Cameron M. Weber

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"The Political Economy of Student Debt and Higher Learning in America"

The Federal Reserve Bank of New York found in July 2015 that over the last ten years college tuition has been growing at a rate more than twice that of inflation, and, that an increase in US government loan programs accounts for 65% of this tuition increase. This means that the average student debt is now $35,000 per person. Further the Federal Reserve Bank of Philadelphia finds that this debt has an "economically negative" effect on small businesses in the United States, which are 99% of all businesses in the United States.

We could postulate that the US government has purposefully put in place programs and policies which encourage debt-creation so that people need work in conventional jobs at large corporations so that we do not question the underlying crony-capitalist system in the United States through political entrepreneurship. In brief this crony-capitalism is the revolving door between central bankers, US Treasury Department officials and brokers (such as Goldman Sachs and the Bank of America) who have a monopoly on selling US government bonds for fees and a monopoly on money creation, taxation and nation-state debt creation.[i]

The US income tax code allows the write-off of debt interest payments before taxes which encourages debt creation, the US government guarantees mortgage-backed bonds, which encourages housing mortgage debt creation, the US government bails-out banks which can then give consumer credit to those that can't afford it, and this list goes on and on. However this conjecture is not refutable so we'll just take in at face value.

US government loan programs (the most common being below-market rate loans[ii]) mean that college seems more affordable to people who would not normally go to college absent these below-market loans.[iii] More students in college is not necessarily a good thing, some people may be better served by focusing on the trades and technical occupations and self-employment and self-determination. Increasing one's debt to attend college may not pay-off for those who might practice the crafts, or maybe more specifically, work for themselves in technical or craft or small business occupations not requiring the signal of an expensive college degree to potential employers.[iv]

When the US government intervenes into the market effecting the cost of higher learning, we find that demand shifts-out (the appendix contains supply and demand graphs which illustrate the narrative contained here). More people have preferences for a college education because the government programs are seen as a subsidy, and therefore those who were not be able to afford a college degree now believe that they are able to do so. This shift-out of demand means that more people are willing and able to attend college, and, the shift in demand also raises the price of tuition, which we know has increased at a greater pace than have inflation and income (which has mostly been stagnant, except for the crony-capitalists, since the financial crisis of 2008). Because of the intervention more people attend college and at a higher price had there not been the intervention. What is more is that this higher tuition often takes shape as debt.

The key to reducing student debt, and reducing tuition, is not to give "haircuts" on student debt which will just increase demand for student debt[v], but rather to remove the incentives for creating this debt in the first place by defunding the US Department of Education's loan portfolio. Furthermore, a cynic might say that the reason the federal government creates incentives for people to borrow money to attend an institution of higher learning that they cannot afford, and relatedly to buy houses that they cannot afford, is so that indebted people work in establishment occupations nine-to-five to pay off debt, instead of questioning the underlying crony-capitalist nature of the American enterprise system, something we saw quite abit of during the bailouts of bankrupt banks and businesses after the 2008 financial crisis.

We can call this crony-capitalism "socialized risk and private profit," debt helps feed this corrupt system. Removing the income tax deduction on debt interest payments is also necessary to reduce the debt financialization of the economy and to reduce status quo cronyism.

References

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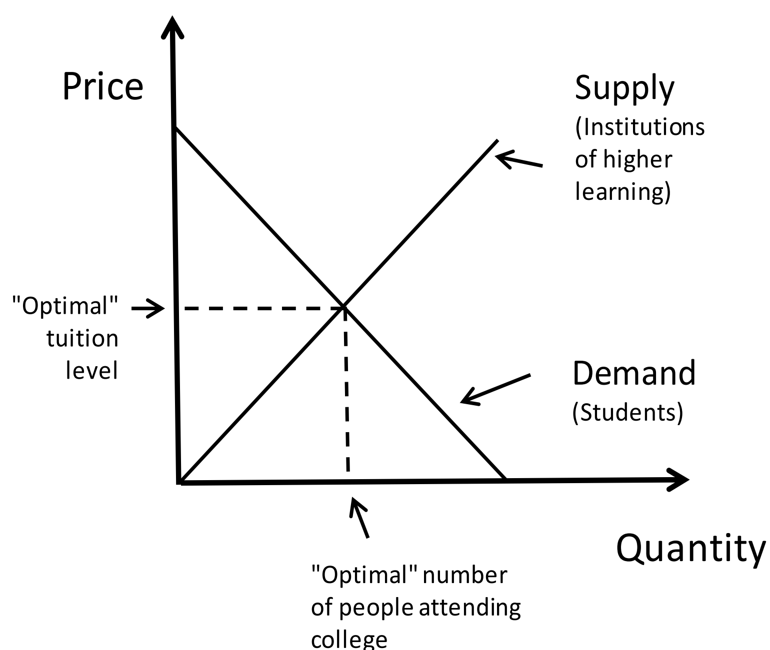
Richard Arum and Josipa Roksa (2014). *Aspiring Adults Adrift: Tentative Transitions of College Graduates*, University of Chicago Press.

Phoebe Hoban (2010). *Alice Neel: The Art of Not Sitting Pretty*, NY: St. Martin's Press.

David O. Lucca, Taylor Nadauld, and Karen Shen (2015). "Credit Supply and the Rise in College Tuition: Evidence from the Expansion in Federal Student Aid Programs," Federal Reserve Bank of New York.

Appendix

Illustration 1: The Market for Higher Learning in America

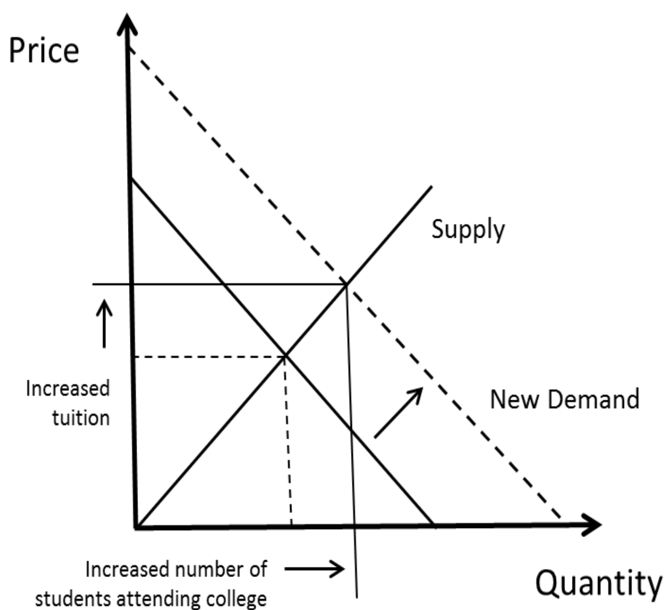


In Illustration 1 we find the Supply and Demand graph for higher learning in America. Demand is downward sloping, people are willing to buy more as the price goes down. Supply is upward

sloping, people are willing to sell more when the price goes up. What emerges then from this market interaction is the "optimal" price and quantity as institutions of higher learning compete to cooperate with students, and students compete with each other to cooperate with institutions of higher learning (optimality in economics is the emerged price and quantity which maximizes consumer and producer surplus, which is by definition what market interaction does absent monopoly power). We might know that each transaction (the student and institutional relationships) may be unique, we also know that models by definition abstract from reality, the point is to help explain the underlying logic of human economic exchange.

In Illustration 2 we examine what happens when the government intervenes into the (idealized and abstracted) market for higher learning in America. We see the emergent higher tuition price and higher number of people attending college due to the US government loan program subsidy shifting-out demand.

Illustration 2: Consequences of Government Debt-based Tuition Programs in the Market for Higher Education in America



[i] Hank Paulsen who was George W. Bush's treasury secretary allowed Lehman Brothers to fail while bailing AIG. Prior to being at the Treasury Paulsen was the Goldman Sachs partner in charge of the China desk. The Peoples Bank of China owns more than $1 trillion in US government and US government-guaranteed debt, Lehman was a competitor to Goldman and AIG owed Goldman a lot of money. Timothy Geithner, who was Barak Obama's treasury chief was previously the President of the New York Federal Reserve Bank. The Obama administration nationalized the bankrupt General Motors and gave equity ownership to the United Auto Workers. The UAW are big donors to the Democrat Party.

[ii] The NY Fed also finds that Pell Grants to the poor have less of an effect on tuition raises than do below market loans for tuition. However Phoebe Hoban tells the story of how when Alice Neel was working for the US government art project in the 1930s (which is when government-encouraged debt creation kicked into high gear with housing mortgage programs) Neel would hide her phone and radio when the officials came to make sure she wasn't making too much money to stay employed with the government.

[iii] The US Department of Education certifies which colleges are able to offer government loan programs, this creates monopolist competition giving higher education institutions significant leeway in how to price tuition.

[iv] Arum and Roksa (2014) find that the US economy is overly-credentialed, more college graduates are working at minimum wage retail positions crowding-out employment for the working poor.

[v] See for example, "Government to Expand Program to Forgive Student Loan Debt," by Stephanie Saul in the New York Times, November 18, 2015.