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Hearing before the Senate Banking, Housing, and Urban Affairs Subcommittee on Economic Policy: "The Student Debt Burden and Its Impact on Racial Justice, Borrowers, and the Economy"
April 13, 2021

Chair Warren, Ranking Member Kennedy, and Members of the subcommittee: Thank you for inviting me to discuss federal student loans and their role in the economy.

The federal student loan program has gained increased attention as the size of the portfolio has grown from $516 billion in 2007 to around $1.6 trillion today. I look forward to presenting the data and economic evidence to help inform this discussion.

In this testimony, I will make the following points:

- Despite its shortcomings, the federal student loan program, on average, represents a good investment for students.
- Blanket debt forgiveness does not have a high "bang-for-your-buck" in terms of stimulating the economy. While more targeted relief may be needed, it's a poor use of resources to cancel loans for everyone, especially highly educated students who are most likely to be high earners. There are much better ways to spend $1.6 trillion.
- Blanket debt forgiveness would introduce a moral hazard that could encourage students to borrow more and reduce incentives for schools to contain costs.
- Reforms should be made with the objective in mind. If the goal is to help struggling borrowers, then give them targeted relief without giving a windfall to the wealthy. Those who are able to pay back the full amount should be expected to do so. If the goal is to help low-income students afford the cost of college, programs like Pell Grants are much better forms of direct assistance.
- Given the nation's unsustainable fiscal outlook, any student loan relief or changes to federal higher education financing should be offset either with savings from within the student loan program or elsewhere in the federal budget in the form of increased revenue, decreased spending, or some combination. It may be *worthwhile* to provide targeted loan relief, but that does not mean it is *free*.

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The Role of Student Loans in Completion and Earnings

Despite its flaws, the federal student loan program is currently one of the country's primary tools for expanding access to higher education. While increased access to borrowing does tend to increase personal debt, it also leads to students taking more and harder classes, taking on fewer second jobs and less credit card debt while in school, completing college at higher rates, defaulting at lower rates, and increasing earnings.[1] On average, the increase in lifetime earnings far exceeds the cost of the loan.[2]

While repaying loans can be burdensome, not having access to the loans in the first place would prevent many from pursuing and completing higher education. Proposals to make college free, even in their most expansive forms, are estimated to decrease borrowing by just 15 percent.[3] Making undergraduate public colleges and universities tuition-free does not change the cost for those undergraduates attending private colleges (3.6 million in 2018) or graduate school (3 million in 2018).[4] Furthermore, many students attending "free" public colleges would still need to borrow to cover the cost of living while attending school full-time.

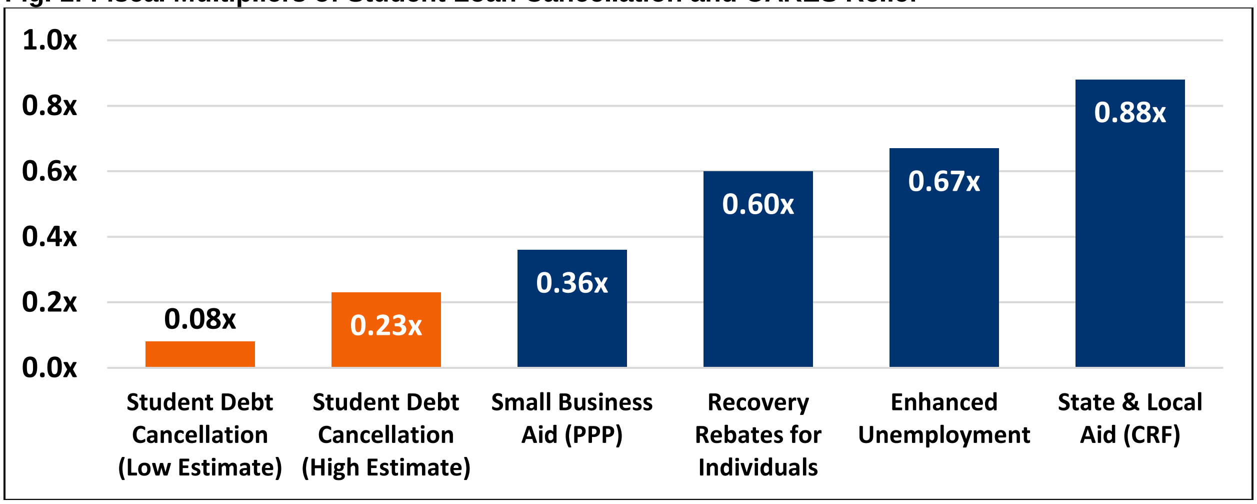
To be sure, there are problems with the federal student loan program. Because going to college doesn't always lead to higher earnings, owing a fixed monthly payment can be burdensome to many. Policymakers should find ways to alleviate some risks of borrowing to pay for education, either by reforming the loan program or finding a different financing mechanism altogether. But for many people, borrowing to pay for their education is the right decision in the long run, leading to a long-term increase in earnings that more than makes up for the short-term cost of paying off their loans.

[1] Mark Wiederspan, "Denying Loan Access: The Student-Level Consequences When Community Colleges Opt Out of the Stafford Loan Program," Economics of Education Review, Vol. 51, April 2016, https://www.sciencedirect.com/science/article/abs/pii/S0272775715000837?via%3Dihub; Benjamin Marx & Lesley Turner, "Student Loan Nudges: Experimental Evidence on Borrowing and Educational Attainment," American Economic Journal: Economic Policy, Vol. 11, No. 2, May 2019, https://www.aeaweb.org/articles?id=10.1257/pol.20180279; and Sandra Black et al., "Taking It to the Limit: Effects of Increased Student Loan Availability on Attainment, Earnings, and Financial Well-Being," NBER Working Paper Series, August 2020, https://www.nber.org/system/files/working_papers/w27658/w27658.pdf.
[2] Beth Akers and Matthew Chingos, "Is a Student Loan Crisis on the Horizon?", The Brookings Institution, June 2014, https://www.brookings.edu/research/is-a-student-loan-crisis-on-the-horizon/.
[3] Jason Delisle & Preston Cooper, "Free College and the Debt-Free Fantasy," American Enterprise Institute, June 2020, https://www.aei.org/research-products/report/free-college-and-the-debt-free-fantasy/.
[4] "Digest of Education Statistics," National Center for Education Statistics, https://nces.ed.gov/programs/digest/2019menu_tables.asp. Latest numbers are from 2018.

Blanket Student Loan Forgiveness Would Do Little to Stimulate Economy

A common argument for blanket loan forgiveness is that it would be a form of economic stimulus. However, the Committee for a Responsible Federal Budget estimated in November that canceling all federal student debt would have a fiscal multiplier between 0.08x and 0.23x, far lower than the major provisions contained in the various pandemic relief bills to date.[5] For comparison, the Congressional Budget Office estimated that the Economic Impact Payments (stimulus checks) in the CARES Act provided a 0.60x multiplier, while the enhanced unemployment benefits provided a 0.67x multiplier. Given that two additional relief packages have been enacted since November and economic prospects are stronger now, the debt forgiveness multipliers would likely be even lower if re-estimated today.

Fig. 1: Fiscal Multipliers of Student Loan Cancellation and CARES Relief



Source: Congressional Budget Office, CRFB calculations

Blanket student loan forgiveness is a relatively ineffective form of economic stimulus for a few reasons. First, forgiving all student debt would not suddenly unleash $1.6 trillion into the U.S. economy. People make monthly payments on their loans, and that monthly payment roughly corresponds to the increase in income borrowers would gain if all their student debt was forgiven. The normal amount of loans repaid per year is $70-85 billion, which is a relatively small immediate benefit compared to the full cost of forgiving all debt.[6] Further, only 8 percent of all federal student loan dollars (10 percent of borrowers) are in active repayment right now given the Biden Administration's pause of student loan payments through September. As long as that pause is in effect, loan forgiveness would not increase the monthly incomes of the 90 percent of borrowers who are already not paying their loans.[7]

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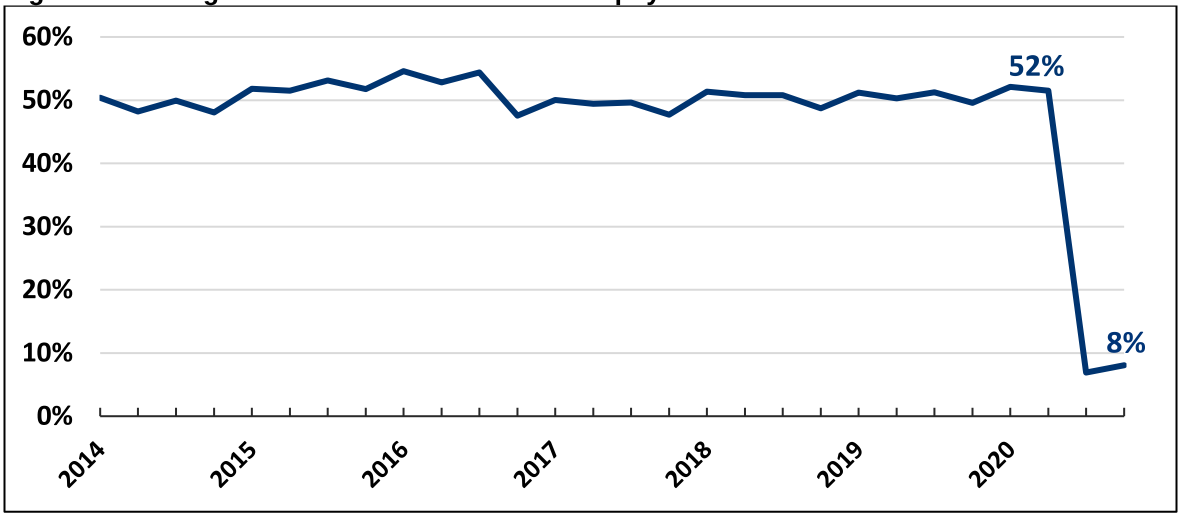
[5] "Canceling Student Loan Debt is Poor Economic Stimulus," Committee for a Responsible Federal Budget, November 2020, https://www.crfb.org/blogs/canceling-student-loan-debt-poor-economic-stimulus.

[6] $70 billion from Jordan Weissmann, "An Extremely Important Statistic About Student Debt That Has Never Been Published," Slate, March 2021, https://slate.com/business/2021/03/student-loan-total-annual-government-payments.html.That number does not include the amount from a small portion of the portfolio, so the higher number is the author's estimate to account for that discrepancy.

[7] "Portfolio by Loan Status," Office of Federal Student Aid, https://studentaid.gov/sites/default/files/fsawg/datacenter/library/PortfoliobyLoanStatus.xls

Fig. 2: Percentage of Student Loan Dollars in Repayment



Source: Department of Education

There would likely be a small additional boost in spending from people knowing they no longer have debt. However, this tendency – known as the "wealth effect" – would be unlikely to increase spending by more than 3-6 cents per dollar of debt forgiven.[8]

We expect that more tailored proposals to forgive $50,000 or $10,000 in student debt would also have similarly low, or even lower, multipliers. That's because over $500 billion in student loan debt is held by more than 9 million borrowers who have their monthly payments tied to their incomes. For many of those borrowers, cancelling $10,000 of their debt would have *no* effect on their monthly payments. For those with low incomes, they are already paying $0 per month, and for those who are paying some amount per month, it would only reduce the number of months they would need to repay. Helping borrowers finish paying off their loans in 2029 instead of 2031 would have virtually no effect on stimulating the economy in the near term.

Second, blanket loan forgiveness is a poor way to target stimulus because it gives the most benefit to higher-income households and those with no trouble repaying their loans, even if the dollar amount of forgiveness is capped at $10,000 or $50,000.[9] An additional dollar given to someone with a high income is much more likely to be saved and provide little economic boost to demand.

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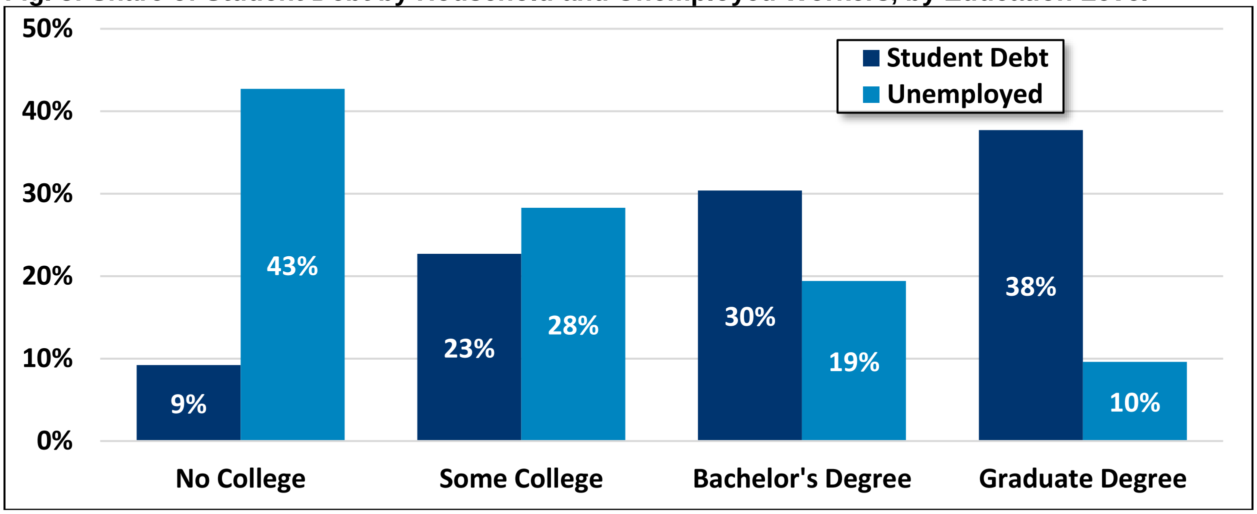
[8] Anna Louie Sussman, "New Estimates of the Stock Market Wealth Effect," NBER: The Digest No. 8, August 2019, https://www.nber.org/digest/aug19/new-estimates-stock-market-wealth-effect; Daniel Cooper, "Wealth Effects and Macroeconomic Dynamics," Journal of Economic Surveys Vol. 30, 2016, https://scholar.harvard.edu/files/kdynan/files/1._wealth_effects_and_macroeconomic_dynamics.pdf; and Mark Zandi et al. "Weighing the Wealth Effect," Moody's Analytics, March 2018, https://www.moodysanalytics.com/-/media/article/2018/weighing-the-wealth-effect.pdf.

[9] For an exhaustive analysis of the redistributive effects of blanket student loan forgiveness, see Sylvain Catherine & Constantine Yannelis, "The Distributional Effects of Student Loan Forgiveness," NBER Working Papers, December 2020, https://www.nber.org/papers/w28175.

Before the onset of the COVID-19 pandemic, over 70 percent of monthly student loan payments were paid by the top 40 percent of earners.[10] The median weekly income of a full-time worker with a bachelor's degree is $1,283, and $1,627 for those with graduate degrees. Compare that to workers with only a high school degree, who earn a median weekly income of $781: any additional cash is more likely to be spent by the worker without a college education.[11] Almost half of all outstanding federal student loan dollars were used to attend graduate school.[12]

Fig. 3: Share of Student Debt by Household and Unemployed Workers, by Education Level



Source: People's Policy Project, Bureau of Labor Statistics, CRFB calculations
Share of student debt in 2019 by household; share of unemployed (not seasonally adjusted) in March 2021

Especially considering the uneven, "k-shaped" recovery from the early months of the pandemic, in which higher-educated workers were more likely to retain their jobs and workers with lower levels of education lost work or had their hours cut back, forgiving debt of those who fared better financially during this crisis is a particularly poor use of resources. More than 70 percent of currently unemployed workers do not have a bachelor's degree, including 43 percent who never attended college.

Blanket Debt Forgiveness Could Create a Moral Hazard

Absent other reforms to higher education financing, blanket student debt forgiveness would likely result in increased borrowing and reduce incentives for schools to keep costs under control.

The people who would benefit from student debt forgiveness are those who have already taken out loans and have outstanding balances. If student debt were cancelled without other significant changes to the student loan system, a reasonable person might expect the moral case for blanket

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[10] Sandy Baum & Adam Looney, "Who Owes the Most in Student Loans: New Data from the Fed," The Brookings Institution, October 2020, https://www.brookings.edu/blog/up-front/2020/10/09/who-owes-the-most-in-student-loans-new-data-from-the-fed/.
[11] Bureau of Labor Statistics, data for 4th quarter of 2020.
[12] "The Volume and Repayment of Federal Student Loans: 1995 to 2017," Congressional Budget Office, November 2020, https://www.cbo.gov/publication/56706.

debt forgiveness to be just as strong next year as it is now. The expectation that $10,000, $50,000, or even all of their debt might be forgiven at some point could become an influential factor driving more students to borrow more money than they might have before. Using the same logic, many borrowers would likely decide to pay down as little of their debt as possible over as long a timeframe as possible.

That same expectation would lead many borrowers to be less sensitive to tuition increases, which would alleviate pressure on schools to rein in costs, especially graduate schools where student loan amounts are not capped.[13] This could create a vicious feedback loop where students borrow more, incentivizing schools to raise prices, which in turn forces students to borrow even more.

In the meantime, pressure would build on Congress to offer another round of blanket forgiveness, all while doing nothing to address the underlying issues in federal higher education finance policy.

Issues with the Current Federal Student Loan System

While federal student loans are still a good bet on average, there are significant problems within the portfolio. Before the pandemic, about half of the loans that ought to have been in repayment were not. That is to say, over 20 million borrowers who should have been making progress towards paying off their loans were instead delinquent, in forbearance or a hardship deferment, or were in default.[14]

The causes of this non-repayment are multifaceted, but for a large number of borrowers, their education investment did not pay off.[15] Keep in mind, this non-repayment number does not include the additional 9 million borrowers enrolled in Income-Driven Repayment (IDR) plans, which now accounts for 34 percent of all dollars in the portfolio. 75 percent of borrowers in these plans are not paying enough to cover the interest owed each month, so their loan balances are *increasing* over time.[16]

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[13] After factoring out any other forms of financial aid, students enrolled in graduate school (as well as parents) can borrow up to the cost of attendance (tuition plus cost of living).
[14] Office of Federal Student Aid: Federal Student Loan Portfolio, https://studentaid.gov/data-center/student/portfolio.
[15] Borrowers who don't complete school make up a large share of defaulters, see: Ben Miller, "Who Are Student Loan Defaulters?" Center for American Progress, December 2017, https://www.americanprogress.org/issues/education-postsecondary/reports/2017/12/14/444011/student-loan-defaulters/. Borrower behavior as it relates to student loans is also complex and dependent on other factors, see: Jason Delisle & Alexander Holt, "Why Student Loans Are Different: Findings from Six Focus Groups of Student Loan Borrowers," New America, March 2015, https://static.newamerica.org/attachments/2358-why-student-loans-are-different/StudentLoansAreDifferent_March11_Updated.e7bf17f703ad4da299fad650f47ac343.pdf, and "Borrowers Discuss the Challenges of Student Loan Repayment," The Pew Charitable Trusts, May 2020, https://www.pewtrusts.org/en/research-and-analysis/reports/2020/05/borrowers-discuss-the-challenges-of-student-loan-repayment.
[16] Office of Federal Student Aid and "Income-Driven Repayment Plans for Student Loans: Budgetary Costs and Policy Options," Congressional Budget Office, February 2020, https://www.cbo.gov/publication/55968 .

There are several groups of people we should be concerned about in the current student loan program. The first are those who borrow to attend school and either do not earn a degree or do earn a degree but not a sufficient increase in income to justify the loan. Various forms of Income-Driven Repayment programs exist for these borrowers, all of which reduce a borrower's monthly payment to an amount that is considered affordable based on their income, even to the point of having a $0 payment for low incomes. If borrowers participate in these programs, the government forgives their loans after 10, 20, or 25 years.[17] However, the fact that over 9 million borrowers are currently in default shows that simply having these options available is not a cure-all. More can be done to target relief for struggling borrowers. Policymakers could also consider changes to loan availability for schools where a large group of students leave with high debt levels and no increase in income.

The next group of people that policymakers should be concerned about under the current system are parents. The original premise of the student loan program was that the increase in future income from a student's education would allow them to pay back the loan affordably over time, thus justifying taking out a loan in the first place. We don't run credit checks for student loans, because a backward-looking credit score doesn't reflect a student's future earnings potential. However, this same logic does not hold for parents, who experience no increase in income due to their child's education, and thus have no increased ability to pay back the loan after the child graduates. Thus, in the current system, the federal government increasingly acts as a subprime lender to low-income parents, saddling them with high levels of debt that they won't be able to pay back.

There is also concern related to the amount of student debt that Black households are taking on. A higher percentage of Black households hold student debt compared to white and Hispanic households, and the average amount of debt they hold is also higher.[18] Research has also found that Black students with bachelor's degrees are more likely than their white counterparts to pursue graduate education. Black households have less wealth on average and are more likely to borrow for college than white households.[19] The large gap in wealth between Black and white households in the United States is a concerning issue, but student loan relief is a poor mechanism to significantly reduce that gap and does not justify a massive giveaway to wealthier households that have the ability to pay back their loans. While additional targeted economic relief is worthy of consideration, the barriers that Black households face do not justify a poorly targeted and regressive giveaway to other households.

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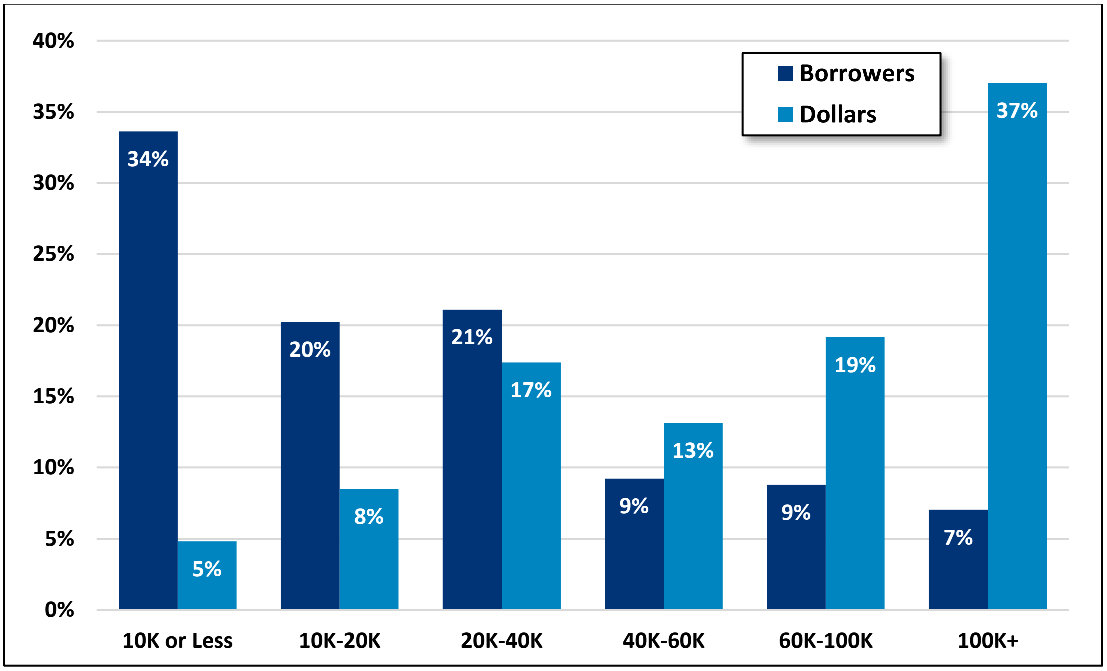
[17] Loans are forgiven after 10 years of payments in an IDR program while working for a full-time for a government or nonprofit employer. This is known as Public Service Loan Forgiveness.

[18] Survey of Consumer Finances Interactive Chartbook, https://www.federalreserve.gov/econres/scf/dataviz/scf/chart/.

[19] Judith Scott-Clayton & Jing Li, "Black-White Disparity in Student Loan Debt More Than Triples After Graduation," Brookings, October 2016, https://www.brookings.edu/wp-content/uploads/2016/10/es_20161020_scott-clayton_evidence_speaks.pdf.

Finally, much of the perceived student loan crisis is related to borrowing for graduate school. Graduate school loans now account for almost half of the federal student loan portfolio in terms of dollars.[20] Graduate students can borrow an unlimited amount up to the cost of attendance, meaning unlike undergraduate loans which have set caps, whatever the school decides to charge determines how much a graduate student is allowed to borrow. The more generous version of IDR enacted in 2012 (and subsequent versions thereafter) represents a windfall for graduate students who accumulate high levels of debt, even after they begin earning high incomes.[21]

Fig. 4: Share of Student Loan Portfolio, by Total Outstanding Balance (4th Quarter 2020)



Source: Department of Education

At this point, the IDR program is subsidizing high-debt graduate degrees. Borrowers with over $100,000 of debt, despite attracting a large amount of media attention, represent only a small portion of borrowers in the overall student loan portfolio (7 percent). However, they represent a significant portion of outstanding dollars (37 percent) and an even larger portion of dollars in IDR (52 percent).[22]

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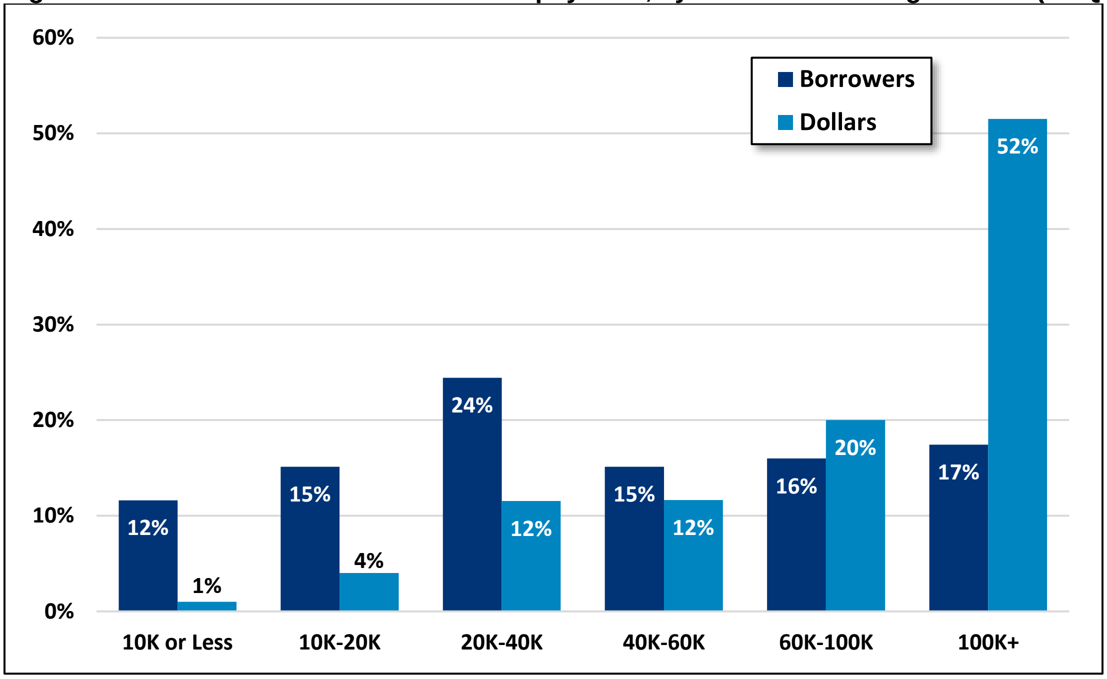
[20] CBO, "The Volume and Repayment of Federal Student Loans."
[21] Jason Delisle and Alex Holt, "Safety Net or Windfall? Examining Changes to Income-Based Repayment for Federal Student Loans," New America, October 2012, https://static.newamerica.org/attachments/2332-safety-net-or-windfall/NAF_Income_Based_Repayment.18c8a688f03c4c628b6063755ff5dbaa.pdf.
[22] Office of Federal Student Aid: Federal Student Loan Portfolio, https://studentaid.gov/data-center/student/portfolio.

Fig. 5: Share of Loans in Income Driven Repayment, by Total Outstanding Balance (4th Quarter 2020)



Source: Department of Education

One way to prevent students from amassing these eye-popping amounts of debt is to cap borrowing for graduate students. Uncapped borrowing for graduate school has only been in place since 2006 and is therefore a relatively new phenomenon. If lawmakers think the absence of firm caps on borrowing for graduate school leads to economic gains, then they should structure the IDR program so that graduates who earn high incomes pay back the full amount. If such high levels of debt are considered unconscionable and immoral, then lawmakers should cap graduate student borrowing.

While blanket forgiveness of student debt would be extremely wasteful, additional targeted relief may be necessary due to the variation in outcomes for those attending college. This feature is already reflected in the current IDR system, but more can be done to help struggling borrowers. The IDR system should be reformed and streamlined to be easier to use. Ballooning balances as a result of IDR payments that cover less than accruing interest may also be a significant impediment to enrolling more borrowers into IDR. A variety of proposals to address this issue have been put forward across ideological lines, and a more equitable IDR program could likely make some of these proposals budget neutral or even save money for the government. By ensuring that high-debt, high-income borrowers enrolled in IDR pay their fair share, the program could be restructured so that relief could be more quickly targeted towards borrowers whose loans do not lead to an expected increase in income. In addition, loans that are forgiven under the normal IDR process should not be taxed as normal income. Doing so essentially shifts a portion of a debt that is 20-25 years old from the Department of Education to the IRS. While the current moratorium on that tax will remain in effect for the next 5 years, it should be made permanent in a budget neutral way by getting graduate borrowers to pay back into IDR for longer.

We Should Not Be Borrowing to Fix Student Loans

Policymakers authorized over $5 trillion of additional borrowing for relief and stimulus measures to address the pandemic. By the end of this fiscal year, debt-to-GDP could reach a record high of nearly 108 percent, overtaking the previous record of 106 percent reached just after WWII. Much of that borrowing was the right thing to do in response to such a cataclysmic and unprecedented public health emergency. In fact, one of the reasons the Committee for a Responsible Federal Budget advocates for responsible fiscal policy in good times is to ensure the country has the capacity to borrow in response to emergencies like the one we've collectively experienced for more than a year now. Borrowing both to manage the public health crisis and to help individuals and businesses stay afloat in the face of major economic shocks is responsible fiscal policy. However, debt was on an unsustainably rising path before the pandemic and the nation's precarious fiscal situation should not be denied or ignored. Now, with the economy poised to take off as vaccinations increase and communities reopen, policymakers must return to paying for the fiscal priorities they wish to enact.

There are many worthwhile policies that policymakers should consider, including increasing targeted relief to struggling borrowers. But if a policy is worth doing, it's worth paying for. Paying for a policy helps it become permanent, decreasing uncertainty about future education policy and allowing students to plan for their future.

Blanket student debt forgiveness is not one of those worthwhile policies. It is unfair and unequitable, providing the highest benefit to high-income earners with graduate and professional degrees. Whether the goal is to stimulate the economy, stop the rise in the cost of college, close the racial wealth gap, help low-income families, or reduce reliance on borrowing student loans, blanket debt cancellation is an extremely expensive policy that offers very low or no returns to those policy goals. And not only does it not reduce the cost of education for future students, it may actually increase them. And it could cost up to *$1.6 trillion*.

An economic relief package shouldn't forgive the loans of doctors and lawyers in the name of sending a small fraction of those dollars to struggling borrowers. Even $10,000 in blanket debt forgiveness is still extremely expensive. For the same ten-year cost, the maximum Pell Grant could be doubled. A package of education reforms should provide assistance to those who need it without the giveaway to those that don't.

Each dollar our federal government spends reflects our priorities as a country, and not all of these policies are created equal. While the federal economic response to COVID-19 has thus far proven remarkably successful in many ways, lockdown policies and the virus itself disproportionately affected certain groups of Americans. Those with lower levels of educational attainment and lower earnings were far more likely to lose their jobs during the pandemic, while many with higher levels of education were able to keep their jobs and actually saw their savings increase. As a nation, our priorities should be continuing the economic recovery and ensuring whatever relief our government provides is targeted directly towards those struggling the most.