**Centre for Global Higher Education: Empirical workshop topics**

**Understanding Student Loan Repayment Burdens**

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1. *Introduction*

Professors Bruce Chapman (ANU) and Lorraine Dearden (UCL), and Dr Dung Doan (ANU), are members of the CGHE and are in Project 2.5. What follows is an explanation of some of the empirical work we are currently engaged in that we would like to discuss on 10th April at our CGHE research workshop.

 *2 Repayment Burdens: The basic concept*

Over the last 30 years international higher education financing reform has been underway which involves the adoption of income contingent loans (ICL), most often to replace the usual form of higher education financing involving time-based repayment loans (TBRL). The essential difference concerns debt collection: an ICL is repaid if and only when debtor’s income in a particular period exceeds a threshold level, but with a TBRL repayment obligations are set over a fixed period of time. ICL reform began in an international context in Australia in 1989, and ICLs have since been adopted in about 10 additional countries.

A very significant methodological and empirical focus of what we have been, and are currently, engaged in, relates to calculations associated with potential repayment difficulties for relatively low income student debtors in TBRL systems, such as those in, for example, the US, Canada and Colombia. This relates to the concept of a “repayment burden” (RB), which is measured as the proportion of a debtor’s earnings required to repay a student loan. RBs are critical to the policy debate concerning comparisons of ICL and TBRL, since for ICL this proportion is set by law. In Hungary, Australia, England, and New Zealand, for example, the maximum RB is six, eight, nine, and twelve percent of debtor’s earnings. However, since TBRLs require fixed repayments over a set period of time, RBs can vary widely among debtors as well as over a debtor’s lifetime simply because of earnings variation.

There are several reasons that RBs might be critical to the welfare of debtors. One is that high RBs must result in consumption hardship since at some point purchases of goods and services must be decreased or postponed in order to meet debt repayment obligations. A second and related concern is that even if income is high enough to accommodate the loan repayment obligation in a given period the possibility of future consumption hardship given an unanticipated fall in income would give rise to stress and anxiety. Finally, in the event of persistently very high RBs, some debtors will be forced to default on their loans and this results in a loss of credit reputation and thus future access to other commercial borrowings.

A burgeoning pool of research, much of it emanating directly or indirectly from the CGHE, has reported RBs under TBRLs in various countries and consistently reported that this traditional form of student loan creates excessive burdens to low-income debtors. Those in the bottom 20 percent of the graduate income distribution need about 40 percent to above 100 percent of their earnings to service their student debts in any given period. This has been found to be the case for example, in the US (Chapman and Dearden, 2017 and Barr *et al.*, 2017), Ireland (Chapman and Doris, 2017), Japan (Dearden and Nagase, 2017) and South Korea (Doan, 2017). Yet some puzzles arise in interpreting the RB experience of many countries’ loan systems, one being that since major repayment difficulties seem to be commonplace, why is it that loan defaults appear to be significantly lower than should be expected from our RB calculations? This is our major motivation in exploring the measurement and interpretation of contemporary RB calculations.

1. *Repayment Burdens: Implicit assumptions underlying contemporary calculations.*

Conventionally RBs are measured as:

$\frac{L\_{it}}{Y\_{it}}$ (1)

where $L\_{it}$ is the required repayment of student loan in period *t* for debtor *i*, and $Y\_{it}$is debtor *i*’s own labour income in period *t*. It is simple to calculate, easy to interpret, and free from bias of debtor’s subjective perceptions; it is a convenient tool to gauge the extent of potential difficulties associated with the burden to repay student debts. But its use and interpretation imposes some critical restrictive assumptions; it is in the relaxation of these assumptions that we seek to add value to the student loan policy debate.

We plan on exploring the limitations of RBs by raising issues related to both the numerator and denominator of equation (1). There are four basic limitations inherent in the use of (1) as a measure of the difficulty associated with repaying student debt: (i) the measure assumes that there are no within-household transfers of both debt obligations and income, (ii) the measure assumes that labor income is the only resource available for debt repayment, (iii) the measure ignores the fact that part of the debtor’s resources must be allocated to living costs, and, (iv) because the measure is a point-in-time calculation, no account is taken of dynamic forces specifically related to changes of income over time.

The issues to be examined relate to:

1. The relevance of per capita (or adult equivalent scale) and total household repayment burden to account for the intra-household allocation of resources and debt obligations within the household
2. The inclusion of non-labour sources of income
3. The inclusion of consumption expenditure to maintain debtor’s and their dependent’s living; and
4. Taking account of, and measuring, dynamic lifetime income processes.

Research has already begun in these areas (Dearden, 2017 and Doan, 2018) and we will take the opportunity at the workshop to report progress.

**References**

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