


Student Loan Policies: Conceptual bases, comparing alternatives and important design issues



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Outline



- 1 Introduction: Celebration, but design issues remain
- 2 Why have student loans anyway?
- 3 Comparing the two sorts of loan arrangements
- 4 Repayment burdens with “normal” loans and ICL
- 5 The important role of loan design and interest rate subsidies
- 6 Illustrating (hypothetical) interest rate subsidies for NZ
- 7 Research and policy issues for loan reform

2 Why have student loans anyway?



Capital market failure

Due to:

- (a) Uncertainties with graduate incomes
- (b) Lack of collateral for banks
- (c) Need for government intervention

3 Comparing the two sorts of loan arrangements



(A) Government guaranteed bank loans (US, Canada):

- (i) Collected on basis of time
- (ii) Consumption hardship possibilities
- (iii) Student default prospects (CSL, see slide)

(B) Income contingent loans (NZ, Australia, England, Hungary):

- (i) Collected on basis of capacity to pay
- (ii) Minimise repayment burdens
- (iii) Provide default insurance
- (iv) Administratively demanding

RAPPEL

REMBOURSEZ VOTRE PRÊT D'ÉTUDES DU CANADA

POUR ÉVITER D'ÊTRE EN DÉFAUT DE PAIEMENT,
COMMUNIQUEZ AVEC VOTRE BANQUE :

- au début de chaque année scolaire;
- à la fin de vos études;
- si vous déménagez;
- si vous abandonnez vos études;
- si vous devenez étudiant à temps partiel.

SINON VOICI LES CONSÉQUENCES :

- votre réputation de solvabilité sera ternie;
- vous n'aurez plus droit à des prêts d'études;
- vous ferez l'objet de mesures de recouvrement;
- vos remboursements d'impôt seront retenus.

REMINDER

REPAY YOUR CANADA STUDENT LOAN

TO AVOID DEFAULTING, KEEP IN TOUCH WITH YOUR BANK:

- when you begin a new school year;
- at the end of your studies;
- if you move;
- if you drop out;
- if you become a part-time student.

CONSEQUENCES IF YOU DON'T:

- poor credit rating;
- no further Canada Student Loans;
- collection action;
- withholding of income tax refunds.

4 Repayment burdens with “normal” loans and ICL



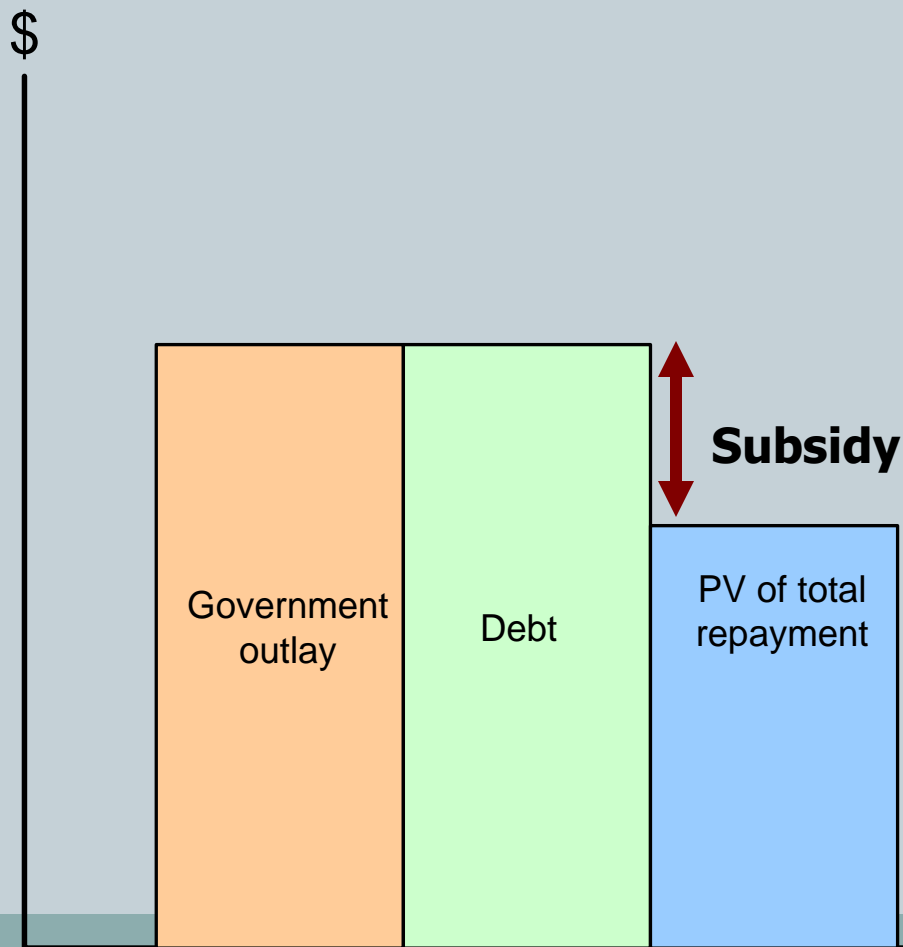
(i) $RB = \text{Loan repayment at time } t / \text{Income at time } t$

(ii) Examples of RB for “normal” loan examples for bottom 20 per cent of graduate incomes: US lawyers, $RB = 65\%$; Thailand female graduates = 75% ; Colombian female graduates = 85% .

(iii) Examples of RB for ICL: NZ $< 10\%$; Australia = 8% ; England $< 9\%$.

(iv) Consumption smoothing and default benefits

5 The important role of loan design and interest rate subsidies



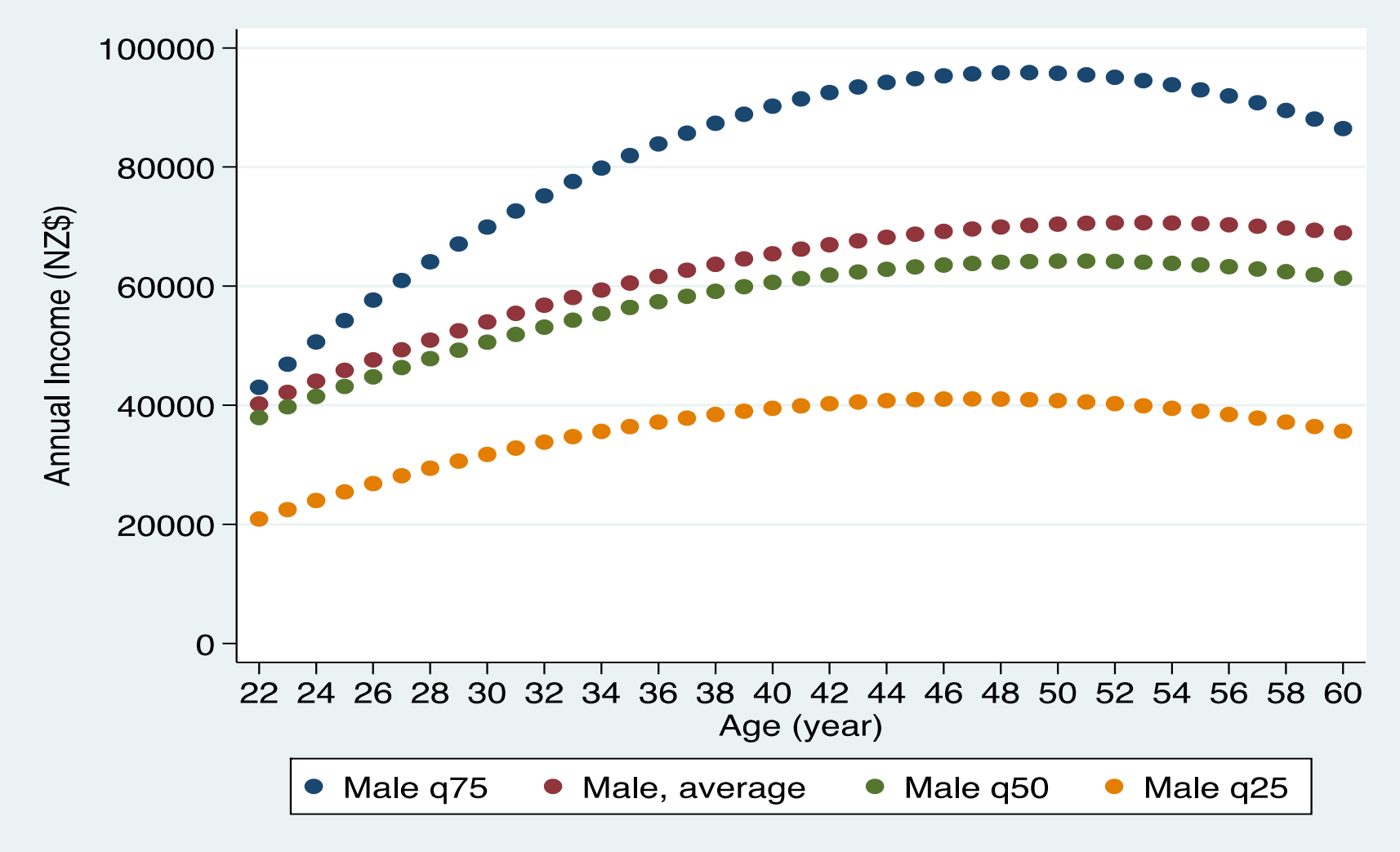
- Repayment conditions of the loan determine if there is an interest rate subsidy
- With subsidies the PV of total repayment is always less than the original debt

6 Illustrating (hypothetical) interest rate subsidies for NZ

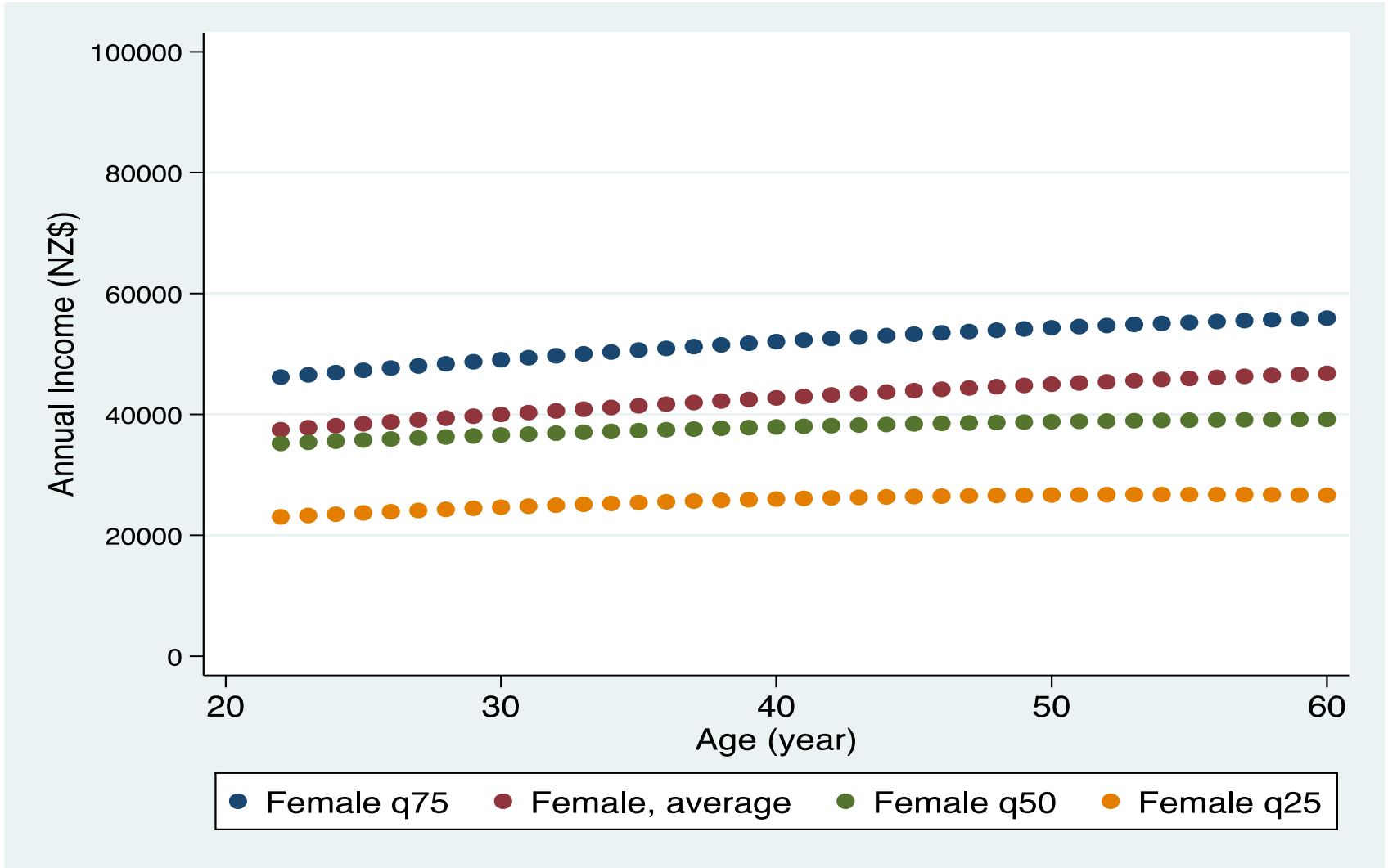
Assumptions with the exercise:

- (i) 2011 Australian graduate incomes to approximate NZ incomes (adjusting for GDP/capita and the exchange rate);
- (ii) Imposing NZ 2012 loan parameters;
- (iii) Breaking down the income data into quantiles; and
- (iv) Showing subsidies for 3 different regimes: real cost of borrowing (1992); zero real cost of borrowing; current -3% real cost of borrowing.

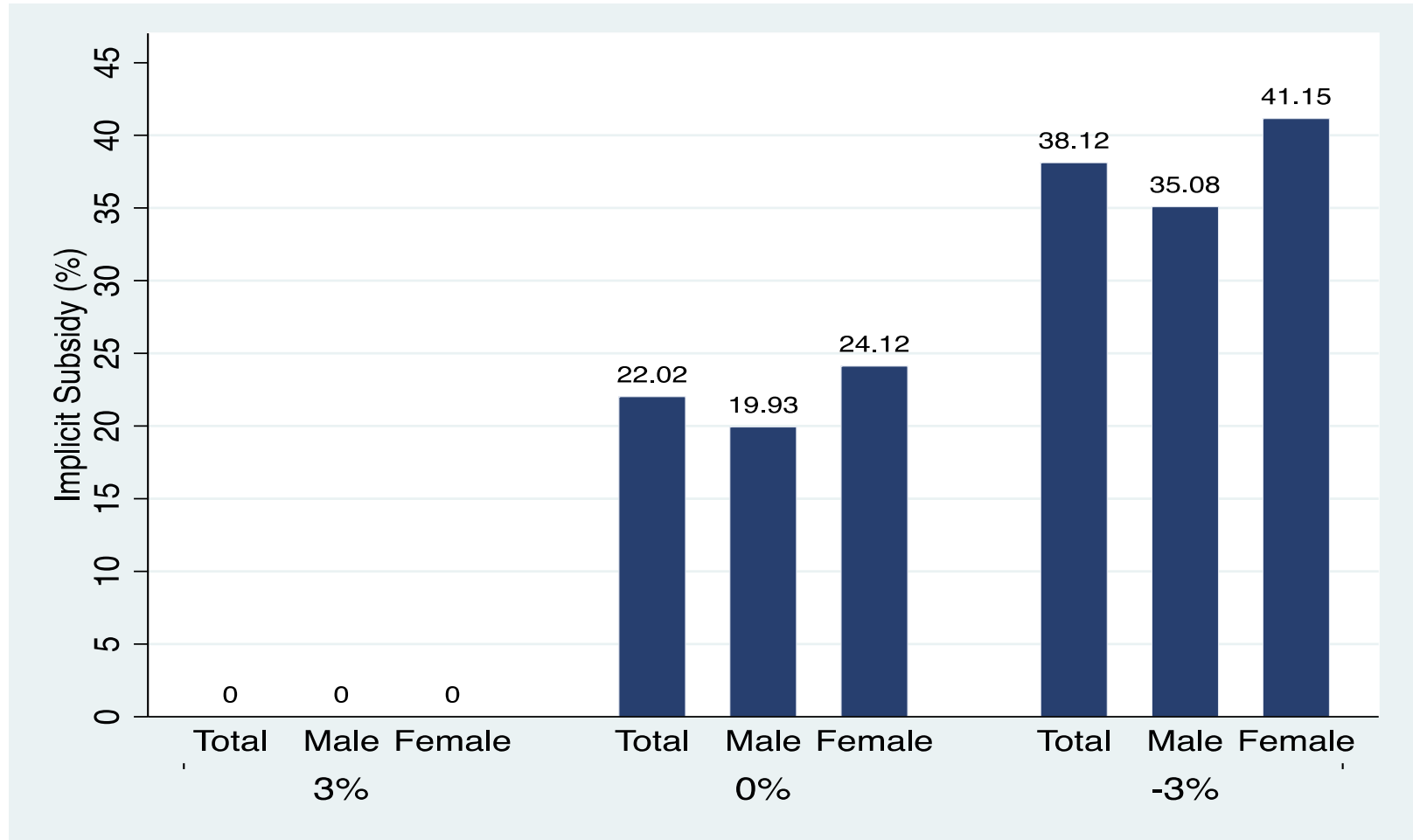
(Hypothetical) Male Graduate Wage Profiles: Quantiles



(Hypothetical) Female Graduate Wage Profiles: Quantiles

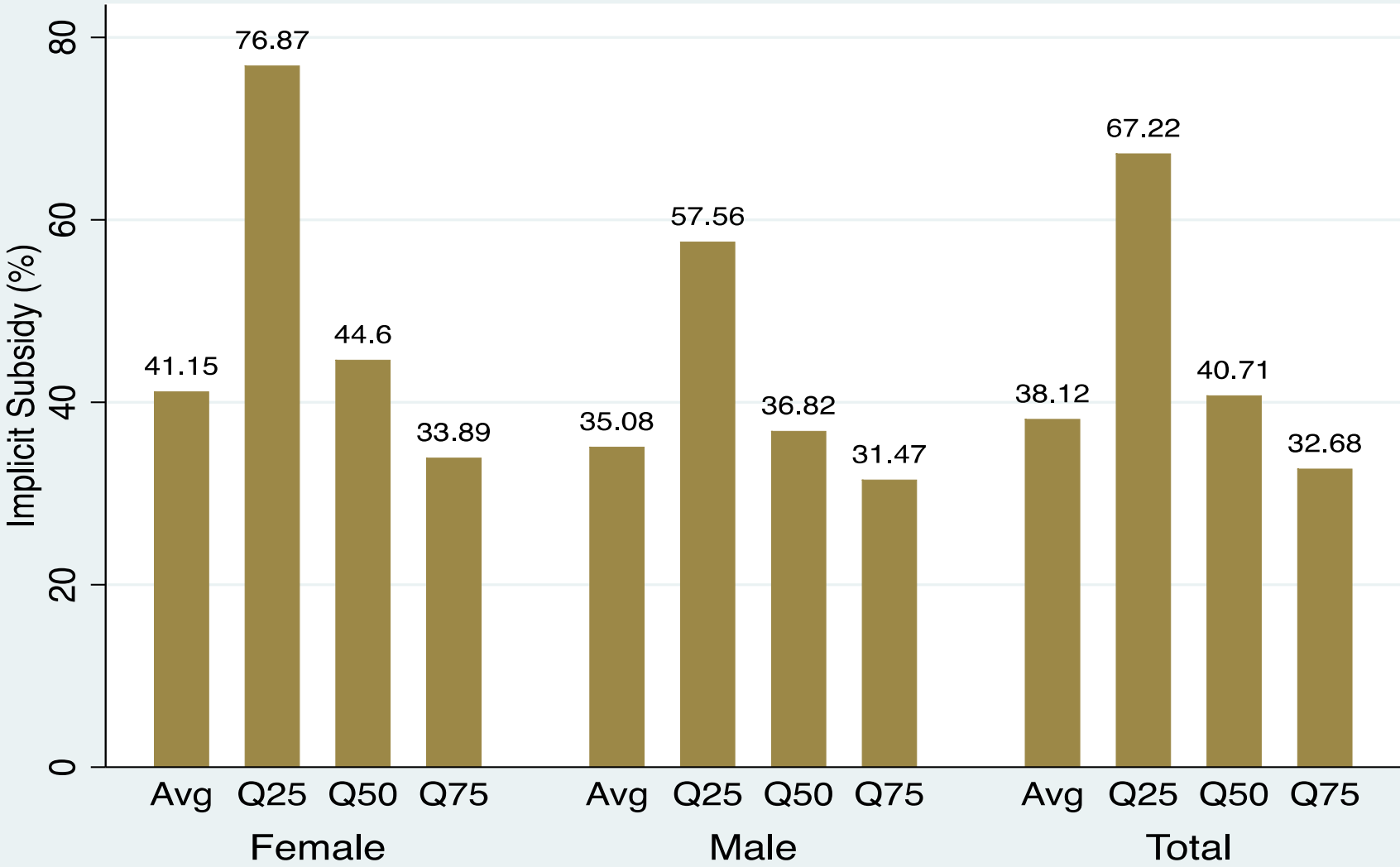


Implicit subsidy results



Note: if the real interest rate is -5% (ie, inflation is 5%), the implicit subsidies for Males = 43.18%, Females = 49.77% and Total = 46.48%

Subsidies by quantile at -3% real interest rate



7 Research and policy issues for loan reform



- (A) What is the right interest rate regime, for tuition and income support?
- (B) What price should be charged?
- (C) Can income support be changed?: Maybe not cheaply with current the NZ interest rate regime).
- (D) Recovering debts from graduates overseas: options from Australia)
- (E) From this morning: (i) no evidence of effects of ICL fees on socio-economic access; (ii) Surcharge instead of ir interest; (iii) how to collect from overseas – some ideas.