The Next Trillion Dollar Bubble

Posted by Arnold Ahlert Bio ↓ on Dec 15th, 2011

One of the oldest economic maxims, "if you subsidize something, you get more of it" has created the next trillion dollar-plus bubble for which American taxpayers will be on the hook. The National Center for Public Policy and Higher Education discovered that published college tuition and fees increased 439 percent from 1982 to 2007, while median family income rose 147 percent. What is driving those costs? The idea that every high school graduate should attend college, and that government–meaning taxpayers–will guarantee loans made to those students.

The bill gets larger each year. Federal assistance to college students has risen 60 percent in the last three years from $97.7 billion in 2008 to $156.1 billion this year. This reflects a steady trend in making ever more money available to students who need financial aid in order to afford college. Back in the mid-1980s, there was a $2500 annual cap on the amount of federal student loans one could access to attend college. Thus, the maximum amount of federal debt one could amass in the process of getting a four-year degree was $10,000.

That amount has more than tripled. For most students, $31,000 is now available and, unsurprisingly, student debt has skyrocketed. The current average debt load for student borrowers is a record $25,250, even as those who attend high-tuition colleges are averaging double that, at over $55,000 per student. And as college tuition continues to rise, so do the number of borrowers. According to the College Board, more than 50 percent of all full-time undergrads at public colleges and universities are now full-time borrowers. At private nonprofit schools, two-thirds of students have outstanding loans.

As indicated above, more money available for borrowing by students has led directly to massive increases in tuition. Those increases substantially exceed the actual costs of the education itself. The Cato Institute reveals that it costs roughly $8,000 to educate an undergraduate at an average residential college, even as a private four-year university averages $37,000 to attend and a public equivalent averages $16,000. The resulting profits allow colleges to expand their facilities, their bureaucracies and their amenities, leading to higher tuition charges.

Hence, a vicious cycle: as college tuition costs increase, the government makes more funding available to students to pay for them. The more funding available–guaranteed by the taxpayers, so that colleges never face the possibility of a loan default–the more they can raise their tuition costs without ever having to worry about getting stiffed.

The American taxpayer, on the other hand, is getting stiffed with increasing regularity. According to the American Department of Education, student default rates rose sharply in 2009, the last year for which statistics are available. 15 percent of borrowers at for-profit colleges and 7 percent of borrowers at public colleges defaulted in the first two years of repayment. This represents increases of 11.6 percent and 7 percent, respectively. Of the 3.6 million borrowers whose first loan payments came due between Oct. 1, 2008, and Sept. 30, 2009, as many as 320,000 walked away from their obligations.

This too creates a vicious cycle. Since student loans are not dischargeable, even through bankruptcy, borrowers face long-term consequences that impinge on their ability to lead the kind of life one expects a college diploma to provide. It can become impossible to borrow money to buy a house or a car, wages can be garnished, tax returns can be seized, and in the ultimate irony, one can have difficulty finding a job in an era where employers are increasingly checking a prospective employee's credit status.

Unfortunately, it's not just defaults that burden the taxpayer. In March 2010, a Democratically-controlled Congress instituted a government takeover of the student loan program as part of Obamacare. Slated to begin in July 2014, those owing student loans would see their payments reduced to 10 percent of their disposable income, down from the current 15 percent. Those who keep up their payments will have their loans forgiven after 20 years, instead of 25. Yet on October 25, in a transparent pander to the youth vote, the president, by executive order, moved the timetable up to 2012.

Both of these moves virtually guarantee that once again "profit," aka a college education, will be privatized, while losses, resulting from the failure to pay one's freely undertaken obligation–either in the form of outright default, or the "forgiveness," of a loan before it is completely paid off–will be socialized.

Yet for those more fully suffused with the American entitlement mentality, even this arrangement is insufficient. In what proponents are laughably characterizing as an economic stimulus, Rep. Hansen Clarke (D-MI) is proposing HR 365, part of which advocates forgiveness of student debt. Why? Government bailed out "rich" bankers, why not "poor" college students?

Such a plan is preposterous. Doubling down on the same bailout mentality that has engendered a massive amount of public anger with respect to the banking system is a fool's errand. It's bad enough the government spent $700 billion of borrowed money on that monstrosity, even if it was a necessary evil. Government has no business subsidizing irresponsible behavior, especially when it is rationalized as two wrongs making a right. Furthermore, why should those Americans who wanted to go to college but didn't, because they couldn't afford it, underwrite the expenses of those who simply want to renege on their responsibilities?

The problem of runaway tuition costs should be attacked at the other end. For example, a study of 198 leading public and private universities produced by the Goldwater Institute reveals that in 2007 “nearly 39 percent of all full-time employees at these universities were engaged in administration, an increase of 39 percent from the number of administrators per 100 students in 1993. Only 29 percent of full-time employees were engaged in instruction, research and service, an increase of 18 percent since 1993.” In other words, the number of bureaucrats has increased twice as fast as the number of teachers.

The Manhattan Institute’s Heather MacDonald offers further insight into this phenomenon, noting that “rising tuitions funnel straight into the preposterously unnecessary diversity bureaucracy and the rest of the burgeoning student-services infrastructure, as well as into the salaries of professors who teach one course a semester, the arms race of ever more sybaritic dorms and social centers, and the absolute monarchies of the football and basketball programs.”

Bloated bureaucracies and high-end amenities don’t translate into better educational experiences. A study led by New York University sociologist Richard Arum of 2,322 traditional-age students from the fall of 2005 to the spring of 2009, revealed that 45 percent of students “made no significant improvement in their critical thinking, reasoning or writing skills during the first two years of college.” After four years, 36 percent “showed no significant gains in these so-called ‘higher order’ thinking skills.”

The fallback position for those touting college at virtually any price is the idea that college graduates make far more money than non-graduates, high school graduates and high school drop-outs. Yet “College Conspiracy,” a film being released on May 15th, will reportedly debunk many of those myths, the most prominent of which is college graduates earn $1 million more over a lifetime than high school graduates. The film notes that that statistic fails to factor in some important variables: most Americans take 6 years to finish 4 years worth of college; tuition at private colleges is increasing at a rate 5.5 percent rate of inflation; and General Equivalency Diplomas (GED) unfairly skew down the earnings potential of regular high-school graduates.

Furthermore, Gerald Celente, editor of The Trends Journal who appears in the film, contends colleges are handing out “degrees in worthlessness.” He cites social studies, philosophy, art history, women’s studies, minority studies, foreign affairs, public administration, corporate management, and marketing as the most conspicuous wastes of time and money.

Yet even if one assumes such a film has its own axe to grind, one thing is certain: math doesn’t lie. If college tuition, aided and abetted by government subsidies, continues to almost triple relative to family income, at some point the amount of debt incurred to obtain a college degree will surpass the additional income one may derive from it. Considering that any attempt to reign in government’s role in facilitating these runaway costs is inevitably characterized as “depriving needy students of critically needed funds,” the trend is likely to continue.

Or at least it will until the bubble pops, exactly like the government-abetted housing bubble did. Are Americans ready for another trillion dollar bailout precipitated by irresponsible government? American are furious with “greedy” bankers. What about greedy college administrators and professors?