

## ***Higher Ed Bubble: Students Pay Just 43% Of Direct Cost***

By DAVID HOGBERG, INVESTOR'S BUSINESS DAILY  
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Students are paying less and less of direct college costs, relying more on government grants and loans. That has encouraged universities to jack up tuition expenses, fueling a vicious circle reminiscent of the housing bubble.

U.S. universities charged students \$190 billion in 2001-02 for tuition, fees, room and board and more, according to data from Sallie Mae. By 2010-11 that had more than doubled to \$410 billion. Even after adjusting for inflation, student charges shot up 72%.

During that time, paying directly for college has declined as a percentage of overall costs, while paying indirectly via government loans and grants has increased. In 2001-02, direct family contribution accounted for 52% of students' higher education bills, while indirect payments accounted for 42%. By 2010-11 that was reversed with grants and government loans accounting for 52% and family contributions amounting to 43%.

### **'Someone Else's Money'**

"What these data show is people consuming higher education are increasingly paying for it with someone else's money," said Neal McCluskey, associate director of the Center for Educational Freedom at the libertarian Cato Institute. "And that includes the loans, because students can get loans at a cheap rate because taxpayers are on the hook for all the risk."

Richard Vedder, an economics professor at the University of Ohio who has studied the economics of higher education at length, sees a link between the price of tuition and the change in how we pay for college.

"I look at the evidence, an explosion in tuition costs accompanied by an explosion in grants and student loans," Vedder said. "What else can explain it?"

When students and families pay for college indirectly, either someone else is paying, in the case of grants, or payments are deferred as with loans. This makes them far less sensitive to the price of tuition and other expenses than they would be if they were paying out of their own pocket. So colleges can hike charges far more than inflation.

Average annual tuition in 2010 for all colleges was about \$17,464 based on data from the National Center for Education Statistics. That's a whopping 32% hike after inflation since 2000.

Not everyone agrees that the shift is responsible for the rise in tuition and overall college costs.

"If you look at the for-profit institutions, tuition is pretty much a function of grants and loans," said Sandy Baum, a senior fellow at George Washington University and independent policy analyst for the College Board. "But where the vast majority of students go, (four-year non-profits, state institutions, community colleges) ... there is no evidence that loans and grants lead to higher tuition."

She claims that the share of students receiving federal and state grants is not that high. She blames tuition hikes at public universities on cuts in state aid.

Since 2008, inflation-adjusted state funding of higher education has fallen 1%, data from the State Fiscal Survey show. But real funding jumped 20% over the entire 2000-11 period, suggesting that other factors are behind rising tuition costs.

"To say that there is no evidence is wrong," McCluskey said. "There is a fair amount of empirical evidence that shows student aid leads to higher prices."

He points to articles in *Economics of Education Review* and *Journal of Human Resources*. The first one showed that Pell grants did cause higher tuition prices at private colleges but not public institutions. The second found student aid in Georgia — the HOPE scholarship — resulted in higher costs at four-year colleges in that state.

But nailing down the link is hard. One reason is that when tuition rises, students often automatically qualify for more aid. It can thus be hard to determine if tuition is rising due to increased aid or aid is increasing because of higher tuition prices.

"In addition to the empirical evidence, you have to use common sense," said McCluskey. "Basic economics says that when you subsidize something, like we have with higher education, you get more demand and higher prices."