Student Debt and Consumer Costs

in the Minneapolis-St. Paul Area

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The state PIRGs are non-profit, non-partisan public interest advocacy groups. The state PIRGs started the Higher Education Project in 1994 to secure more student aid, with a focus on increasing grant aid, lowering the cost of borrowing, and providing better service to students in the federal financial aid system.

For more information:
State PIRGs' Higher Education Project: www.pirg.org/highered
Student Debt Alert: www.studentdebtalert.org

EXECUTIVE SUMMARY

Higher education in America continues to be critical for both individual success and the economic and political health of our country. While college attendance has grown over the past two decades, state appropriations and federal aid have failed to keep pace with the rising cost of college. As a result, more students than ever must rely on student loans to pay for a four-year degree and start their post-collegiate lives with significant debt.

In fact, *student loan debt is rising faster than the cost of living or health care costs*. Between 1993 and 2004, the average debt for college graduates with loans increased by 107% to $19,200. At the same time, in the Minneapolis-St. Paul area, the cost of living increased by 35%, and health care costs (including insurance, drugs and medical care) increased by 58%.

Two-thirds of college graduates in 2004 finished school with student loans. After student loan interest rates increase significantly in July 2006, many borrowers will find it even harder to afford necessities such as health care, rent and groceries because of higher loan payments.

High debt can affect where graduates live, the kind of careers they pursue, when they start a family or purchase a home, and whether they can save for retirement. The combination of high student debt and low earnings can lead to default, ruined credit and wage garnishment.

To reduce student debt and ensure that higher education remains within reach for all Americans, we need to increase need-based grant aid; make loan repayment fair and affordable; protect borrowers from usurious lending practices; and provide incentives for state governments and colleges to control tuition costs.

INTRODUCTION: HIGHER EDUCATION INCREASINGLY PUTS STUDENTS IN DEBT

In America, a college education has always served as a passport to success. A college graduate earns on average nearly $1 million more over their lifetime than a comparable high school graduate.[1] As America moves to a more knowledge-based economy, a college diploma is becoming more essential than ever for even entry-level jobs.[2]

Higher education is equally critical for the economic, political and social health of our nation. Colleges train the corporate leaders and innovators who drive American and global businesses. They educate our nurses, teachers and public servants. They offer opportunities for Americans of all backgrounds and thus serve as a force for fairness and equality.

While college attendance has grown over the past two decades, state appropriations and federal aid have failed to keep pace with the rising cost of college. As a result, more students must rely on student loans to pay for a four-year degree and start their post-collegiate life with significant debt.

In 1993, Congress increased the loan limits for federal student loans and expanded eligibility for the program. Participation in the loan programs grew significantly as college costs rose faster than grant levels. In 1993, 46% of college students graduated with debt. By 2004 that number had increased to 66% for all college graduates and 62% for public, four-year college graduates (Table 1).[3]

Table 1. Percentage of College Seniors Graduating with Student Loan Debt, 1993 and 2004

	1993	2004
Total	46.5%	66.4%
Public 4-Year Schools	42.6%	62.4%
Private 4-Year Schools	54.1%	73.9%

Source: 1993 & 2004 National Postsecondary Student Aid Study

FINDINGS: STUDENT DEBT IS RISING FASTER THAN THE COST OF LIVING

To put student debt levels in context, we compared student debt with basic consumer costs between 1993 and 2002. Our analysis, based on data from the federal Bureau of Labor Statistics' Consumer Price Index (CPI), found that student loan debt is rising significantly faster than the cost of living. Student debt even outpaces the dramatic growth in the cost of health care over the past decade. Specifically:

• Between 1993 and 2004, the average debt for seniors graduating with student loans increased by 107%.

The average borrower graduated in 1993 with $9,272 in student loan debt. By 2004, the average graduating borrower carried $19,210 in undergraduate debt, an increase of 107%. Graduates from public four-year colleges carried slightly less debt, averaging $17,250, while private college graduates had $22,125 in average debt (Table 2).[4]

Table 2. Average Debt Carried by Graduating Seniors with Student Loans, 1993 and 2004

	1993	2004
Total	$9,272	$19,210
Public 4-Year Schools	$8,014	$17,250
Private 4-Year Schools	$11,356	$22,125

Source: 1993 & 2004 National Postsecondary Student Aid Study

About the Consumer Price Index

The Bureau of Labor Statistics' Consumer Price Index (CPI) surveys the cost of core consumer goods such as food, housing, transportation, medical care and apparel. The data are collected in 87 urban areas by surveying retail and service establishments as well as landlords and tenants. Data are collected on a monthly basis and date back to 1913 for some consumer goods. Businesses use the CPI to calculate "cost of living" wage increases for employees, and the federal government uses it to determine changes in funding for Social Security, food stamps or school lunches.[5] Researchers frequently use the CPI as a standard measure of inflation.

• The rise in the average debt carried by a graduating college student has outpaced inflation in the Minneapolis-St. Paul area. The overall cost of living in Minneapolis-St. Paul increased 35% between 1993 and 2004.

Between 1993 and 2004, the cost of living (as measured by the CPI) increased 35% in the Minneapolis-St. Paul area (Table 3).[6] In other words, $100 spent in 1993 is equivalent to $135 spent in 2004. This was slightly higher than the 30% general inflation rate over the same period for the United States as a whole.

This increase in the CPI reflects higher costs for various consumer goods and their significance in an average household's budget. In addition to accounting for inflationary increases, the CPI reflects the rapidly growing cost of gasoline and health care.[7]

Table 3. Increase in Consumer Costs and Student Loan Debt Between 1993 and 2004

Cost of Living: Minneapolis-St. Paul	Medical Expenses: Minneapolis-St. Paul	Average Debt: Nationally
35%	58%	107%

Source: Bureau of Labor Statistics Consumer Price Index (CPI)

• The rise in the average debt carried by a graduating college student has outpaced the increase in health care costs in the Minneapolis-St. Paul area. Health care costs in Minneapolis-St. Paul, including insurance, drugs, and medical services, increased by 58% between 1993 and 2004.[8]

Between 1993 and 2004, health care and medical costs (as measured by the CPI) increased by 58% in the Minneapolis-St. Paul area, faster than the rate of inflation.[9] This increase has been driven by the rising cost of prescription drugs and other treatment, hospital stays and doctors. Still, average student debt levels grew even faster (Table 3).

ECONOMIC REALITIES OF RISING STUDENT DEBT

Going to college increasingly requires student debt, creating new economic pressures for recent graduates. Larger loans and rising interest rates result in larger monthly payments to balance with core expenses such as rent, food, and health care.

A recent study by the Commonwealth Fund found that two in five college graduates can expect to spend at least part of the first year out of college without health insurance.[10] In fact, 18-24 year olds are the most underinsured age group, with more than 30% lacking coverage; 25-34 year olds fare only slightly better, with more than 25% uninsured.[11]

The rapid rise in student debt comes while the real median income of younger Americans has only modestly increased. The Federal Reserve found that between 1995 and 2004, real median income for households with income earners under 35 increased by only 4.4%, compared with a 23% increase for those in the 45-54 age range.[12]

High debt can affect where graduates live, the kind of careers they pursue, when they start a family or purchase a home, and whether they can save for retirement.[13] According to Harvard Law School professor and personal bankruptcy expert Elizabeth Warren, "[I]t's really about what it means to be 28 and try to make loan payments and health insurance premiums and still put something aside for a down payment for a house. Think about how much extra room you have to have in your budget to cover those three things. Most can't do it."[14]

Even average debt can prevent students from entering critical public service careers with low starting salaries, such as teaching and social work. A recent report by the state PIRGs found that 23% of public four-year college students graduate with too much debt to manageably repay as a starting teacher. Thirty-seven percent (37%) of public four-year college graduates have too much debt to manage as a starting social worker.[15] If the goal of a college education is to provide students with new opportunities and life paths, debt can serve as a roadblock for many graduates.

THE IMPACT OF RISING INTEREST RATES

The growth in student loans will soon collide with rising interest rates, making a college education even more costly and making it more difficult for borrowers to achieve financial stability. Over the past decade, students have been able to combine their loans and lock in historically low interest rates through a process called "consolidation." (As recently as 2005, interest rates for student loans were 3.34%, with incentives from both private and public loan programs to drive rates down further.)

Starting in 2006, all new federal student loans will be at a fixed 6.8% interest rate. This rate will protect students from potentially higher rates in the near future but will prevent students from benefiting when interest rates go back down.

The increase in debt and interest rates will be most painful to students with high debt and low salaries. These students may have to make tough choices between core costs such as health care, rent and loan repayment.

SOLUTIONS TO CURB STUDENT LOAN DEBT

The federal government provides programs to allow graduates with high debt to extend their repayment, making smaller monthly contributions over a longer time period. While this can ease pressure on recent graduates' budgets, it also results in higher interest costs over time and debt than can last for decades.

Colleges, universities and state and federal governments should address the challenges that debt poses to graduates with low or moderate incomes by controlling the growth in student debt and making loan repayment more fair and affordable. We suggest a number of solutions to address the issue of unmanageable student debt:

<u>Increase Need Based Grant Aid.</u> The federal Pell grant, which helps students with lower incomes, has been stagnant at $4,050 a year for the past four years while college costs have soared. At the state level, merit-based aid programs have been supplanting need-based aid programs while the overall pool of funds remains the same. Increasing need-based grant aid will reduce how much students have to borrow.

<u>Make Repayment Fair and Affordable</u>. Loan payments should be manageable for borrowers at all income levels, and student debt should not grow unchecked or last indefinitely. Loan repayment policies must be improved so that they do not push borrowers into poverty or discourage people from getting a college degree.

<u>Promote Borrower Protections</u>. As costs rise higher than federal loan limits, students and parents are turning to unregulated private loans to fill the gap. All student loans should have fair and clear interest rates, and students and parents need basic consumer protections in the private loan market. Lenders that give borrowers misleading information and/or charge predatory rates must be punished.

<u>Establish Incentives to Limit Tuition.</u> State governments and colleges that keep tuition costs low should receive financial incentives that further enable them to maximize enrollment at an affordable cost to students.

METHODOLOGY

To calculate the average student debt level and percentage of students graduating with loans, we used the National Postsecondary Student Aid Study, a nationwide survey conducted by the Department of Education's National Center for Education Statistics. To calculate changes in the Consumer Price Index, we used the Bureau of Labor Statistics' data on All Urban Consumers.

The CPI for the Minneapolis-St. Paul area includes the following counties: Anoka, Carver, Chisago, Dakota, Hennepin, Isanti, Ramsey, Scott, Sherburne, Washington, and Wright counties in Minnesota and Pierce and St. Croix counties in Wisconsin.

END NOTES

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