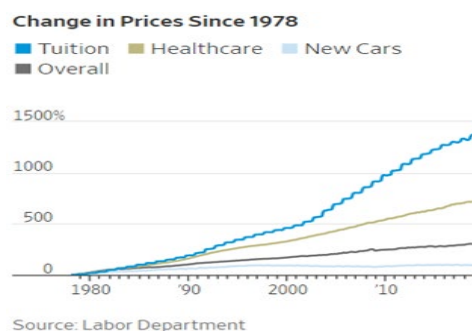


The so-called student debt crisis seems to make headlines routinely, especially as the 2020 election season approaches. The issue is politically polarizing, with far-left candidates like Senator Elizabeth Warren proposing legislation that would forgive student debt and eliminate tuition at public institutions. However, such disruptive proposals are unlikely to pass through Congress. Indeed, college graduates achieve an education that will carry them through the rest of their lives. But, in many instances, they carry a financial burden that lingers for decades.

The fundamental issue is a question of economic value – is the degree a student earns worth the cost (i.e. the student loan) of achieving it? Certain fields of study, such as engineering, medicine or computer science, offer promising salaries that more than likely will cover the cost of achieving a degree. But for other fields of study, such as education and philosophy, the expected income might not sufficiently cover the cost of a loan, which in turn can make the degree quite costly. This economic reality should not preclude students from pursuing their interests. But at a minimum, prospective students should carefully evaluate the financial implications of assuming a college loan.

According to a Wall Street Journal article (The Long Road to the Student Debt Crisis, Josh Mitchell, 2019), borrowers currently owe more than \$1.5 trillion in student loans, or about \$34,000 per person. Furthermore, college tuition has risen 1,375% since 1978, more than four times the rate of inflation, according to the Labor Department (see chart below). Moreover, four in ten recent graduates are in jobs that don't require a degree, according to the New York Federal Reserve. What's worse is that roughly half of enrolled students actually graduate within 8 years. Degree or not, the student loan must still be repaid.



Let's work through the math of a student loan in terms of a cost-benefit analysis. What follows is a simplistic – yet informative – exercise. Assume a prospective college student chooses an institution of higher learning that costs \$20,000 annually (pick any number). A fortunate prospect has the ways and means to pay for the tuition outright. But for most, the tuition must be financed through a loan. Considering a four-year degree, that's \$80,000 in financing. According to credible.com, the average interest rate on an undergraduate loan is roughly 5% annually. Furthermore, the typical loan term is 120 months (i.e. ten years). Let's assume that the monthly loan payment, based on the figures above, is \$700 per month (principal plus interest).

According to the Bureau of Labor Statistics, the median weekly income of a high school graduate with no college degree is \$718, or \$37,336 per year. In comparison, the same statistic for earners with a college degree is \$1,189, or \$61,828 per year. The economic benefit of having a college degree is obvious – reasonably expect to earn roughly 66% more with a bachelor degree. Compound this differential (\$61,828 versus \$37,336) over decades and the cumulative effects are substantial. For example, over a ten-year period, an earner with a college degree makes roughly \$250,000 above the earnings of an earner without a college degree.

On the surface, obtaining a college degree is quite valuable economically. But we must factor in the cost of achieving the degree. To earn, on average, the marginal \$250,000 benefit of a college diploma over ten years, most prospective students must lay out the cost of a student loan. In our example, this debt service equates to \$84,000 over the life of a loan. Pay the debt and ultimately you come out ahead after ten years (i.e. plus \$166,000). The earnings potential after the loan expiration is exponential – a higher than average wage and no student debt.

The reality, however, is that the future earnings of a college graduate is uncertain. In a worse case scenario, a young adult entering the workforce cannot find employment that sufficiently covers the cost of the student loan. In other words, the investment today (i.e. the student loan) does not ultimately pay off. Instead, you are potentially under a debt burden that's not easy to pay off.