The College Board
National Dialogue On Student Financial Aid

Research Report 5

PATHWAYS TO COLLEGE NETWORK

January 2003

The Role of Student Loans in College Access

Sandy Baum, Ph.D., Professor of Economics, Skidmore College

Most discussions of student loans focus on the difficulties they generate for students. The necessity of relying on loans may discourage some qualified high school graduates, particularly those from low-income and underrepresented backgrounds, from participating in postsecondary education; the portion of student aid funds that takes the form of loans has increased dramatically over the years; students are accumulating high levels of debt that could have a serious impact on their postcollege options, including deterring them from entering socially beneficial but low-paying occupations; too many students are unable to repay their loans and end up in default. All of these concerns are valid and should be addressed by public policy. However, it is also true that student loans play a vital role in increasing access to educational opportunities for students from all backgrounds. Borrowing to pay for education is a sound decision for most students, and student loans are a vital part of college financing policy, increasing both the equity and the efficiency of the student aid system.

Increasing Reliance on Loans

Loans, which constituted 47 percent of student aid funds a decade ago, rose to 61 percent by 1996-97. The introduction of federal education tax credits into the mix has decreased the relative role of loans, which constitute 54 percent of the aid students now receive (College Board, 2002). More students are borrowing, and they are, on average, accumulating significantly larger educational debts than they were even a few years ago. As reported in Table 1, data from the National Postsecondary Student Aid Survey indicate that the average debt of graduating seniors who borrowed at four-year institutions increased from $11,800 in 1995-96 to $16,900 in 1999–2000, an increase of about 30 percent in inflation-adjusted dollars (National Center for Education Statistics, 1998, 2002).

Table 1

Growth in Average Debt Levels: Graduating Seniors at Four-Year Colleges and Universities

	1995-96	1999–2000
% who have borrowed	52%	62%
Average debt	$11,800	$16,900

Source: National Center for Education Statistics, *Student Financing of Undergraduate Education, 1999–2000; 1995-96.*

It is important to note, however, that a considerable amount of the increase in borrowing results from the introduction in 1993 of the unsubsidized Stafford Loan program. The number of borrowers has increased much more rapidly than the size of individual loans. This growth is fueled by the availability of loans to students without documented need, many of whom are likely using these loans to replace parent contributions from income, assets, or other borrowing sources. (See Table 2.)

The availability of loans to all students regardless of need clouds the role loans are playing in the financing of education for low-income students. Middle- and upper-income students who rely on student loans because of choices they or their families make are in a situation very different from that of low-income students, who face much more limited choices and are more likely to find their opportunities significantly restricted by the need to borrow.

Table 2

Growth in Loans: 1993-94 to 2001-02

	# of borrowers	Average loan	Average loan (constant 2002 $)
Stafford sub.	31.3%	+9.7%	-9.7%
Stafford unsub.	421.8%	+51.6%	+24.8%
Total Stafford	91.6%	29.0%	+6.2%
PLUS	+84.1%	+68.1%	+38.5%

Source: The College Board, *Trends in Student Aid, 2002*

Among low-income students, it is important to distinguish between those who are independent and those whose ability-to-pay is linked to family income. Independent low-income students are significantly more dependent on debt financing than are more traditional students. In 1995-96, loans constituted 47 percent of the total aid for independent low-income full-time undergraduates, compared to 28 percent for dependent low-income full-time undergraduates (Choy, 2000). Among low-income independent students, only 40 percent were able to obtain all of their federal loans under the subsidized Stafford program, whereas 80 percent of dependent undergraduates were eligible for enough subsidized loans to be able to avoid unsubsidized borrowing (Berkner, 2002). On one hand, this is good news. Truly low-income students are most easily identified by parental income, whereas some independent students may have low levels of personal income, despite the fact that they come from non-poor families. On the other hand, as the average age of college students increases and more students are relying on their own resources to finance education, manageable financing strategies for independent students are increasingly important.

Alternative Financing Strategies

Given the limited availability of grant aid, students whose families are not in a position to finance their educations are forced to choose among alternatives, all of which involve considerable amounts of sacrifice and compromise. The only way to diminish their reliance on loans is to enroll less than full-time and/or to work long hours while in school. A recent report from the American Council on Education suggests resistance to borrowing has a cost. Table 3 summarizes these findings. Among students who began college in 1995, 32 percent had dropped out without earning a degree three years later. While these data do not provide evidence about the reasons why students do or do not complete degrees, those who had enrolled less than full-time full-year were particularly unlikely to persist, with 48 percent in this category dropping out. While students who worked between 1 and 14 hours per week were less likely than those who did not work at all to drop out, working longer hours was negatively associated with persistence; 53 percent of those working 35 or more hours per week dropped out.

In contrast to the association between enrolling part-time and working long hours to ease college financing, borrowing is associated with staying in school. Only 25 percent of those who borrowed dropped out, compared to 35 percent of nonborrowers. Least likely to drop out were students who borrowed and worked less than 15 hours per week. It is possible that personal characteristics that make students less likely to borrow also make them less likely to persist. However, these findings certainly do not support the idea that the accumulation of student debt poses a bigger risk to degree completion than alternative financing strategies.

Even students who are willing to borrow are often forced to seek alternatives because of the current limits imposed on Stafford loan borrowing. While precise data are difficult to obtain, it is clear that students are turning to sources of credit that carry significantly higher interest rates than federal loans. Too many students use credit cards

Table 3
Borrowing, Working, Enrollment Patterns, and Persistence: Students Entering in 1995

	No degree, not enrolled in 1998	Still enrolled in 1998	Attained AA degree or certificate by 1998
All students	32%	57%	11%
Attendance pattern			
Full-time/full-year	16%	75%	9%
Other	48%	39%	13%
Borrowed federal student loan			
No	35%	55%	10%
Yes	25%	61%	14%
Hours worked per week while enrolled			
None	27%	59%	14%
1–14	16%	78%	6%
15–34	31%	58%	11%
35 or more	53%	35%	12%
Working and borrowing status			
Borrowed, did not work	26%	59%	15%
Borrowed, worked 1–14 hrs.	11%	84%	4%
Borrowed, worked 15+ hrs.	28%	55%	17%
Did not borrow or work	27%	59%	14%
Did not borrow, `worked 1–14 hrs.	21%	73%	5%
Did not borrow, worked 5+ hrs.	42%	49%	9%

Source: Jacqueline King, *Crucial Choices: How Students' Financial Decisions Affect their Academic Success*, American Council on Education, 2002.

Table 4

Credit Cards for Tuition and Fees

	Percent who charge TF	Of those who charge TF, percent who carry balance
Traditional	14%	40%
Nontraditional	25%	52%
Dependent	15%	37%
Independent	27%	50%
Full-time	15%	40%
Part-time	38%	50%
Four-year	15%	43%
Two-year	21%	50%

Source: TERI and Institute for Higher Education Policy, “Credit Risk or Credit Worthy?” 1998

to cover some of their tuition and fees. (see Table 4) Nontraditional students are most likely to fall into this category, with independent students, those attending part-time, and those enrolled in two-year institutions most likely to use this high-cost source of funds (Teri, 1998).

Is Borrowing Excessive?

Concern about levels of borrowing that will cause serious problems for students is certainly appropriate. There is, however, no evidence to date that typical student debt levels are unmanageable. A 1998 study (see Table 5) of student borrowers in repayment found that with average total debt of about $19,000 ($11,000 of undergraduate debt, on average) and monthly payments averaging close to $200, half of the respondents said they felt burdened by their loan payments, but two-thirds said that the availability of loans was very important in allowing them to continue their education after high school and that the payments were worth the benefits. Fewer than 20 percent said that they had altered their career plans because of student debt. Moreover, there was no evidence that debt levels measurably affected other major lifestyle options, such as home ownership and marriage (Baum and Saunders, 1998).

Comparison of the repayment experiences of Pell recipients to non-Pell recipients in this study revealed that the Pell recipients had somewhat higher average debt levels than other students, as well as lower postgraduation

Table 5

Pell Recipients (low-income students) Debt and Attitudes versus non-Pell Recipients

	Pell Recipient	No Pell
	(37%)	(64%)
	(n=404)	(n=694)
Average total debt	$17,900	$19,300
Average undergraduate debt	$12,400	$10,900**
Average monthly payment/ current income	12.6%	11.7%
Current income	$25,500	$27,700**
	Pell	**No Pell**
Loans extremely or very important for continuing education after high school	82%	72% **
Extremely or very burdened by loan payments	52%	49%
Agree payments unpleasant but benefits worth it	66%	66%
Continued education beyond undergraduate degree	28%	40%
Undergraduate debt important factor in preventing grad. school attendance	50%	38%
Significantly changed career plans due to student loan debt (% who agreed) [Not statistically significant difference]	19%	15%
Knew how much debt they were accumulating	57%	61%
	Pell	**No Pell**
Total debt/current income > 100%	25%	26%
Monthly payment/income >15%	21%	19%
Undergraduate debt/current income > 100%	19%	16% *
Undergraduate debt > $20,000	16%	12% **
Graduate degree	20%	30% **

* Difference significant at the .10 level ** Difference significant at the .05 level

incomes. Despite having to devote a slightly higher percentage of their monthly incomes to debt repayment, Pell recipients did not feel more burdened by loan repayment and were as likely as others to feel that the benefits were worth the cost of repayment. They were, however, significantly more likely than others to report that loans had been very important in providing access to college. Although not conclusive, there was some evidence suggesting that African American and Hispanic borrowers were more likely than others to feel burdened by their loans and to report that they modified their career plans because of student debt (Baum and Saunders, 1998).

Conclusions

Any student would prefer to receive grant aid, rather than have to borrow to finance college education. For some potential students, particularly those from low-income and underrepresented groups, the prospect of borrowing likely discourages enrollment. More adequate grant funding is clearly necessary for those students whose decision about enrolling and persisting in postsecondary education is most sensitive to price. The reality that the value of the long-term investment in education makes borrowing a sound financial decision is not sufficient to allow low-income students to overcome the daunting gap between the resources at their disposal and the cost of college.

This problem should not, however, obscure the very important role that borrowing does and should play in increasing access to postsecondary education. People with college degrees earn 80–90 percent more than those with only a high school education (U.S. Census Bureau, 2001, Table 18). In addition to the other personal benefits from higher education, the earnings premium is, for most people, more than enough to pay back significant amounts of education debt while still enjoying a measurably higher standard of living than would be available without a college education.

Moreover, however successful advocates for educational opportunity may be in increasing need-based grant aid in the near future, a significant gap will remain that will have to be filled by borrowing. Helping students and their families to understand the benefits of college education and the extent to which education debt is manageable for graduates is a critical part of efforts to increase successful participation in higher education among low-income students. Many students fully intend to borrow $20,000 or more to buy a car when they graduate from college. The $20,000 they borrow to finance college should be viewed as a better investment, not as a greater hardship than consumer debt.

General resistance to student loans is largely misplaced and may serve to restrict access to higher education. That said, some groups of students are particularly vulnerable to debt and some students do, in fact, borrow more than they can reasonably manage to repay. Policy efforts should focus on protecting these students, rather than on imposing general limits on borrowing. More generous limits on borrowing under subsidized federal loan programs would assure that students with financial need have access to loans with the most favorable terms.

In addition to access to adequate loan funds and more generous grant aid for low-income students, a low-income insurance policy that would protect borrowers whose education does not pay off in the labor market would reduce the barriers to educational access created by the growing reliance on loans. Graduates who choose to enter public service and other relatively low-paying occupations of particular social value should benefit from systematic and readily available loan forgiveness provisions. Policies might also be designed to reduce the payment obligations of those who are unable to find employment that provides them with a reasonable rate of return to their educational investment.

References

Sandy Baum and Diane Saunders, 1998. *Life After Debt: Results of the National Student Loan Survey.* Braintree, MA: NellieMae.

Lutz Berkner, et al. (2002). “Student Financing of Undergraduate Education: 1999–2000.” NCES 2002-167. Washington: National Center for Education Statistics.

Susan Choy (2000). Low-Income Income Students: Who They Are and How They Pay for Their Education. NCES 2000-169. Washington: National Center for Education Statistics.

Jacqueline King (2002). *Crucial Choices: How Students’ Financial Decisions Affect their Academic Success*, American Council on Education.

National Center for Education Statistics, *Student Financing of Undergraduate Education*, 1999-2000; 1995-96

TERI and the Institute for Higher Education Policy (1998). *Credit Risk or Credit Worthy?*

The College Board, *Trends in Student Aid*, 2002.

U.S. Census Bureau (2001). *Statistical Abstract of the United States, 2001*. Washington, DC: U.S. Department of Commerce.