

Paying Off Student Loans

by Warren Clark

Many students expect that postsecondary education will result in better employment and higher earnings. However, to acquire this education, students must find the necessary financial resources. In Canada, paying for postsecondary education has always been a responsibility shared by society through tax dollars, and by parents and children through personal savings. Since 1980, tuition fees have grown by 115%, while average family income has risen by only 1% (after adjusting for inflation). The result is increased pressure on families to find ways to pay for postsecondary education. Government student loans provide one way for young people to invest in their future.

Although student loans provide essential financial help for many, they are not without risk. Much concern has been expressed about student debt levels and whether the growing dependence on loans is creating serious problems for borrowers and for society. Are students defaulting on loans, particularly if they are unable to find well-paying jobs after graduation? Do prospects of heavy debt discourage some students from enrolling in postsecondary programs or cause them to drop out before they reach their educational goals? Another concern is how a high debt load may affect students' post-graduation plans. Do they modify future educational plans, or decisions about buying a home or a car, or starting a family.¹ Using data from the National Graduates Survey of 1995 Graduates (NGS), this article examines the extent of indebtedness, the repayment record and the impact of high debt on postsecondary graduates who used government loans to help finance their studies.

Employment earnings and student loans are primary sources of funding

When asked how they had financed their education, both college and bachelor's graduates most frequently identified

1. Choy, Susan P., Sonya Geis and C. Dennis Carroll. 1997. Early Labor Force Experiences and Debt Burden. National Center for Education Statistics, Report 97-286, Washington, D.C.

CST What you should know about this study

During the summer of 1997, Statistics Canada, in partnership with Human Resources Development Canada (HRDC), interviewed nearly 43,000 people in the National Graduates Survey of 1995 Graduates (NGS). This sample represented over 295,000 Canadian residents who had graduated from trade/vocational, college and university programs during 1995. The survey focussed on the education, training and labour market experiences of these graduates during the two years immediately following graduation. Graduates were also asked about how they financed their education, the extent of any student loans, scholarships, bursaries and if they had difficulties repaying their student loans. In addition, the survey asked about how much graduates owed to government student loan programs at graduation in 1995, and at the time of the interview in June 1997. Graduates were also asked about the amount they owed to other sources.

The results presented in this article are for college graduates (community college and similar institutions) and for graduates of bachelor's degree programs. Undergraduate certificates and diplomas, and first professional degrees (e.g., medicine, dentistry, veterinary medicine and law) are excluded from the bachelor's degree group.

employment earnings (59% college, 69% bachelor's) and student loan programs (41% college, 42% bachelor's) as primary sources of funds. Parents ranked a close third for bachelor's graduates. Scholarships, fellowships, prizes, grants and bursaries were rarely identified as a significant source of funding.²

Students from families with lower parental education more likely to borrow

Government student loan programs were designed to allow students of limited financial means to acquire postsecondary education. Student loan eligibility is assessed based on students' living arrangements, education and living costs, and the financial resources available to the student, including parental income and contributions. Using parents' education as a

1995 grads owed between 130% and 140% more to student loan programs than 1982 graduates.

proxy for socioeconomic well-being (since parental income is not available from the NGS), it is clear that graduates whose father had not completed high school were more likely to use government student loans than those whose father had a university degree. However, while the use of student loans decreased with parental education, the use of other types of loans (personal loans, loans from relatives, credit cards) increased.

Compared with the class of 1982, college and bachelor's graduates from the class of 1995 owed between 130% and 140% more to government student loan programs at graduation (after adjusting for inflation). On average, the 1995 graduates owed \$9,600 (college) and \$13,300 (bachelor's) when they graduated.

Averages, however, don't tell the complete story. While some borrowers (7% of college and 22% of bachelor's) owed more than \$20,000 at graduation, others (21% of college and 14% of bachelor's) owed less than \$5,000. With these widely varying amounts, graduates face different pressures to find a good job and begin repayments.

2. Scholarships, fellowships, awards and prizes were a much more common way of financing education among first professional (14%), master's (23%) and doctoral (59%) graduates.

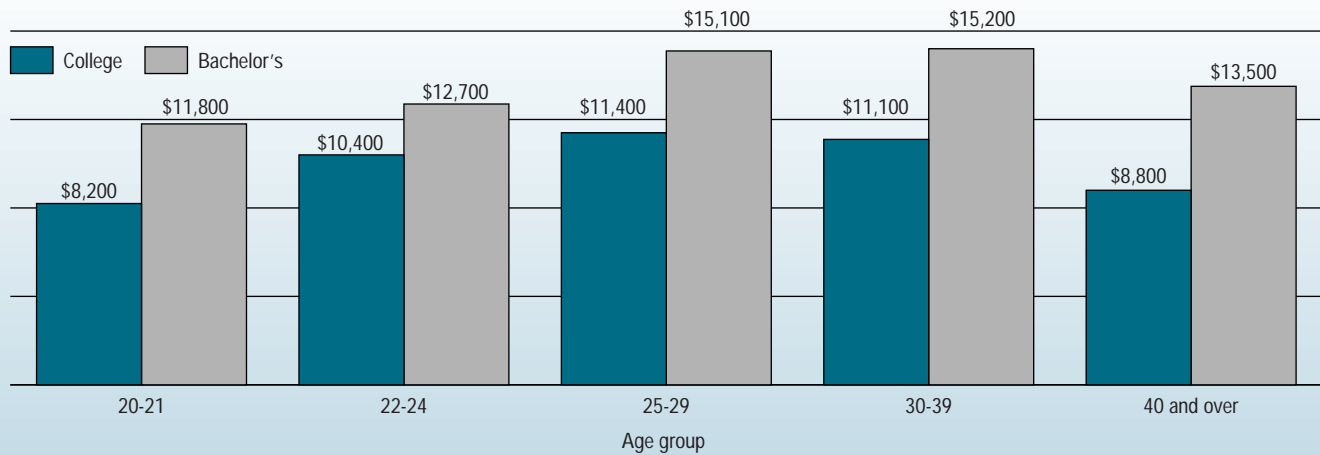
| Education of father ¹ | College | | Bachelor's | |
|---|--|---|--|---|
| | % who borrowed from student loans programs | Average amount owed to student loan programs at graduation (\$) | % who borrowed from student loans programs | Average amount owed to student loan programs at graduation (\$) |
| Total | 46 | 9,600 | 50 | 13,300 |
| Less than high school | 48 | 9,600 | 56 | 14,600 |
| Completed high school | 44 | 10,000 | 54 | 13,500 |
| Some postsecondary | 49 | 9,600 | 52 | 13,000 |
| Trade/vocational certificate or diploma | 48 | 9,000 | 55 | 12,900 |
| College certificate or diploma | 49 | 8,700 | 54 | 12,400 |
| Bachelor's degree | 40 | 9,300 | 44 | 12,100 |
| First professional | 44 ² | 10,300 ² | 34 | 13,300 |
| Master's or doctoral degree | 38 | -- | 43 | 11,500 |
| Not reported | 53 | 9,200 | 48 | 16,700 |

-- Amount too small to be expressed.

1. A similar relationship exists between loan use and mother's education.

2. High sampling variability.

Source: Statistics Canada, National Graduates Survey, 1997.



Source: Statistics Canada, National Graduates Survey, 1997.

The class of 1995 is taking longer to repay student loans

| | Year of graduation | | | |
|--|--------------------|--------|--------|--------|
| | 1982 | 1986 | 1990 | 1995 |
| Average amount owed at graduation (1995 \$) | | | | |
| College | 4,000 | 6,200 | 6,700 | 9,600 |
| Bachelor's | 5,800 | 9,000 | 9,700 | 13,300 |
| First professional | 9,500 | 13,700 | 14,600 | 21,100 |
| Master's | 6,700 | 8,500 | 10,000 | 13,700 |
| Doctorate | 5,400 | 6,900 | 9,500 | 12,900 |
| Average amount owed two years after graduation (1997 \$) | | | | |
| College | -- | 3,400 | 4,400 | 7,700 |
| Bachelor's | -- | 5,400 | 7,100 | 11,000 |
| First professional | -- | 8,000 | 10,800 | 16,600 |
| Master's | -- | 4,600 | 6,700 | 10,000 |
| Doctorate | -- | 2,700 | 4,700 | 7,800 |
| Average reduction in loans between graduation and two years later (%) | | | | |
| College | -- | 45 | 35 | 19 |
| Bachelor's | -- | 40 | 27 | 17 |
| First professional | -- | 42 | 26 | 21 |
| Master's | -- | 45 | 33 | 27 |
| Doctorate | -- | 60 | 50 | 39 |

-- Amount too small to be expressed.

Source: Statistics Canada, National Graduates Survey.

Age of graduates also appears to influence borrowing patterns. For example, graduates aged 25 to 29 were more likely to borrow and owed larger amounts than others. While younger graduates may rely on their parents for financial help, many of those over age 30 had a career prior to entry into the program and studied part-time. With help from parents and income from a steady job, both younger and older graduates relied less on government student loans to finance their education.

Class of 1995 slower at repaying student loans

Borrowers are not required to begin repaying their student loans if they continue studying full-time after they graduate. Although not necessarily full-time, 31% of college and 45% of bachelor's graduates were back in school after their "first" graduation in 1995. It is therefore not surprising that as of June 1997, 17% of college and 23% of bachelor's borrowers were not making payments on their loans. In fact, 11% of college and 16% of bachelor's borrowers owed more two years later than they had at graduation.

Other borrowers don't make payments because they are having financial

difficulty. On average, 1995 college and bachelor's graduates had repaid less in the two years after graduation than had the class of 1990. While 1995 college graduates had repaid only 19% of their loans by 1997, 1990 college graduates had paid off 35% by 1992. Similarly, 1995 bachelor's grads repaid 17% compared with 27% paid off by their 1990 counterparts. This means that 1995 graduates will probably repay their loans over a longer period than previous borrowers. Several reasons may underlie the slower rate of repayment: pursuing further studies after graduation; inability to find a well-paying job; or lower interest rates which may encourage people to pay off their loans more slowly.

Will 1995 graduates pay off their student loans?

Although the debt burden of graduates has increased substantially, about 41% of college and 32% of bachelor's graduates had either already paid off their loans or expected

to pay them off before 2001. However, about another 40% did not know when their loans would be repaid in full.

In fact during the two years following graduation, one-sixth of 1995 college and bachelor's borrowers indicated they were already having difficulty making payments on their government student loans. Only about one-third of these borrowers received assistance from government or other lenders, such as the federal government's Interest Relief Program. This program suspends principal payments and assumes graduates' interest payments when their income falls below a specified threshold. As a last resort, graduates may default on their loans. Indeed, some 4% of 1995 borrowers had defaulted by 1997.

The two most significant factors contributing to loan repayment difficulties were the size of the loan and income after graduation. For example, only 8% of bachelor's graduates with a loan of less than \$2,000 had difficulty

CST Canada Student Loans Program

Human Resources Development Canada estimated that in 1996, the typical living costs for an eight-month college or university program were between \$10,000 and \$13,000 for students living away from home, and between \$3,400 and \$6,400 for students living at home with their parents. Based on these estimates, the cost of a four-year program can exceed \$50,000 for someone living away from home and \$25,000 for a student living at home.¹

The Canada Student Loans Program (CSLP) allows eligible Canadian citizens and permanent residents to finance their postsecondary education with government-sponsored loans.² Full-time students in a program lasting at least 12 weeks may qualify for a loan based on the costs of their program and on the financial resources available to them. For 1997-98, the CSLP provided funding to meet 60% of a student's assessed need for the period of enrolment (up to a maximum of \$165 per week). Part-time students may also qualify for a loan if their family income is below a specified threshold (based on the number of people in the family). The CSLP can be supplemented with provincial student loan programs.

The 1998 federal budget introduced several improvements to the Canada Student Loans Program. Under the CSLP, the government pays interest on the loan while the borrower is in school. Interest accrues after graduation, but payments are not required for six months; after this grace period,

the borrower is responsible for paying off the loan, usually over the next 9 1/2 years. For those facing financial difficulties, the federal government may pay the interest for a maximum of 30 months after the borrower has left school (extended from 18 months); also during this time, the borrower need not make payments on the principal.

The 1998 budget also introduced a 17% federal tax credit on the interest portion of payments for both federal and provincial student loans. Income thresholds for interest relief were raised, and in 1999, partial interest relief will be available for those with higher incomes. For borrowers who have used all of their interest relief, the loan repayment schedule may be extended to 15 years and interest relief to 54 months. For those who still have financial difficulty at least five years after their studies, the government may reduce the loan principal if payments exceed a certain percentage of income.³

1. Human Resources Development Canada. "The costs of post-secondary education." http://www.hrdc-drhc.gc.ca/student_loans/engraph/content/cost.html.

2. Quebec and the Northwest Territories operate their own student assistance plans and receive other payments from the federal government.

3. Finance Canada. "Budget 1998 – Building Canada for the 21st Century – The Canadian Opportunities Strategy: Helping Manage Student Debt." Ottawa. <http://www.fin.gc.ca/budget98/pamphe/studpae.html>.

repaying, compared with 34% of those with loans of \$30,000 or more. Similarly, those with incomes below \$30,000 had nearly three times as much difficulty repaying their loan as graduates with incomes over \$50,000 (21% versus 8%).

Stable employment also played a significant role in repaying loans. Not surprisingly, those with longer term jobs were less likely to find making repayments difficult. While 19% of those who had been in their job for less than six months as of June 1997 had difficulty repaying, this was true for only 12% of those who had held their job for two or three years. However, bachelor's borrowers who had job tenure beyond three years were equally likely to have loan repayment difficulties as borrowers with less than 6 months in the same job (19%). Not surprisingly, unemployed borrowers had

more difficulty repaying their student loans than those working full-time; one-quarter of unemployed borrowers versus one-sixth of borrowers working full-time had difficulty repaying.

Women university graduates had more trouble repaying student loans

Women were more likely than men to experience difficulties repaying their loans. At the bachelor's level, 20% of women experienced difficulties compared with 15% of men. This discrepancy may be due to the fact that women borrowed, on average, about \$1,000 more than men and that their incomes were approximately \$3,700 less than men's in 1996. In contrast, women and men who graduated from college experienced only marginal differences in repayment difficulties.

Difficulty in repaying loans varied from province to province. In New Brunswick and Newfoundland, 23% of bachelor's graduates reported having trouble paying down their loans. In contrast, bachelor's graduates from Quebec, where undergraduate tuition fees were the lowest in the country, were least likely to report difficulties (14%). Quebec graduates also had one of the lowest debt levels at graduation (\$11,600 in student loans) while those in Saskatchewan had the highest (\$16,200).

Summary

The class of 1995 borrowed more from student loan programs than any group of graduates in the previous 15 years. Because their earnings did not keep pace with these increasingly large loans, many graduates experienced repayment difficulties. Within two years of graduation, one in 20 borrowers ended up defaulting on their loan. Yet for every member of the class of 1995 who had defaulted, there were five or six who had repaid their loan within two years of graduation.

CST Student loans in the United States

As in Canada, tuition in the United States has increased much more quickly than family incomes. Between 1980-81 and 1995-96, tuition fees climbed by more than 90%, while family incomes grew only 9% after accounting for inflation.¹ In 1995-96, 60% of graduates in American bachelor's programs had borrowed an average \$18,200 (Canadian dollars)² to finance their education. Among associate degree recipients (similar to Canadian community college graduates), 42% had borrowed an average of \$6,900 (Canadian dollars).³

In addition to student loans, about 10% of parents of graduates in 1995-96 borrowed from the U.S. Department of Education's PLUS program to help finance their children's education. Another study conducted by the University of Michigan indicated that 21% of borrowers using home equity lines of credit used some or all of those loans to finance education compared with 7% of borrowers using traditional equity loans.

1. The College Board. 1997. *Trends in Student Aid: 1987 to 1997*, Washington, D.C.
2. Canadian dollars were calculated based on the May 1996 exchange rate of \$1.369 CDN = \$1 U.S.
3. United States General Accounting Office. "Students have increased borrowing and working to help pay higher tuition fees." Washington, D.C., GAO/HEHS-98-63, p.6.

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Warren Clark is an analyst with *Canadian Social Trends*.