Groups at Risk of Negative Returns to Education Investment

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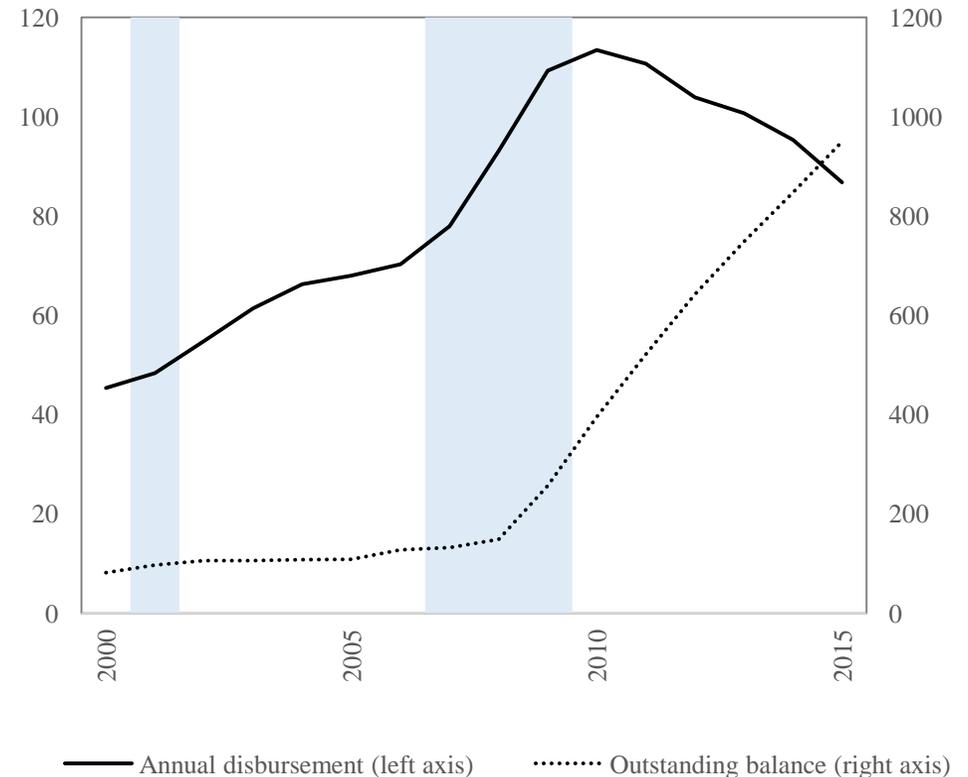# Overview

- Context
- Risk sharing proposals
- Types of risk
- Risk of defaulting

Loan disbursement and outstanding debt

- Two different trends:
  Annual disbursements falling
  Cumulative balances growing

- Outstanding principal, interest, and fees

- About $88b disbursed in FY15:
  50% went to undergrads
  52% disbursed by privates
  70% is unsubsidized

Source: FSA loan portfolio reports and Board of Governors of the Federal Reserve System (US), Federal government; consumer credit, student loans; asset, Level FGCCSAQ027S; https://fred.stlouisfed.org/series/FGCCSAQ027S.

Annual disbursement (left axis) .... Outstanding balance (right axis)

Distribution of student loan debt
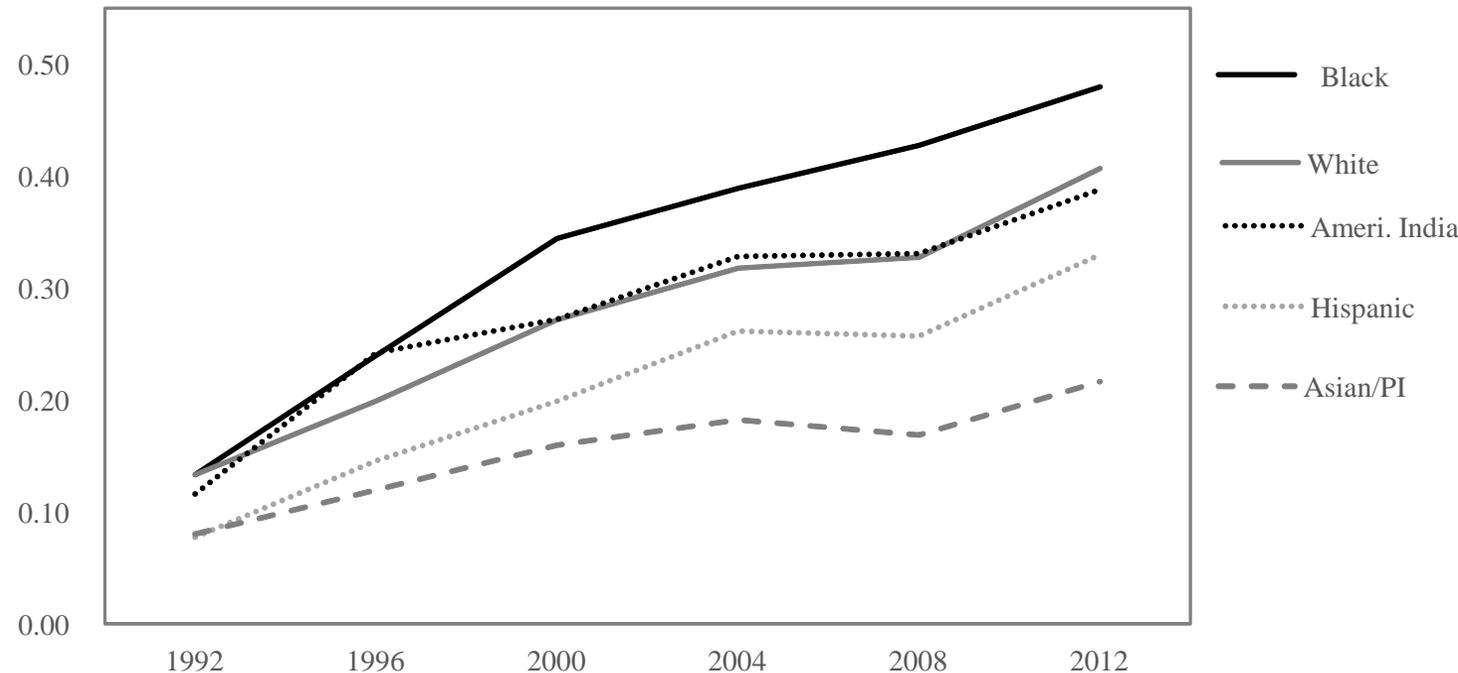
- Loan research focuses on:

  Informational interventions

  Effects on enrollment

  Distribution of debt

- Black students are most likely to borrow, and to borrow more

- Racial gaps are widening

Source: National Postsecondary Student Aid Study (NPSAS) multiple years using T4LNAMT1 excluding PLUS

Federal risk-sharing proposals

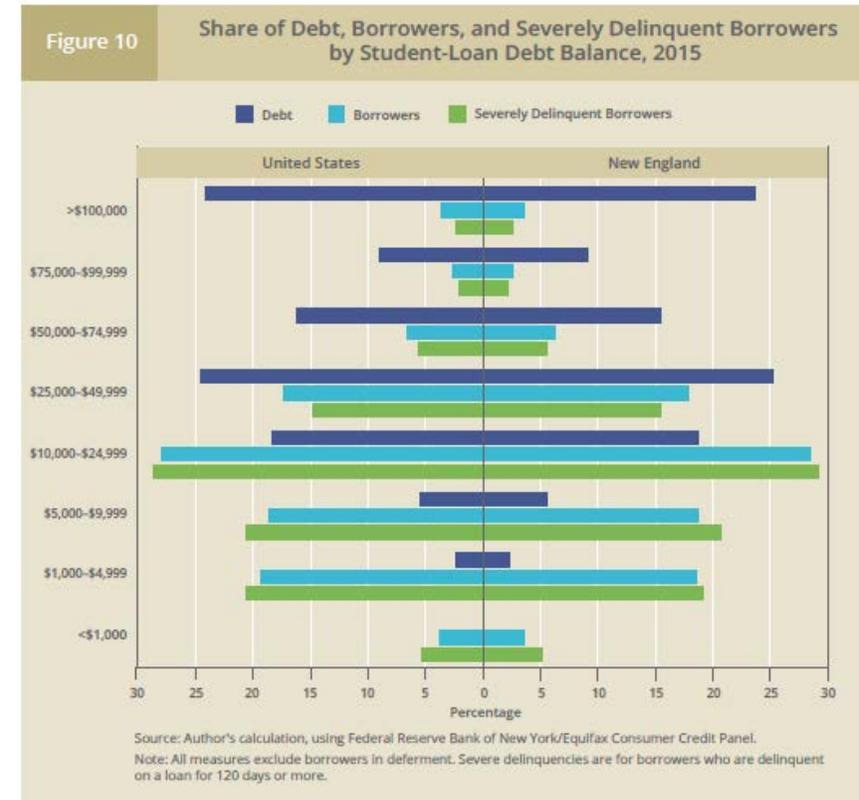|	Reed, Durbin, Warren, & Murphy	Shaheen & Hatch
Risk measure:	Cohort Default Rate	Cohort repayment rate
Penalty thresholds:	15% - 30%	< 45%
Sanctions:	5%-20% of outstanding balance on defaulted loans	20% of non-repayment principal balance
Pell bonus:	Yes	Yes
Perkins & PLUS excluded:	Yes	Yes

Risk sharing precautions:

- CDR gaming (e.g., forbearance)
- Repayment rate by plan (e.g., IDR)
- Number *and volume* in default
- Disbursement vs revenue
- Undergraduate loans only
- How will colleges respond?
- Who enrolls in these colleges?

Two basic types of risk

- Income risk
  - Never enough income to repay debt
  - Long-term economic hardship
  - High debt, but with degree

Source: Federal Reserve Bank of Boston (2016). Student Loan Debt, Delinquency, and Default: A New England Perspective.

Two basic types of risk

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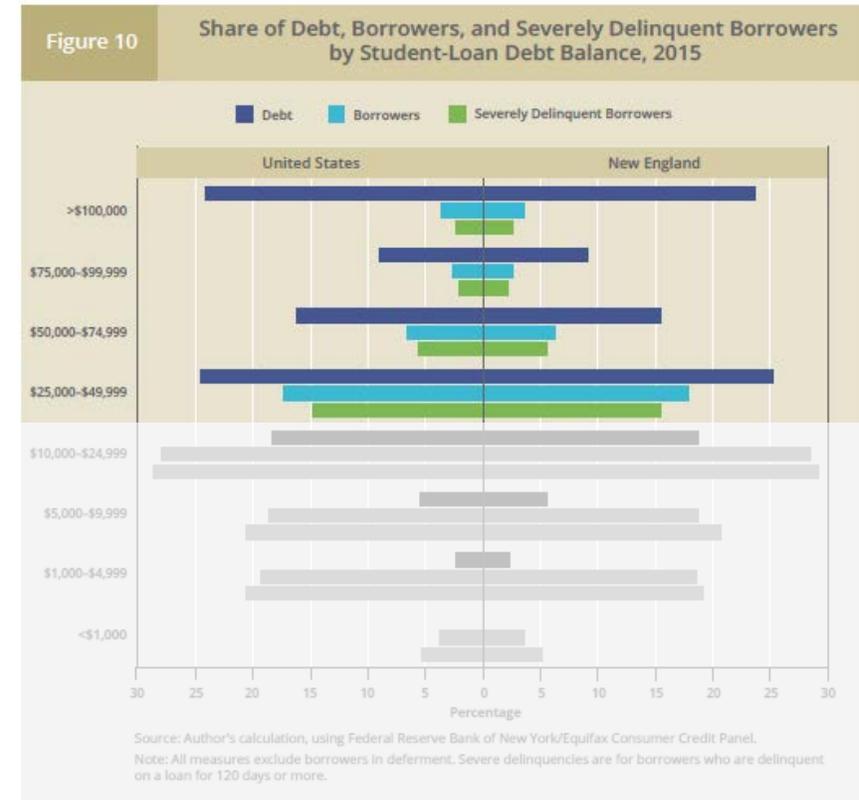 - Long-term economic hardship
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Figure 10 Share of Debt, Borrowers, and Severely Delinquent Borrowers by Student-Loan Debt Balance, 2015

■ Debt ■ Borrowers ■ Severely Delinquent Borrowers

United States — New England

>$100,000
$75,000-$99,999
$50,000-$74,999
$25,000-$49,999
$10,000-$24,999
$5,000-$9,999
$1,000-$4,999
<$1,000

30 25 20 15 10 5 0 5 10 15 20 25 30
Percentage

Source: Author's calculation, using Federal Reserve Bank of New York/Equifax Consumer Credit Panel.
Note: All measures exclude borrowers in deferment. Severe delinquencies are for borrowers who are delinquent on a loan for 120 days or more.

Source: Federal Reserve Bank of Boston (2016). Student Loan Debt, Delinquency, and Default: A New England Perspective.

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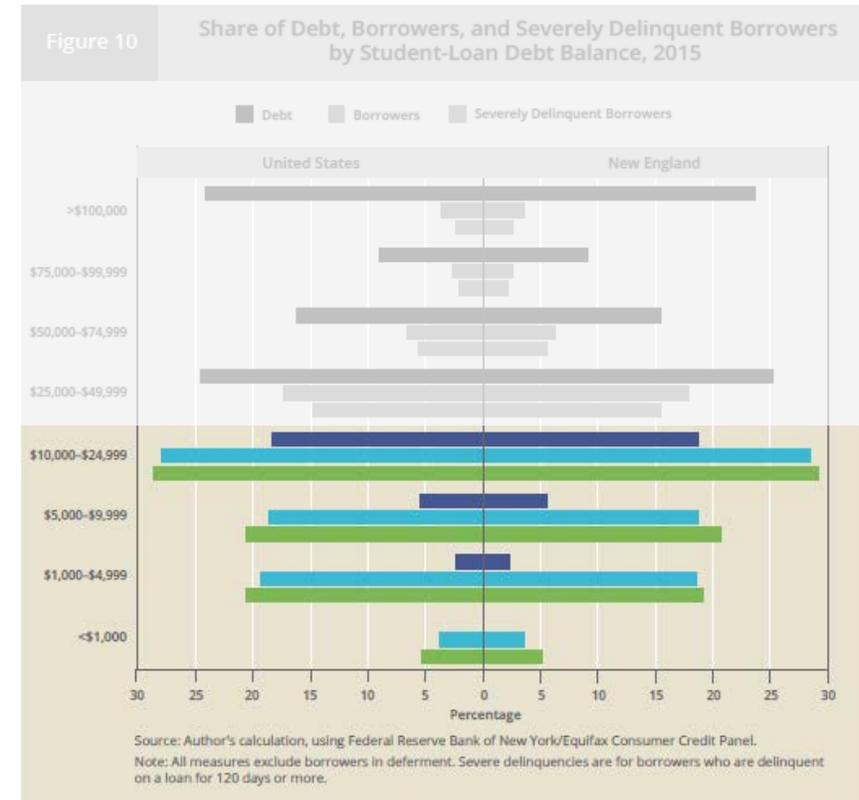 - Long-term economic hardship
  - High debt, but with degree

- Liquidity risk
  - Not enough monthly income to pay bills
  - Temporal economic hardship
  - Low debt, no degree

Source: Federal Reserve Bank of Boston (2016). Student Loan Debt, Delinquency, and Default: A New England Perspective.

Risks of defaulting

1. **Debt and no degree**

2. College choice

3. Lifecycle of debt

4. Navigating complexity

5. Default is not a "pre-existing condition"

Figure 26. Undergraduate Loan Repayment Outcomes at Year 3 by Completion Status, 2011 Repayment Cohort

Note: Years are fiscal years.
Source: Department of Education

Source: White House (2016). Investing in Higher Education.

Risks of defaulting
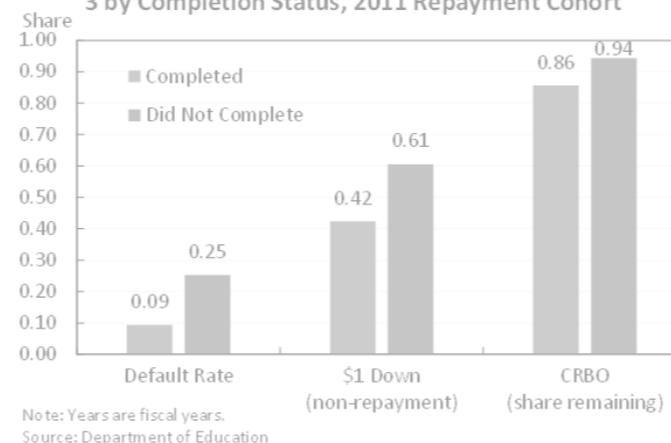
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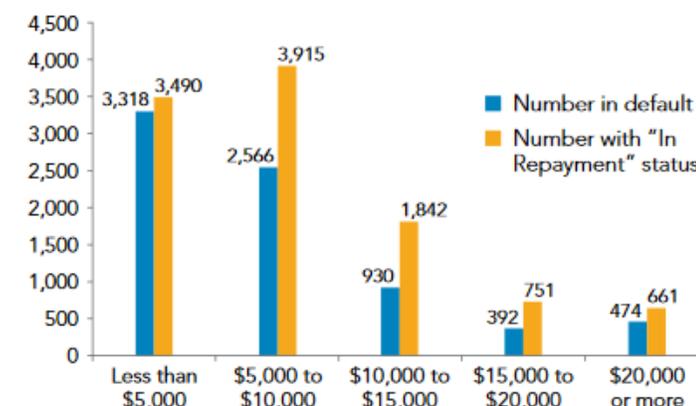
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Figure 26. Undergraduate Loan Repayment Outcomes at Year 3 by Completion Status, 2011 Repayment Cohort

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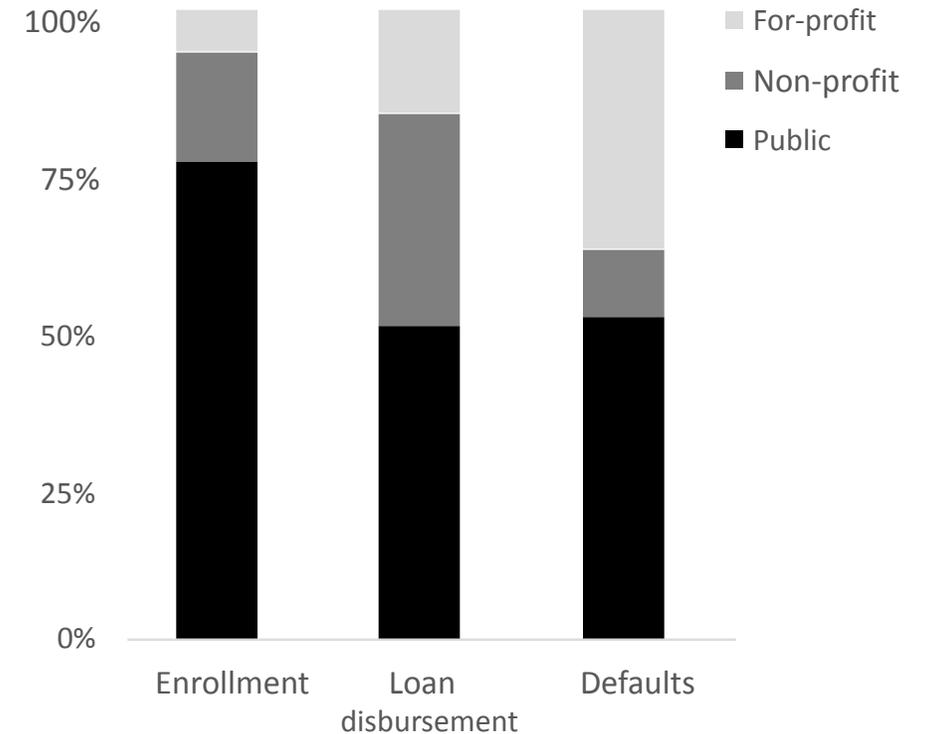Figure 17: FY2011 Borrowers with an "In Repayment" Status Compared to Borrowers with a Defaulted Status

Source: Campbell & Hillman (2015). A Closer Look at the Trillion. American Association of Community College Trustees.

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Source: Author's calculations from College Scorecard and FSA loan portfolio data
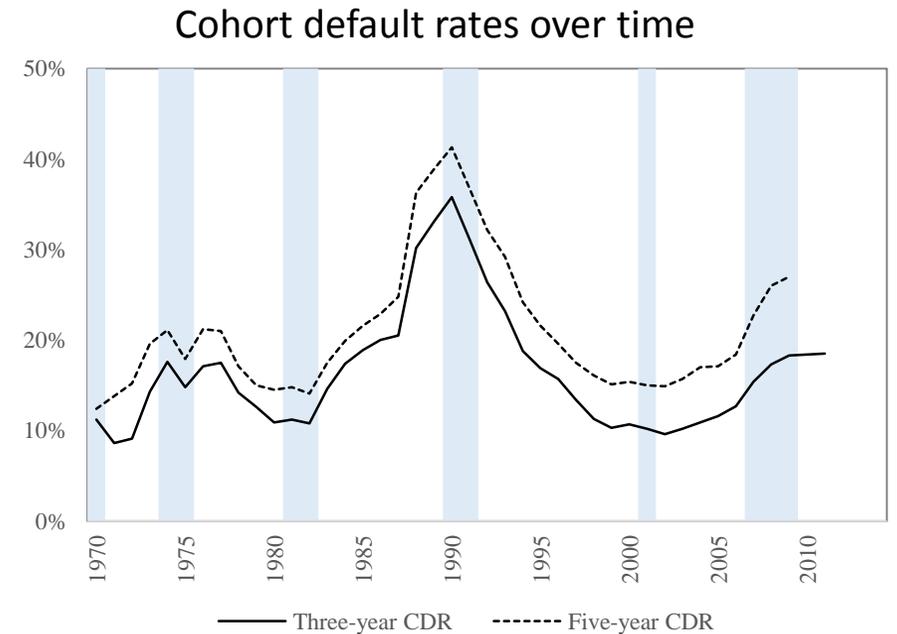
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Cohort default rates over time

Three-year CDR   Five-year CDR

Source: Looney & Yannelis (2015) A Crisis in Student Loans?
Brookings Institution using i_cdr3 and i_cdr5

No Board endorsement of any person or entity

Risks of defaulting

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Figure 24: FY2011 Defaulters, by Number of Payments Made

Payments Made	Number of Defaulters	Percent	Average Debt
No Payment	5,115	66.6%	$7,493
At Least One Payment	2,565	33.4%	$8,191
Total	7,680	100.0%	–

Note: The incidence of payments may be underreported because FFEL servicers are not required to report payment information.

Source: Campbell & Hillman (2015) A Closer Look at the Trillion. American Association of Community College Trustees, Washington, DC.

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Moving forward

To better understand the causes and consequences of default, we should know:

1. Efficacy of financial literacy interventions

2. Efficacy of default management plans

3. Role of servicers in contacting/rehabilitating defaulted loans

4. Role of state authorization and accreditation in consumer protection

5. How borrowers navigate repayment

6. How local economic conditions shape default

7. Lifecycle of repayment relative to earnings