"

Executive Summary



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KU THE UNIVERSITY OF
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**ASSETS &
EDUCATION
INITIATIVE**

FOREWORD

The Assets and Education Initiative (AEDI) is a center at the University of Kansas's School of Social Welfare (<http://aedi.ku.edu/>). AEDI's mission is to create and study innovations related to assets and economic well-being, with a focus on the relationship between children's savings and the educational outcomes of low-income and minority children as a way to achieve the American dream.

In today's financial aid landscape, advancing this mission requires attending not only to the role of assets in shaping educational attainment and equity, but also understanding the effects of student borrowing on the educational outcomes, return on educational investment, and long-term financial health of households. It is our hope that our research on these matters and analysis of others' findings add to the national conversation about the relative impacts of different approaches to college financing. In these investigations, we are particularly attuned to the implications of policy decisions and the drift of policy effects on disadvantaged children whose fates hinge more than anyone's—and more than ever—on educational attainment. We believe that the evidence clearly indicates that postsecondary education can be a path to economic mobility and an essential means of sustaining the American dream for some children. Through our research, dialogue, policy recommendations, and other efforts, we aspire to help make it a path authentically available to all children.

We look forward to imagining, together, how asset-based financial aid can make higher education a more valuable proposition for all of America's students—especially those disadvantaged in the current system—and to discussing how it can serve as an alternative to the current student loan program if combined with a bold vision of asset transfers in the spirit of the Homestead Act or the G.I. Bill of old. We assert that rebalancing current financial aid policies could bring their effects more in line with their original intents, restoring higher education to its role as a powerful arbiter of equity in a more prosperous U.S. economy. We further believe that addressing this policy challenge is among the most important tasks on the current domestic landscape, with nothing short of the American Dream at stake.

With warm regards,



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Executive Summary

According to Shapiro, the American Dream “is the promise that those who work equally hard will reap roughly equal rewards” (Shapiro, 2004, p. 87); that is, the American Dream holds that this country is a meritocracy where effort and ability are the primary determinants of success. Institutions provide the economic conditions that make it possible for people to believe that their hard work and ability will determine their success or failure. This task is facilitated by Americans’ strong desire to feel as though their destiny can be controlled and that institutions will ‘echo’ their own contributions, rather than work against them.¹ Primed to look for evidence of this ‘effort plus ability equals outcomes’ equation, Americans cling to this ideal, even as it recedes in reality for many. There is no evidence that Americans today are less capable or less committed than in previous generations, in the aggregate. Instead, particularly in today’s highly specialized, technology driven, global world, the upward mobility that animates the American Dream is only possible if effort and ability are combined with institutional might.

Post-Great Recession, Americans are surrounded by examples of unsupportive institutions and the crumbling aspirations of those whose effort and ability have failed to yield advancement. These adverse conditions are not just constraining financial progress; they imperil the foundation of even this robust American Dream. Today, a majority of Americans (63 percent) no longer believe American institutions are able to facilitate children being better off than their parents (Luhby, 2014). Instead of aspiring to economic mobility, many now hope for financial security – not dreaming of getting ahead but striving not to fall behind. While some Americans display tremendous capacity to hope against all hope, the average person requires grounds for believing that achieving the American Dream is possible. In this sense, belief in the American Dream as it relates to one’s own life is more malleable than the vague ideal one might hold for the country; it can and does readily change depending on the economic context in which one finds oneself. This suggests that people see the American Dream as more or less achievable in their own lives based largely on how institutions like the education system, labor market, and economic markets are functioning for them (Hochschild & Scovronick, 2003).

The significance of the U.S. education system in sustaining the American Dream cannot be overstated. Americans’ understanding of ‘effort and ability’ features educational attainment prominently, particularly the higher education widely understood to correlate with superior employment and earnings prospects and, then, upward mobility. Here, too, though, the aspirations of a generation of young people are colliding with the economic realities they confront, contributing to the shaky foundation on which the American Dream stands today. While it is clear that it does pay to get an education, there is plenty of evidence to suggest that it pays off unevenly. First, economically disadvantaged students carry their inferior academic preparation—forged in inferior primary and secondary schools and exacerbated by familial differences in educational investments—into post-secondary education, where it contributes to lower completion rates (Bailey & Dynarski, 2011) and longer paths to degree because of the need to take remedial classes (Engle & Tinto, 2008). Second, even highly-qualified students do not achieve equitably in college, as the economics of higher education strongly influence institutional selection to steer even high-achieving low-income students or students of color to less selective schools that spend less per student on instruction, have lower graduation rates, and yield poorer labor market returns than more competitive institutions (Carnevale & Strohl, 2013). Indeed, analysis of this ‘undermatching’ (Hoxby & Avery, 2012) suggests the existence of two tiers of higher education and powerful forces that track students into one or the other, based more on socioeconomic status than innate ability. Higher education cannot be an equalizing force if it delivers an unequal product with highly disparate outcomes. As evidence of the gap between different types of institutions, more than half of community college students fail to complete a degree, receive a certificate, or transfer to a four-year institution within six years (NCES, 2011), considerably poorer interim outcomes than students at more selective, four-year institutions.

Completion does not erase the legacies of inequity either. Despite the fact that education nearly always ‘pays’ compared to failure to pursue post-secondary studies, research suggests that the precise level of economic advantage afforded from a higher education depends on school selectivity, major, and chosen occupation. Specifically, the rate of return on a bachelor’s degree from a noncompetitive four-year private institution is under 6 percent while the rate of return on a bachelor’s degree at the most competitive public institutions is over 12 percent (Owen & Sawhill,

¹ Perceived control is highly predictive of engagement/motivation (Skinner, Zimmer-Gembeck, Connell, Eccles, & Wellborn, 1998).

2013). While there is certainly an economic need for diverse majors and a case to be made for the non-financial benefits of post-secondary education, the extent to which career choice may be influenced by the student's socioeconomic background also warrants examination, since the lifetime difference in earnings between, for example, a student who majored in engineering and a student who studied arts or humanities can be well over \$1 million (Schneider, 2013). And, finally, even when two students earn the exact same degree from the exact same institution, the real value of that credential may vary depending on the way in which they financed it, as student loan debt may erode asset accumulation for years following degree completion, thus increasing the real cost of the degree (e.g., Hiltonsmith, 2013).

Today, high college costs due in part to diminishing state funding, declining availability of non-repayable financial aid and poorer labor market outcomes may raise doubts in the minds of parents and children about whether the return on college is too risky to justify the investment of required financial and personal resources. In the lives of individual students and in the aggregate for this generation, then, education—one of the most critical institutions shaping opportunity in today's America—may be seen as less capable of facilitating a path to the American Dream.

SHIFTING UNDERSTANDING OF EDUCATION'S WELFARE FUNCTION IN AMERICA

Since the beginning of the 20th century, education has become a locus for the emphasis on opportunity, through expanded support for public schools, colleges, and universities, and eventually through provision of government subsidies to facilitate individual access to higher education. In 1976, in talking about the function of education in the American welfare system Janowitz wrote, "Perhaps the most significant difference between the institutional bases of the welfare state in Great Britain and the United States was the emphasis placed on public education – especially for lower income groups – in the United States. Massive support for the expansion of public education, including higher education, in the United States must be seen as a central component of the American notion of welfare—the idea that through public education both personal betterment and national social and economic development would take place" (pp. 34 & 35). Now such an accepted part of our approach to fostering upward mobility, it must be emphasized that placing education in this central role was not a foregone conclusion, but instead an explicit and intentional decision about how our nation, specifically, would build policy structures to complement individual effort and ability. While European nations have relied on the "direct redistributive role of the welfare state to reconcile citizenship and markets", the United States has chosen to use education as a lever for ensuring equitable outcomes (Carnevale & Strohl, 2010, p. 83). This distinctly American conviction—that economic disparity can be narrowed through individual effort in school, the pursuit of higher education, and calculated public investments in educational opportunities—runs deep. In the past few decades, though, while there is little evidence that Americans' beliefs about the importance of education as a gateway to opportunity have eroded, there has nonetheless been a repositioning and repurposing of education policies, within a shifting frame of 'welfare'. Education has been increasingly viewed as a primarily individual, rather than societal good, with the accompanying retrenchment paralleled by cuts in other arenas of welfare policy, as well. In the higher education domain, this shift can be clearly traced by examining political pronouncements about financial aid since the 1965 enactment of the Higher Education Act.

While education is certainly not the only policy sphere where shifts in arrangements between individuals and the government are reshaping opportunities and risks (Hacker, 2008), these trends are seen vividly in higher education, looking, for example, at the evolution of how presidents talk about, specifically, financial aid policy. In talking about the Higher Education Act Reauthorization of 1968 President Lyndon B. Johnson said, "So to thousands of young people education will be available. And it is a truism that education is no longer a luxury. Education in this day and age is a necessity." Here, the federal government's role is understood as making education available to all. Similarly, speaking of the Higher Education Act Reauthorization of 1980 President Jimmy Carter said, "We've brought college within reach of every student in the nation who's qualified for higher education. The idea that lack of money should be no barrier to a college education is no longer a dream—it is a reality." In education as in labor arrangements, income supports, and other policies that touch family finances, in the mid-1980s a shift occurred. Instead of education being framed as something in which the federal government had a large stake, the burden for paying for college shifted to the individual. Because relatively few households could finance these new obligations without some external assistance, given the high cost of college, this 'risk shift' (Hacker, 2008) necessitated a larger role for student loans, absent policy innovations that would bridge these gaps. In 1983 President Ronald Reagan

explicitly articulated this shift, “The cost of education is primarily the responsibility of the family. The Federal Government has a role to play in helping needy students get a chance to receive a college education.” Clearly, then, as with other welfare policies, one’s view of education is based on values, which then drive the metrics emphasized and the outcomes considered acceptable. In this report, a part of what we contend is that student loans do not align with the notion that effort and ability should determine who succeeds and who fails. Americans believe that people who work equally hard and have roughly equal ability should achieve similar outcomes, and our sharing of these values drive our assertions that, because education has a role in America as part of its welfare state, it matters not only that people have access to financial aid for paying for college. If the American Dream is to remain real, it also matters what type of financial aid they have access to and what its effects are. It is along these dimensions that we encounter concerns with the student loans.

THE STUDENT LOAN PROGRAMS ROLE IN INSTITUTIONALIZING UNEQUAL OUTCOMES

When the Higher Education Act of 1965 was enacted, student loans were not meant to be the primary instrument for financing college. In fact, student borrowing did not become the primary instrument for financing college until about the mid-1980s. Instead, grants were primarily intended for lower-income students, with loans, a compromise of sorts between Democrats’ and Republicans’ different ideas about how to expand educational opportunities, meant to help middle-income students confront the short-term cash crunch associated with the cost of college. During this period student loans were made by private lenders. However, to get private lenders to be willing to offer loans to students who, for the most part, had no credit history, the banks had to be given a guarantee that they could recoup their losses if a student defaulted. The concessions that resulted took student loans down a path which has resulted in a fairly unique debt instrument, one with an outsized significance in U.S. policy and, today, Americans’ balance sheets. If we understand student loan default as a result of the inherent difficulty in accurately predicting the return on college and not simply borrowers’ unwillingness to pay, we see this request for rules that preference lenders, though practical from the perspective of financial institutions, as creating a kind of perverse outcome where the goal becomes more to protect the *financial institutions* than the *recipients*. Given the subsequent trajectory of student loans, where borrowing has become a primary mechanism of college access for most prospective students, this positioning of financial aid within the larger credit market should have perhaps raised more alarm. Again, here it is important to recognize education—and public support for the same—not as mere academic instruction, but as a sort of “American welfare”, vastly preferred to their alternative—direct payments. It is within this role of education that we find greatest concern over this protection of institutions instead of individuals. Here, for our particular emphasis on the educational attainment and equitable outcomes of low-income and otherwise disadvantaged students, for whom education functions more explicitly as a form of welfare than for high-income students, student borrowing may be especially ill-suited.

To show how the student loan program is hindering the ability of education to fulfill its role as an equalizer, we pull together a growing body of research that suggests student loans, large and small, can have negative effects on far too many potential students’ college preparation, the decision to enroll in college, which college to select, whether to stay and complete college, which job to take after college, whether and when to marry, when to have kids, the amount of overall financial stress experienced, whether to buy a home, and whether, when, and how much to save for retirement. We acknowledge that, as with all secondary data analysis, there are no ‘perfect’ studies; however, this evidence on a variety of outcomes, from different researchers utilizing a range of methods and datasets, at a minimum, points to the need for a distinct and fuller assessment of the U.S. student loan system, including its potential role in contributing to Americans’ perceptions that their greatest hopes are increasingly elusive. Reviewing the growing body of research makes a compelling case on its own that the student loan program exacerbates uneven returns on a college degree and erodes, then, some of the equalizing potential of our higher education system.

We recognize, within the context of today’s financial aid debate, that some may view these student loan effects as small costs to pay for the right to receive an education. Indeed, some Americans may choose to delay buying a home or getting married, and generational differences may lead some to make different life choices altogether (Nielsen, 2014). Our intention here is simply to point out the unacceptable inequity of a system that asks some, but not all, students to pay these costs, and frames such inequity as an inevitable price of higher education access. We believe that the American Dream requires that personal preferences and life goals must determine individuals’ paths, not the constraints leveled by the way in which they financed the higher education they pursued on their journey. This leads

to different conclusions about the seriousness of student loan effects and, then, the urgency of constructing alternatives. For example, Rose (2014) states, “A sizable number of people are certainly *inconvenienced* for their first 10 years after graduation and face a long period of repayments, but a relatively small percentage confront default” (p. 30, emphasis added). We would and have agreed with Dr. Rose that it still pays off to attend college, even if you have to take out student loans. However, this certainly does not mitigate the harsh reality that college pays off *more* for those who do not have to take out loans. It is that inequity that is problematic. And the disparity in outcomes is often quite consequential. The average time that it takes to repay student loans grew from about seven years in 1992 to a little more than 13 years in 2010 (Akers & Chingos, 2014), and this is likely to continue to grow as Income-Based Repayment plans grow in popularity (Akers & Chingos, 2014), touted as a way for overburdened students to cope with the strain of their debt burdens. These programs, which have doubled in use over the last two years, extend normal repayment plans from 10 years to up to 25 years. In light of evidence of the long-term financial implications of diverting income to debt repayment instead of asset accumulation, payment schedules that extend the period of indebtedness may only exacerbate the divides. Even if the advantage realized by a student who does not have to borrow for higher education is small, and even if the student who had to take out loans is better off than he or she would be without a college education, this just seems at odds with the goal of education being an equalizer in society. Even more fundamentally, this landscape is incompatible with the spirit of the American Dream that promises that effort and ability will determine who succeeds and fails in life. It is particularly disturbing as a proposed ‘solution’ to the growing public angst about student loans’ effects on the economic mobility and financial security of young Americans, failing as it does to address the underlying causes of their distress.

Particularly out of sync with the stated and understood purpose of student loans to facilitate greater access to higher education, though, are the ways in which borrowing influences students’ decisions prior to college entrance, again in highly unequal ways. Apart from the fact that the mere thought of having to finance college through the student loan program is associated with some students opting not to attend college—debt aversion—the student loan program helps to institutionalize separate educational paths for those who have money for college and those who do not. For instance, field evidence suggests that students facing the prospect of considerable debt may be steered toward two-year colleges as opposed to a four-year college by high school personnel such as teachers and counselors, even when they are academically qualified to attend more selective institutions (Elliott, 2013). One high school counselor put it this way,

Being able to see it made a big difference because I had students that were accepted into 4-year colleges around the state but once we looked at the aid packages, they realized, OK, it doesn’t make sense for me to go down to [4-year college] and take out some loans when I can get money back if I start at [2-year college] and just get my associate’s and then transfer so that, they have to see it, they have to be able to touch it. And I’m the same way, like you can talk to me all day but until I see the numbers, it’s not really going to click with me. (Elliott, 2013, p. 19)

This idea that students who cannot afford to pay for college or cannot afford to take out loans should attend two-year colleges even when qualified to attend more selective colleges helps create the expectation that there are different paths for students with and without money to pay for college. And, yet, today’s conversation about higher education and, specifically, financial aid, is dominated by this thinking. In justifying the student loan program as not diminishing the return on college, researchers have expressed a similar rationale as the counselor, for example,

Nonetheless, for many borrowers even modest student debt crowds out other spending. But our postsecondary system is huge and provides many options. Students can minimize debt by going to a less-expensive public four-year college or by starting at a community college and then transferring to a state four-year school. (Rose, 2014, p. 30)

This idea that to avoid debt students should have to make a decision to attend two-year colleges is also reflected in state and national policy. For instance, the Tennessee Promise offers last-dollar scholarships to ensure free two-year degrees or certificates from the state’s 13 community colleges and 27 technical schools. While we recognize the good intentions in these policy prescriptions, serving as they do to attempt to preserve routes to college completion for students facing significant cost burdens, this approach runs counter to education acting as an equalizer, particularly given evidence of unequal outcomes and returns on degree at different types of institutions. We

acknowledge that for a two-year college is the best option for some students, and the value of these institutions in the U.S. higher education system is clear, but the student loan program should not be part of why students have to decide to attend a two-year college or a four-year college, nor should financial aid options determine how educators advise students. This is an artifact of the overreliance on student debt and a distortion of how Americans believe higher education to work. We do not ask this of students who have the financial resources to attend college. Potential students from upper-income families are much more likely to walk into a pattern of higher education, such that they may never consciously and intentionally ‘decide’ to attend college. For them, higher education still largely serves as an institution that supports the realization of their American Dream, which makes it even more imperative that we find policy levers capable of strengthening this same promise for less advantaged children.

It is because of the role that education has been given as part of our welfare system that education has become America’s largest investment in ensuring equitable outcomes for all Americans. The stakes are high for properly financing and administering higher education, given its outsized function in our economy and our collective identity. Therefore, financial aid is not just a matter of providing students with the money they need to pay for college. We must assess whether or not these finances align with education’s role as an important facilitator of the American Dream. Then, we must muster the political will to build a financial aid system up to this task.

OVERVIEW

In the first part of chapter one, we assert that the real concern should be about outcomes, equity, and the way in which policy is marching towards overreliance on student loans without much consideration of the effects, profound, troubling, and long-lasting though they may be. Often, efforts to raise concerns about the performance of student loans according to these other measures raises quick defense of student borrowing as a vehicle—often, the only available one—for college access. Here, then, we examine evidence that suggests that the student loan program may complicate the subjective calculation that post-secondary education pays off for students. Our point is not to debate that higher education is almost always a ‘good’ investment for American students, even when a student has to take out loans to finance it. Comparing the outcomes of less-educated adults to those of college graduates reveals that it clearly is. The question is whether students understand this, what might interfere with this assessment and its influence on their decisions, and how this process might lead to different actions for lower-income students, as compared to their higher-income counterparts, including in ways that may inhibit loans’ potential stimulus of college access. Potential students from upper-income families are much more likely to walk into a pattern of higher education, such that they may never consciously and intentionally ‘decide’ to attend post-secondary institutions; for them, then, this subjective calculation is far less determinant of ultimate outcomes than for the lower-income children whose opportunity costs may loom much larger and whose pro-education cues may be interrupted by other forces. Chapter one goes on to discuss evidence on the long-term costs of borrowing as significant determinants of later well-being and, then, important considerations in evaluating loans’ true individual and societal implications. Reviewing the growing body of literature makes it clear to us that the student loan program exacerbates uneven returns on a college degree and erodes, then, some of the equalizing potential of our higher education system.

In chapter two we posit that over-reliance on the student loan program is weakening the ability of the education path to act as the great ‘equalizer’ it is meant to be. Instead of dedicating our policy attentions to solving the problems created, exacerbated, or hastened by student loan reliance, we have mostly moved the goalposts, no longer expecting student loans to be a pillar of educational opportunity and equity. Policies respond to the angst that results from damage leveled by the status quo—by delaying requirements for debt repayment, suggesting different educational paths to reduce costs, and advising students to become more educated consumers—but without striking at the roots of the problem. When confronted by evidence of the potential harms—educational, economic, social—wrought by existing debt levels, we attempt to soothe with temporary and partial ‘fixes’ and console ourselves with the notion that most “students will eventually recover.” We contend that the impetus for these well-intentioned but ultimately short-sighted approaches stems in part from an incorrect and incomplete preoccupation with debt levels—for individual students and in the aggregate—as *the* indicator, an emphasis which may potentially confuse the debate.

However, at this point in the policy discussion of U.S. financial aid, it is not enough to merely point out limitations and drawbacks to student loans. Their prominent place within the policy landscape makes the hole that would be created by their absence loom too large, such that many struggle to even imagine alternatives. In pursuit of superior

outcomes and in the belief that we need a new direction for our financial aid system, in the final chapter of the report we present asset-based, rather than debt-dependent, financial aid, embodied in Children's Savings Accounts (CSAs) such an alternative, capable of restoring higher education as a equalizing force and catalyst of a reinvigorated American Dream.

CHAPTER 1. EVEN IF WE SAY IT AIN'T SO, AMERICA HAS A STUDENT DEBT PROBLEM

While we take some issue with the way that the current student debt debate is framed, we concur with the prevailing sentiment that student debtors' balance sheets are problematic. We also agree that the evolution of student borrowing as the central financial aid institution in U.S. higher education has not occurred in a vacuum, and that sustainable and effective solutions will require policy reforms throughout the post-secondary education landscape. This must begin with an acknowledgement of the cost shifting from public to private responsibility for higher education (Hiltonsmith, 2013) and the difficulty that American households face in trying to fill this breach. At the same time, we seek to account for the significant U.S. public investment in student loans, recapture of which would open new possibilities for policy alternatives. Placed against the backdrop of rising college costs and increasingly uncertain economic futures, student loans must be assessed not only at the point of enrollment, but also for their effects prior to, during, and following higher education. Here, we connect the dots from a growing body of evidence, all of which lead to a conclusion that calls into question the wisdom, equity, and viability of our loan dependence. In the aggregate, this body of evidence suggests that student loans are simultaneously more and less alarming for the future of the United States than commonly believed. While student debt may not incite the next financial collapse and while most individual student borrowers do not rack up debt in the six figures, the long-term and cumulative effects of these derailed asset aspirations may constrain economic mobility and threaten the financial security of student borrowers throughout their lives, and *these* effects could transmit significant, albeit indirect, economic fallout from student loans.

- Some figures about debt incidence and degree are fairly well-known. While low-income students continue to face the greatest obstacles to financing post-secondary education, today student debt is a problem for many students. Fry (2012) found that 40 percent of all households headed by individuals younger than 35 years of age have outstanding student debt. Further, the proportion of undergraduate students who took out federal loans increased from 23 percent in 2001–02 to 35 percent in 2011–12 (College Board, 2012). Students are borrowing more, too. Debt loads increased by \$4,700 (19 percent) between 2007-08 and 2011-2012 for bachelor's degree recipients and by \$3,100 (23 percent) for associate's degree holders (Miller, 2014).
- This growth in indebtedness has not occurred in a vacuum, of course. As post-secondary education costs have shifted to students and families, student loans have moved center stage, taking on a prominence within institutions and household finances likely never imagined by their architects.
- Viewing America's student debt problem using only an accounting lens largely obscures the most significant issues, including the extent to which student loans may undercut higher education's role as a catalyst of economic mobility and greater equity. Changing the metrics by which we assess the performance of the student loan system reveals the multiple levels on which U.S. taxpayers, students, and institutions are not getting our money's worth from student loans. A financial aid program that in 2011-2012 school year cost Americans \$70.8 billion (College Board, 2012) should be held to a higher standard, expected to be an equalizing force with regard to educational attainment and financial wellbeing.
- Prior to college, student loans can deter enrollment, particularly for vulnerable students averse to loans, susceptible to steering away from the best-performing institutions, and struggling to understand a complicated return-on-investment calculation. Critically, these potential effects are more salient for lower-income students, as upper-income students are much more likely to walk into a pattern of higher education, such that they may never consciously and intentionally 'decide' to attend college.
- Even if disadvantaged students are not deterred from enrolling by the prospect of large debts, they may not realize the same return on their investments, given their relatively greater risk exposure, particularly in today's post-Great Recession economy. Between 2000 and 2010 the unemployment rate for White workers with a college degree increased from 1.8 percent to 4.9 percent, but for Black college graduates it increased from 2.8 percent to 9.8 percent (Mishel, Bivens, Gould, & Shierholz, 2013).

- Student debt can have corrosive effects on outcomes during college, too, particularly related to persistence. Student loans' failure to produce greater graduation rates is especially concerning, given the extent to which these college completion measures reflect some of our greatest educational policy challenges today.
- After leaving college, the experience of having had to borrow in order to finance higher education has real effects on former borrowers. Student debt may influence career (particularly, steering students away from public interest occupations that often pay less) and social choices (including when to marry). Student borrowers experience greater financial stress, accompanied and no doubt fueled at least in part by rising delinquency and default rates. Cunningham and Kienzl (2011) find that 26 percent of borrowers who began repayment in 2005 were delinquent on their loans at some point but did not default. By 2012, Brown, Haughwout, Lee, Scally, and van der Klaauw (2014) report that just over 30 percent of borrowers who began repayment were delinquent at some point. And some of the practices utilized by borrowers and lenders (including deferment and forbearance, which both delay but do not avoid the costs of repayment) to cope with repayment difficulties may have the perverse effect of deepening loans' negative implications for student borrowers.
- While student borrowers may have reduced access to credit, given their heavy leverage, the greater effects—on individuals and on the macro economy—are in the area of asset accumulation, including homeownership and retirement savings. For example, Elliott and Nam (2013) find that families with college debt may have 63 percent less net worth than those without outstanding student debt. Similarly, over the life course, Hiltonsmith (2013) finds that an average student debt load (\$53,000) for a dual-headed household with bachelors' degrees from four-year universities leads to a wealth loss of nearly \$208,000. Fry (2014) also finds that a household headed by a college graduate without outstanding student debt has seven times (\$64,700) the typical net worth of a household headed by a college graduate who has outstanding student debt (\$8,700). Perhaps explaining these gaps, Stone, Van Horn, and Zukin (2012) find that 40 percent of students graduating from a four-year college with outstanding student loan debt delay a major purchase, including a home.
- While our primary concerns are with the role of student loans in potentially eroding higher education's potential as an equalizing force in U.S. society and economy, this growing body of evidence suggests that individuals and institutions from nearly all quarters have a stake in this debate. At the risk of sounding hyperbolic, we believe that how we seize this policy window of opportunity may help to determine the future course of our nation.

CHAPTER 2. CUTTING OUR LOSSES TO BUILD A BETTER FUTURE: REPLACING STUDENT LOANS WITH CHILDREN'S SAVINGS ACCOUNTS FOR A MORE EQUITABLE, EFFICIENT, AND EFFECTIVE FINANCIAL AID SYSTEM

Evaluation of student loans' role within the U.S. financial aid system and assessment of their contributions to the economic mobility, financial security, and lifetime prosperity—or, in many cases, lack thereof—of Americans today must begin with a fuller accounting of the dimensions on which their effects are felt. Looking at today's policy debate reveals the need for a broader lens on questions involving student borrowing, which tend to center today relatively narrowly around individual and aggregate loan amounts and repayment burdens and associated defaults. This conversation is difficult, calling into question as it does the assumptions that have informed financial aid policy over decades and critiquing a system that helped to finance the educations of millions of Americans, including many of those today driving the debate. We begin, then, with an acknowledgement of these challenges and an attempt to ensure that, at the least, we begin with a common frame of reference, clarity about the measures on which we base our evaluations, and a vision of a possible alternative—asset-based financial aid.

- Here, our analysis goes beyond critiquing only 'over-reliance' on student borrowing. Instead, we question whether there is still a legitimate government stake in student loans, particularly given our primary concern with the educational and later life outcomes of disadvantaged students—especially, low-income students and students of color. For these students, we assert that the centrality of debt as a financing mechanism is particularly indefensible.
- Reinforcing the need for metrics beyond absolute debt levels, evidence suggests that there may be no 'safe' level of student debt (Akers, 2014). Student loans have negative effects on asset accumulation and subsequent financial well-being at levels even far below 'recommended' thresholds, revealing the limitations of any efforts to protect students by simply trying to avoid huge loans (e.g., Egoian, 2013).

- While student debt and its effects on individuals and the larger economy are clearly very salient political topics today, examining student loans through an equity lens exposes more clearly the inadequacy of current policy responses. Indeed, some of these reforms, well-intended though they no doubt are, may only extend loans' negative effects, increasing inequality. To restore the equalizing function of post-secondary education, U.S. policy must reduce absolute borrowing, rather than 'tweak' outcomes through initiatives such as income-based repayment. Here, again, looking specifically at disadvantaged students prompts concern with other approaches, such as funneling students to two-year institutions, which may exacerbate inequality, since wealthier students' college decisions are not so constrained.
- In sharp and disturbing contrast to their stated aims, there is no evidence that student loans support educational outcomes, particularly for low-income students, whose aspirations may even be deterred by the prospect of high-dollar debt. Despite concerns, many still cling to student borrowing as an essential component of the financial aid landscape. This hesitation is understandable given the history and current dominance of student loans within the financial aid landscape. However, only acknowledging the failures of this system will create the space for alternatives that promise superior potential outcomes.
- Asset-based financial aid provides a way to restore the equalizing role of higher education, particularly if combined with reparations for those already harmed by student debt—debt forgiveness for those still in repayment, and asset investments for those who have discharged their debt. While significant positive educational outcome effects may be realized with low levels of asset accumulation, to ensure that Children's Savings Accounts (CSAs) or other asset vehicles could be viable alternatives to the student loan system, these accounts would need to be adequately capitalized, with public transfers complementing family deposits. CSAs are not very expensive, though, particularly when compared to sizeable government expenditures for student loans, and could be funded through repurposing of Pell Grant dollars and capturing revenues currently lost in poorly-targeted education tax credits, in addition to the savings realized through pivoting away from student loans.

CHAPTER 3. FROM INDEBTEDNESS TO ASSET BUILDING: CHILDREN'S SAVINGS ACCOUNTS AS AN ALTERNATIVE TO STUDENT LOANS

At this point, we believe that policy inertia around student loans may stem as much from difficulty imagining alternatives as from real satisfaction with the status quo. Similar, then, to the U.S. debate on health care reform, proposal of new approaches may help to unmoor entrenched interests, particularly to the extent to which these innovations may be revealed to promise not only improvement but, indeed, entirely new directions. This is perhaps our most valuable contribution to this student loan debate, to which we are admittedly new and somewhat peripheral. Our evidence of the potential for educational and financial effects of assets may catalyze new conversations, investments, and opportunities, including, we hope, a convergence of the parallel momentum of rising debt and growing interest in children's savings, streams that offer the greatest promise for young Americans' lives only when they come together.

- Children's Savings Accounts (CSAs) represent more than just a tool for paying for post-secondary education. Evidence—including from a randomized controlled trial, as well as rigorous secondary data analysis—reveals assets' potential for improved outcomes before, during, and after college, particularly when contrasted with reliance on student borrowing. For example, Elliott, Song, & Nam (2013) find that 45 percent of students from low- and moderate-income families with no savings accounts enroll in college. That compares to 65 percent with school savings from \$1 to \$499 and 72 percent of students with school savings of over \$500. Research suggests that these effects likely occur largely through reinforcing a college-bound identity that increases student engagement and builds parents' expectations of higher education throughout a student's academic career (see, Assets and Education Initiative, 2013). In contrast to high-dollar student loans, which show some negative effects on college graduation, college savings may improve a student's chances of persisting through graduation. The results are encouraging, if not yet definitive: five percent of low- and moderate-income (below \$50,000) students with no account and 33 percent of students who have school savings of \$500 or more graduate from college (Elliott, Song, & Nam, 2013).
- In addition to the positive financial effects of reducing dependence on student loans (Elliott, Lewis, Nam, & Grinstein-Weiss, 2014), children who have savings accounts while they are young may be more likely to own

savings accounts as young adults, have more diversified asset holdings, and accumulate higher net worth (Friedline & Elliott, 2013).

- Given the potential connection between initial asset levels and the subsequent ability for income to generate more assets and additional income (Elliott & Lewis, 2014), young adults who leave college with at least some asset ownership may initiate a trajectory of superior earning and asset accumulation.
- These findings have helped to fuel interest in CSAs around the country, with localities, state 529 programs, and others implementing CSAs with varying designs. Families are saving in these accounts, but, if they are going to truly be effective tools for helping low-income and minority students reduce the need for student loans, creative ways for resourcing these accounts are needed. This could include repurposing the Pell Grant to leverage early commitment effects, as well as the savings to be realized through the transition away from student borrowing.

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