

Student loan scheme – it's a good deal

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The recommendations from the tertiary education student support review are expected to be made public some time this month and, pundits think, they could include measures to make the student loan scheme more generous. But there is no justification for making the loan scheme more generous than it is.



There has already been considerable back-sliding since late 1999 as a result of government policy changes, including the write-off of loan interest while students are studying, increases in repayment thresholds and interest rates caps. These changes have significantly increased the scheme's cost (for little policy gain) and will increase loan debt outstanding by one-third by 2020.

Following recent news that the amount of student loan debt outstanding had reached \$6 billion, the New Zealand University Students' Association called for the government to go further than simply enhancing the loan scheme. It wants a living allowance for all students.

The government should ignore student union propaganda around debt. The New Zealand loan scheme is, and has always been, one of the world's most generous. And the post-1999

changes have made it even more so.

This may be surprising to some, but it is undeniable:

- The scheme allows students, irrespective of income, to borrow money to cover tuition fees, living costs, books and student union fees.
- The 'posted' interest rate, at 7%, is far less than banks charge for unsecured borrowing, while the effective interest rate is much lower – 2.7% – because of interest write-offs.
- Students do not pay interest while they are studying – any interest that accrues during this period is written off. That is, taxpayers foot the bill.

The repayment provisions are also favourable. Graduates only begin to repay loans once their earnings reach around \$16,000 (and unlike income tax brackets, this threshold is tied to inflation). Furthermore, student loan repayments are linked to income. Students who don't find a job right after graduation, or who leave the labour force for some reason, don't need to make loan repayments in that year, as long as their income is low enough. Any accrued interest is written off.

Compare those terms and conditions with those faced by farmers, small business owners or homeowners, who borrow commercially. The differences are stark. While a farmer who can't meet repayments because of low income will get a 'friendly' visit from their banker, graduates who can't meet repayment obligations get an interest write-off. Yet, graduates

are, on average, from better-off families and go on to earn higher incomes over their lifetime.

Harsh and unfair? You decide.

The government should resist calls to make the loan scheme more generous, whether by lowering the interest rate or lifting repayment thresholds. More generous terms will simply encourage more borrowing, which would lead to howls of protest and renewed calls for the scheme's elimination! We've been there, done that.

The student support review should instead focus on reducing the loan scheme's built-in subsidies. It could recommend the abolition of interest write-offs for those who are studying and could examine ways of better targeting loans, whether on the basis of parental income, age or location.

Much has been made of the "threat" posed by the growing level of outstanding student loan debt. This is pure hype – student loan debt represents less than 8% of outstanding mortgage debt.

The focus on student debt alone ignores the fact that these loan liabilities have a corresponding asset – the human capital built up through tertiary study. Countless studies have highlighted the benefits – higher lifetime earnings – that accrue to tertiary students. Those who are really concerned about debt could perhaps turn their attention to more serious issues such as government investments in Air New Zealand, idle power plants and unnecessary banks.

Data compiled by the Treasury in the late 1990s showed that, relative to countries such as Canada and the United States, New Zealand's student allowance policy was generous. It is unlikely we have moved down the ladder since then. The trend in recent years has seen countries moving away from allowances toward student loans.

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The funds needed to pay for student allowances must come from somewhere and taxpayers can finance almost five students through loans for the cost of one on allowances.

This is not to deny that students make sacrifices to get a tertiary qualification. They do. But all investments – whether in a new business, technology or a herd of cattle – require some up-front commitment to realise future gains.

Since its inception in 1992, the scheme has created opportunity for hundreds of thousands of New Zealanders by allowing

them to finance their tertiary education. It offers students and taxpayers a good deal. Nicholas Barr of the London School of Economics has called the pre-1999 student loan scheme a world leader.

It is well worth preserving.

This article does not necessarily reflect the views of the Education Forum.

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