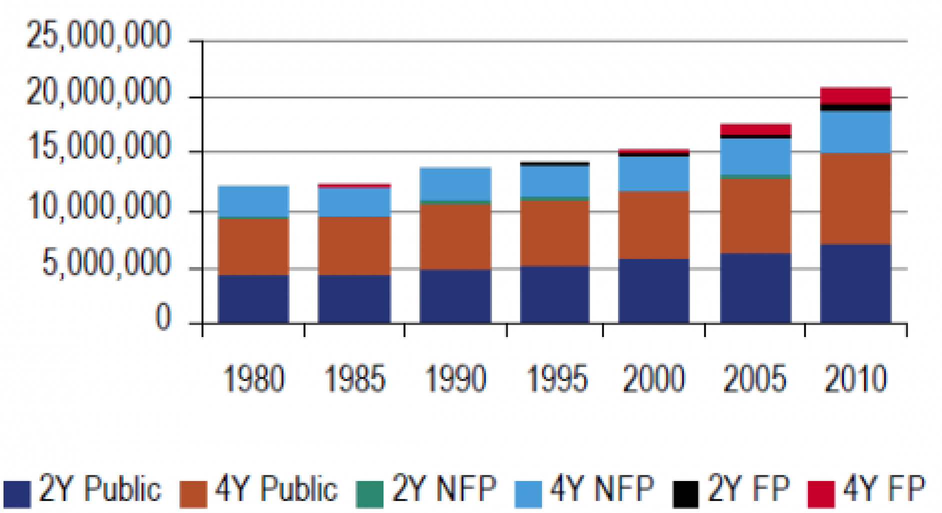
The Student Loan Bubble In 19 Simple Charts

A picture paints a thousand words but in the case of the world of college education (and its surrounding income, unemployment, debt burden, and pricing implications), we decided 19 charts was the simplest way to explain the path to debt servitude that an increasing share of the US population is taking - despite record delinquencies, falling real incomes for graduates, stagnant graduate employment, and rising college costs. As BofAML notes, the **cost of higher education has continued to climb, fueled by debt and government aid**. Over the past twenty years, tuition growth exceeded the average rate of inflation by nearly 3% annually, while both grant aid and Federal loans per full-time undergraduate exceeded by about 5% annually. **This trend is not sustainable, in our view.** The challenging labor market, which has left the youth population underemployed and underpaid, has put the spotlight on the burden of student debt. We expect a correction in the price of tuition and reduction in debt. There will likely be lasting effects on the economy from the high cost of education and large debt burden. **Graduating during a recession leads to permanently lower earnings growth, making it that much harder to service the debt burden.**

Enrollment in college has never been higher...

Chart 25: Fall enrollment in degree-granting institutions by control and level of institution (# of students)



Source: The Department of Education. Control refers to public or private. Level refers to program length

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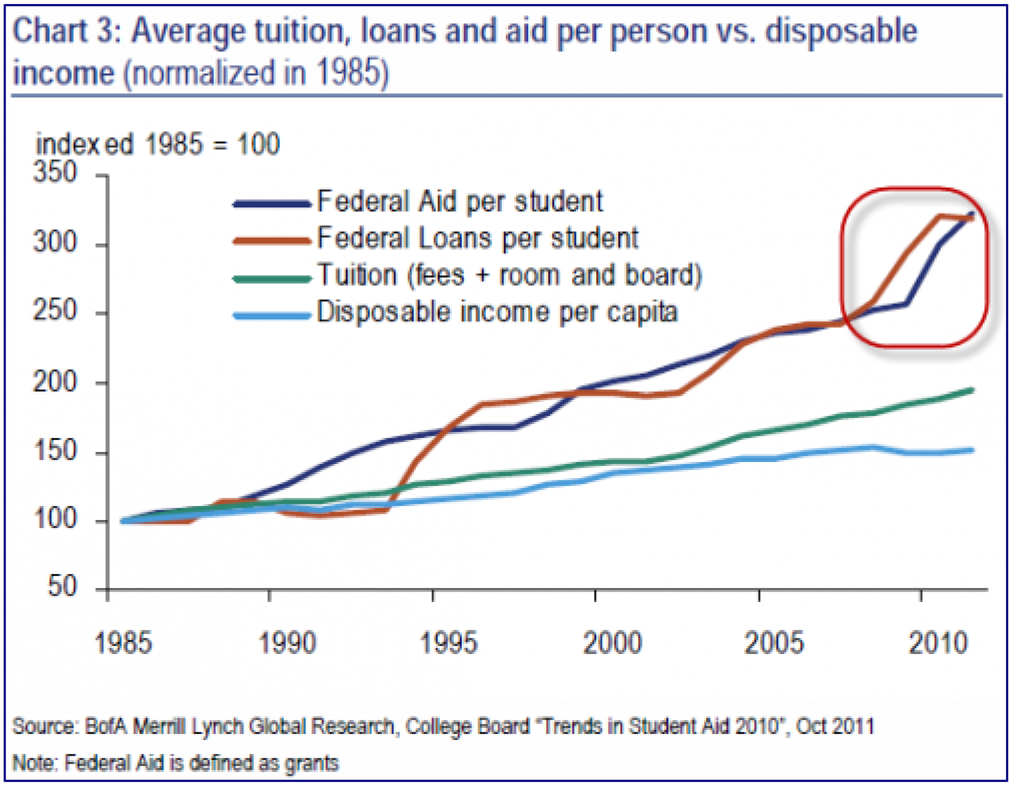
Which appears to have spurred a post-Lehman jump in Federal Aid and Loans...



And sure enough - Student debt has taken over the 'debt' lead from credit card and auto debt...

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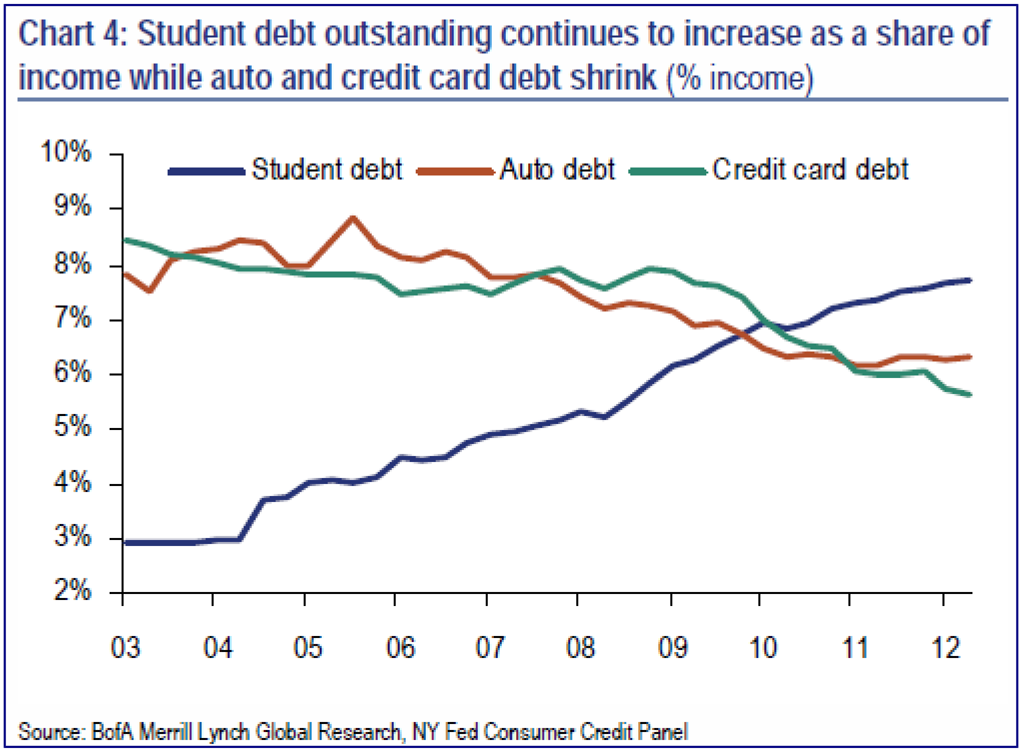

And as with every credit-fueled bubble - this has inflated the price of the good or service...

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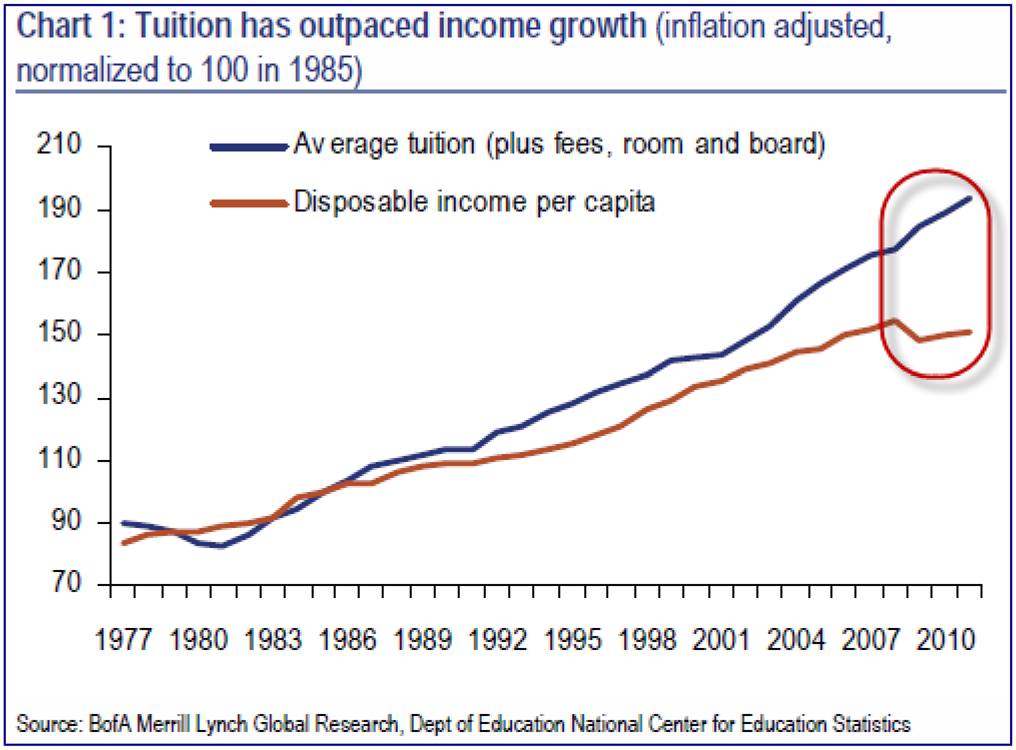

Chart 1: Tuition has outpaced income growth (inflation adjusted, normalized to 100 in 1985)

Source: BofA Merrill Lynch Global Research, Dept of Education National Center for Education Statistics

But has NOT benefited the 'student' in reality as **real income of college grads has fallen just as fast as high school grads since 2007**...

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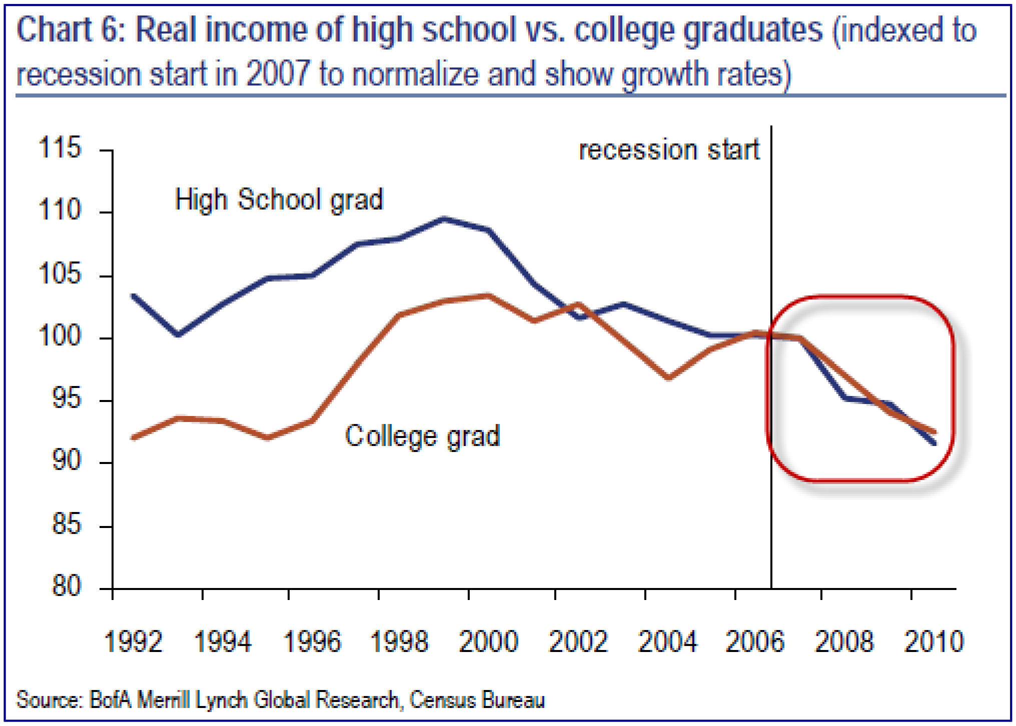

Chart 6: Real income of high school vs. college graduates (indexed to recession start in 2007 to normalize and show growth rates)

Source: BofA Merrill Lynch Global Research, Census Bureau

...though over a longer period - **an extended academic career has paid off (so more college and more debt is better?)**...

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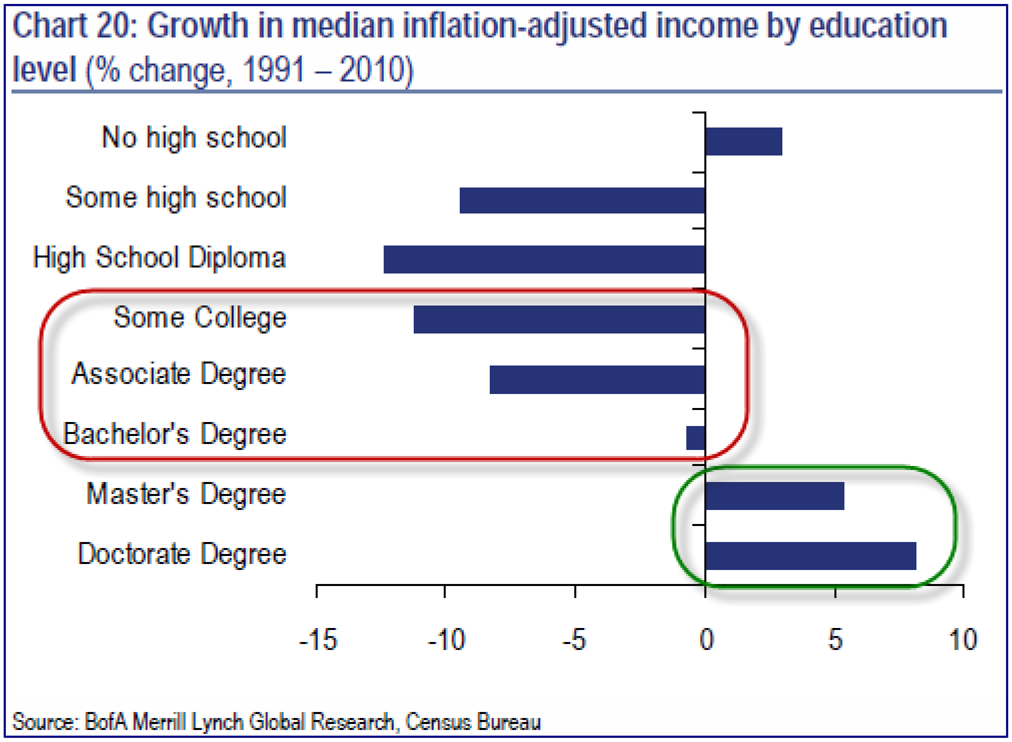

of course, **corporations have been quick to recognize the money flow and degree granting institutions have risen dramatically**...

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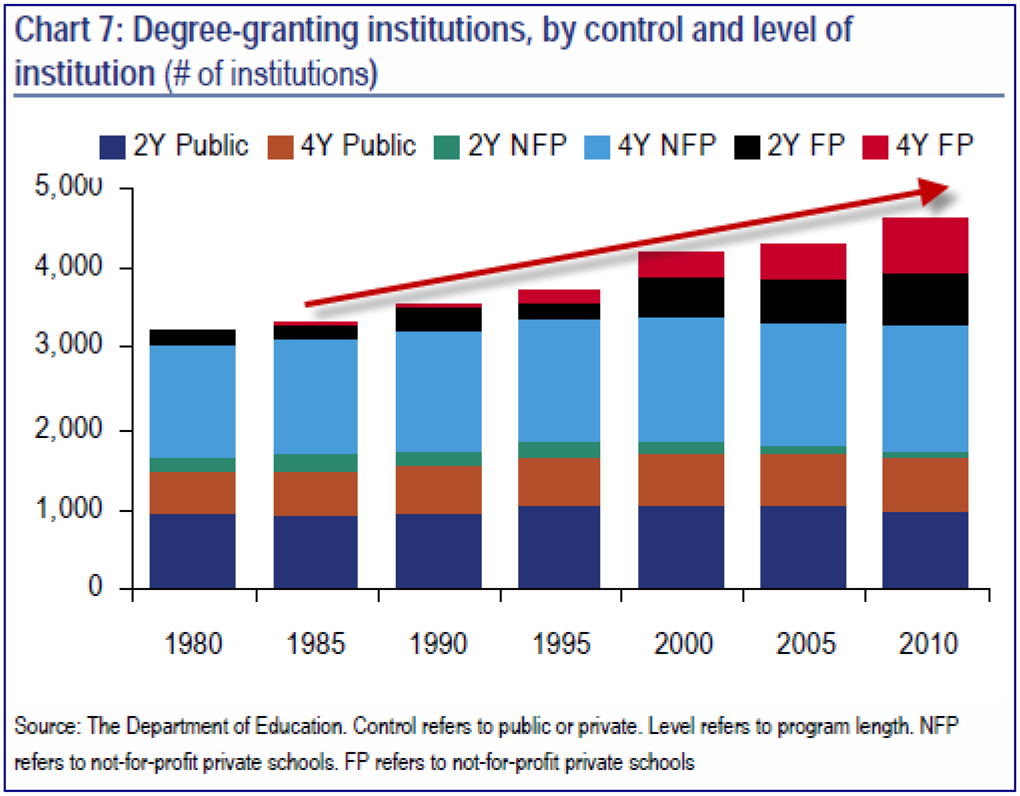
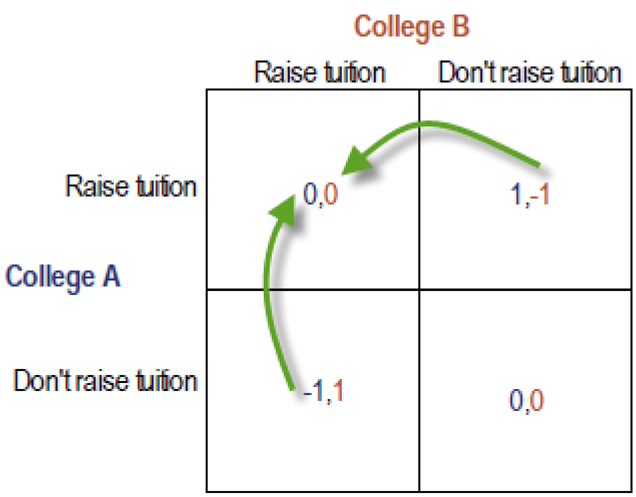


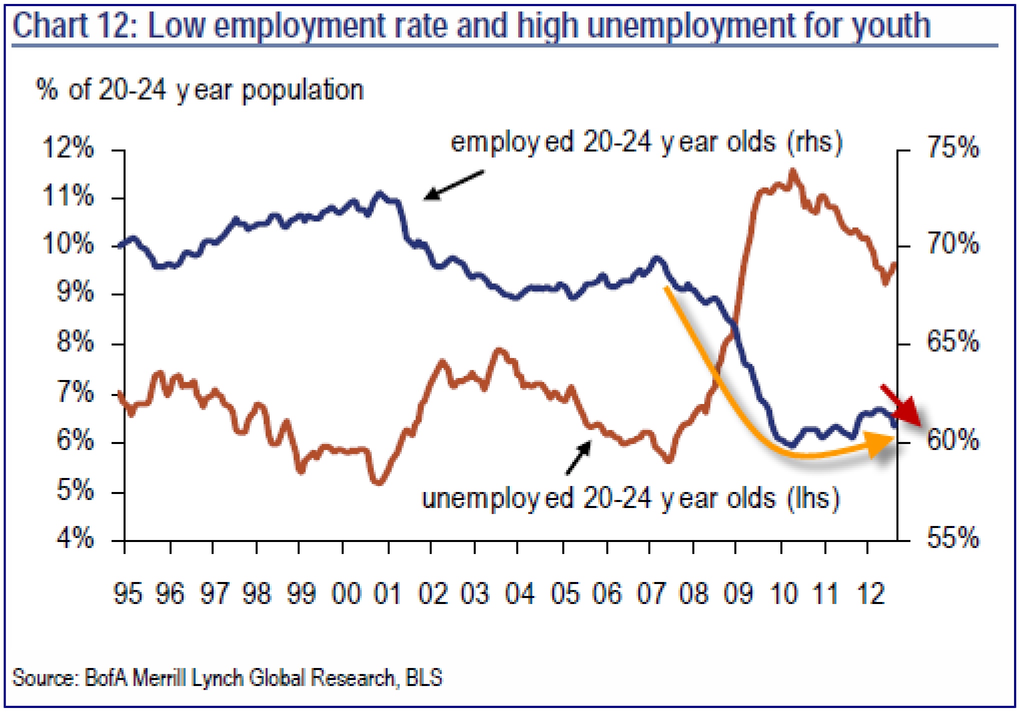
and the money flows to best ranked schools - which **incentivizes raising fees in a 'Prisoner's dilemma' world...** ***(dominant strategy is to raise tuition - as indicated by the green arrows)***

Chart 8: Prisoner's dilemma for college tuition: optimal outcome is for both colleges to raise tuition



Source: Gillen, Andrew. "Introducing Bennett Hypothesis 2.0." Center for College Affordability and Productivity, February 2012, BofA Merrill Lynch Global Research

So while firms are doing well, **the 'product' they are selling is not helping as employment remains low for 20-24 year olds**...



and **young adults are increasingly leaving the workforce in a hurry**...

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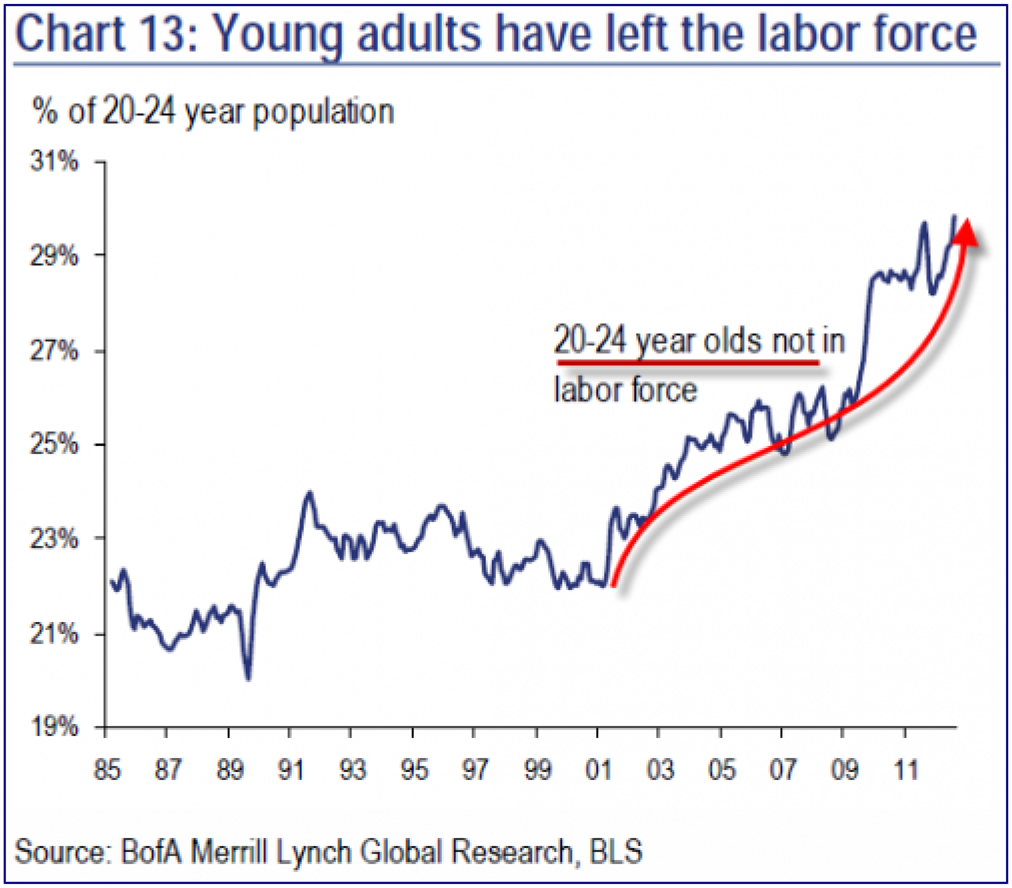

or **taking part-time jobs**...

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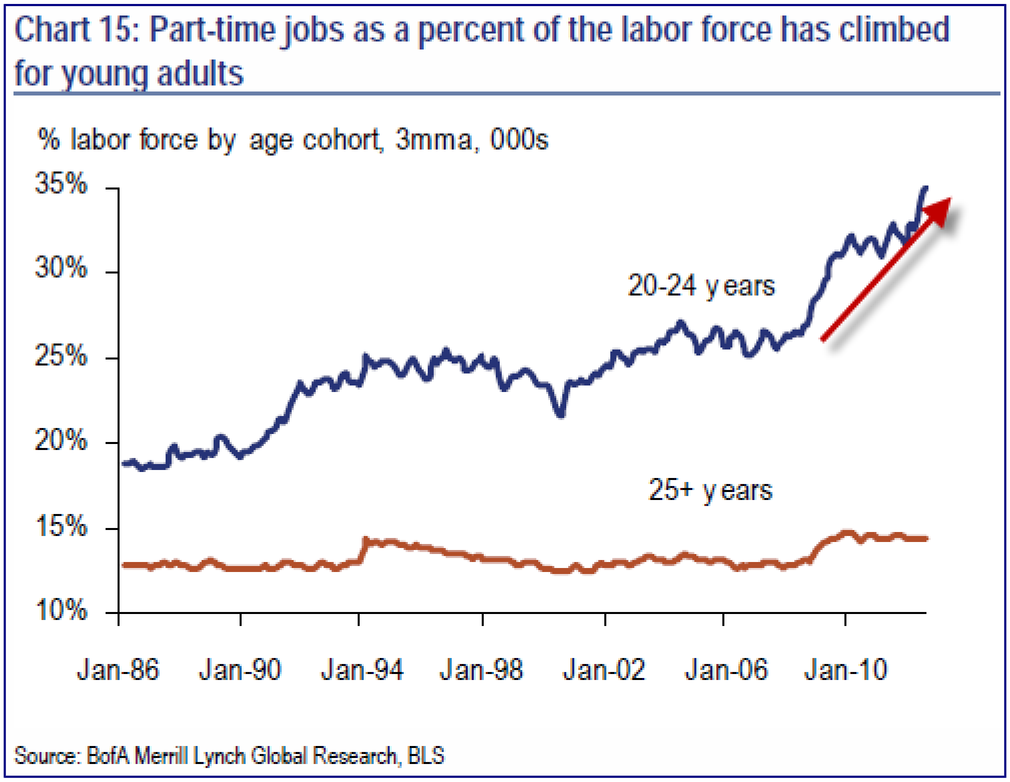

leaving the burden back on the parents...

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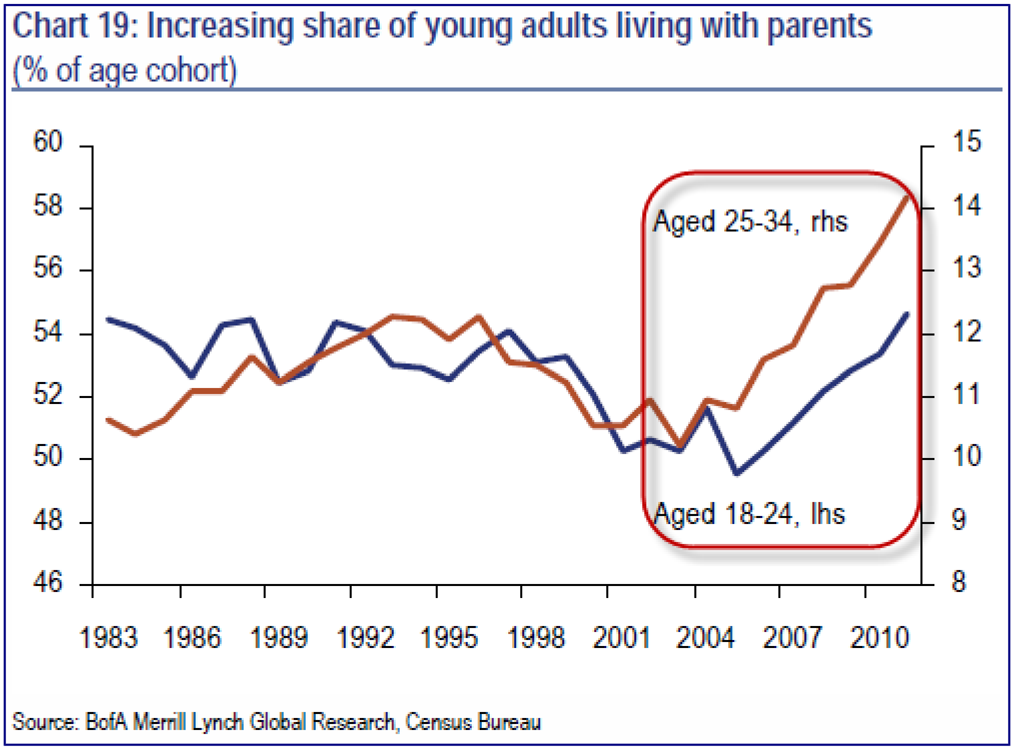

but the **jobs that are expected to grow are the low-paying jobs**...

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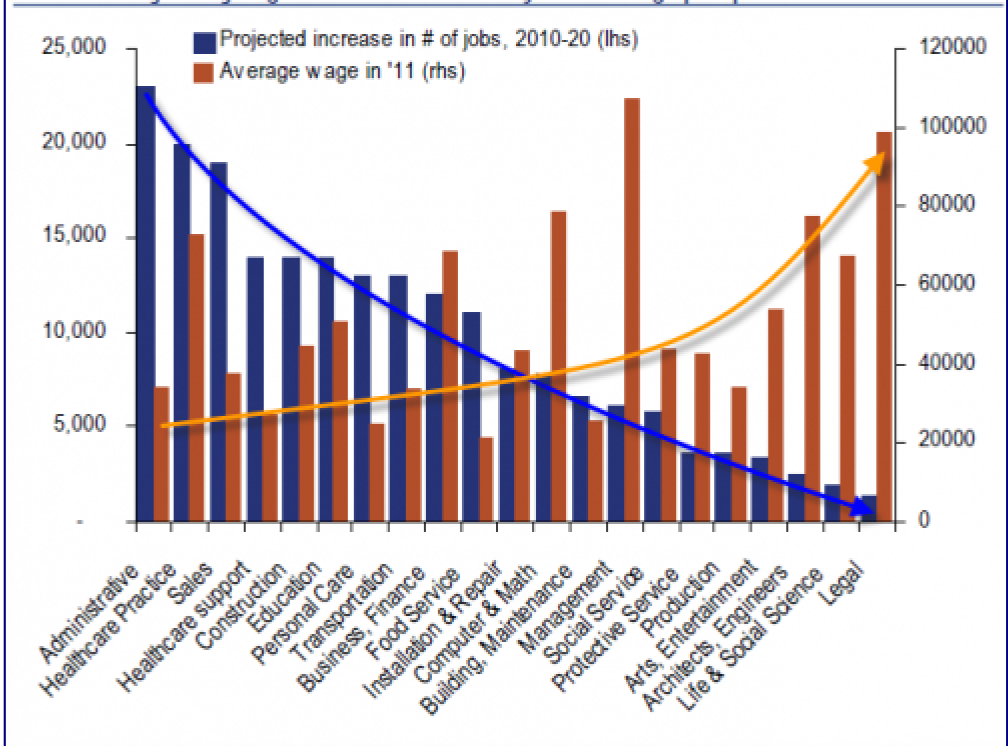
Chart 22: Projected job growth over the next 10 year and wage prospects



Source: BofA Merrill Lynch Global Research, BLS Occupational Handbook

But **what will change after the election** - especially for the for-profit education companies...

Table 6: BofAML's views around various election outcomes on for-profit education companies

	Republican Sweep	R President; Split Congress	R President; D Congress	D President; R Congress	D President; Split Congress	Democratic Sweep
Regulatory environment	Improves	Improves	Improves	Remains negative	Remains negative	Remains negative/worsens
Federal financial aid	Greatest likelihood for cuts (Pell, subsidized loans)	Funding likely maintained or cut	Funding likely maintained	Funding likely maintained	Funding likely maintained	Greatest likelihood for increases
90/10*	Greatest likelihood for easing	Likely no change (split Congress), though greater chance of easing with R President.	Congress might try to make 90/10 more restrictive. President could try to block	Congress might try to make 90/10 less restrictive, which the President could try to block	Likely no change (split Congress). Greater chance of more restrictive with D President.	Greatest likelihood 90/10 gets more restrictive
Legislation (comments here focus on changes for for-profits vs. funding levels)	HEA likely reauthorized more rapidly; outcomes for for-profits incrementally positive	HEA reauthorization takes longer (split Congress). R's will block negative legislation, but D's will try to block positive changes.	HEA reauthorization could move faster. D's try for negative legislation. R President could try to block.	HEA reauthorization could move more rapidly. R's could try for positive legislation. D President could try to block.	HEA reauthorization takes longer (split Congress). Greater likelihood for negative legislation that R's would try to block.	HEA likely reauthorized more rapidly; outcomes for for-profits much more negative

Source: BofAML Global Research. *For-profits cannot receive more than 90% of revenue from federal financial aid. If they exceed the limit for 2 straight years, they risk losing access to federal financial aid.

As the **government provides an increasing share of the massive student loan market...**

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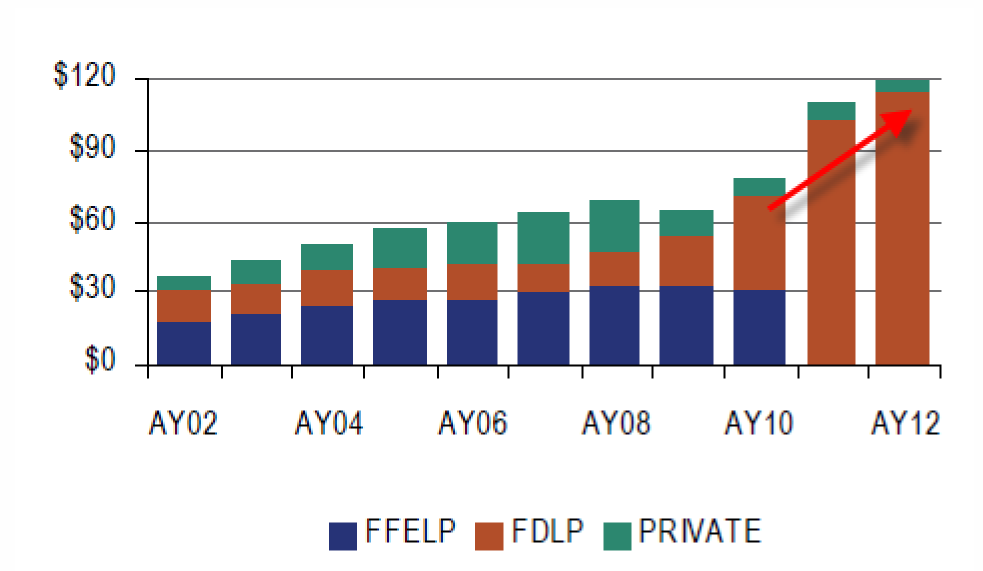
Chart 30: New loan volume by student loan type ($ billions)



Source: The Department of Education, BofA Merrill Lynch Global Research. FFELP loans are ultimately guaranteed by Federal government and owned by private lenders, FDLP loans are owned by the Federal government and private student loans have no Federal guarantee and owned by private lenders.

leaving the student burdened with government loans...

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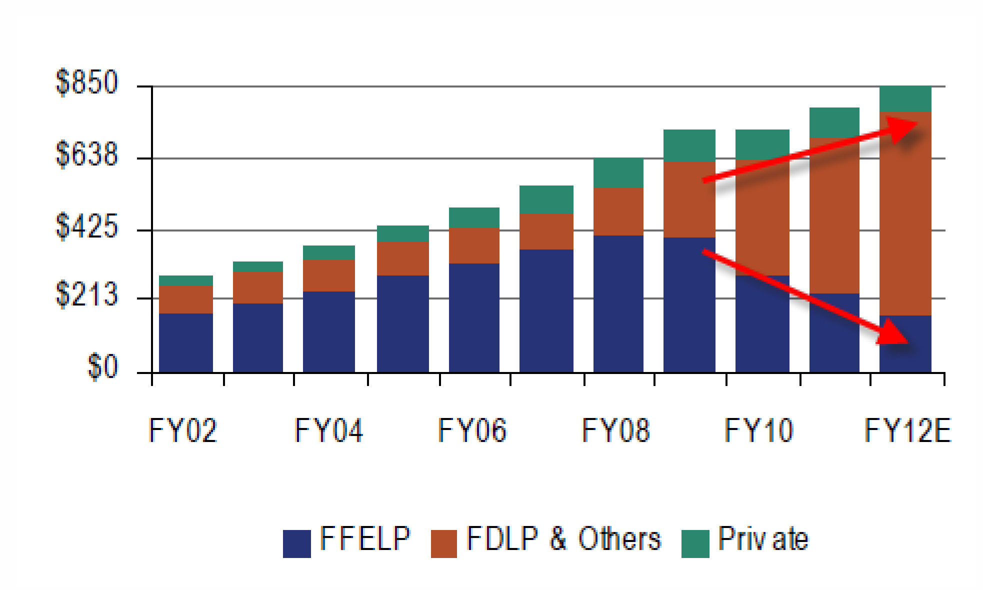
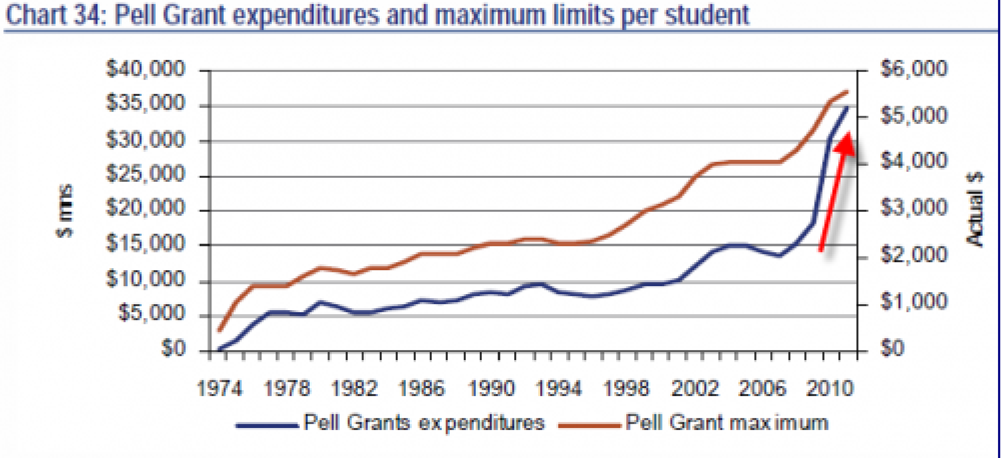
Chart 31: Outstandings debt by student loan type ($ billions)



Source: The Department of Education, BofA Merrill Lynch Global Research. FFELP loans are ultimately guaranteed by Federal government and owned by private lenders, FDLP loans are owned by the Federal government and private student loans have no Federal guarantee and owned by private lenders.

as even the **lowest income grads are getting assistance in record amounts via Pell Grants**...

Chart 34: Pell Grant expenditures and maximum limits per student



Source: Department of Education. College Board. Expenditures are represented in constant dollars

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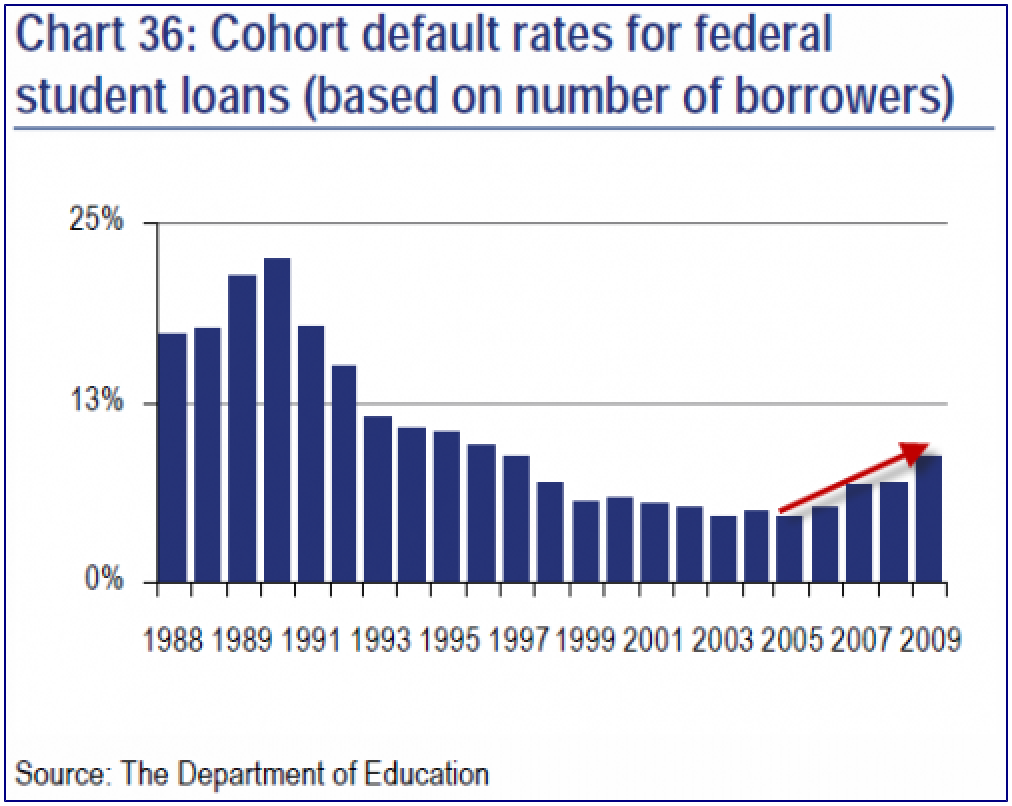
but **delinquencies are rising**...



at record rates...

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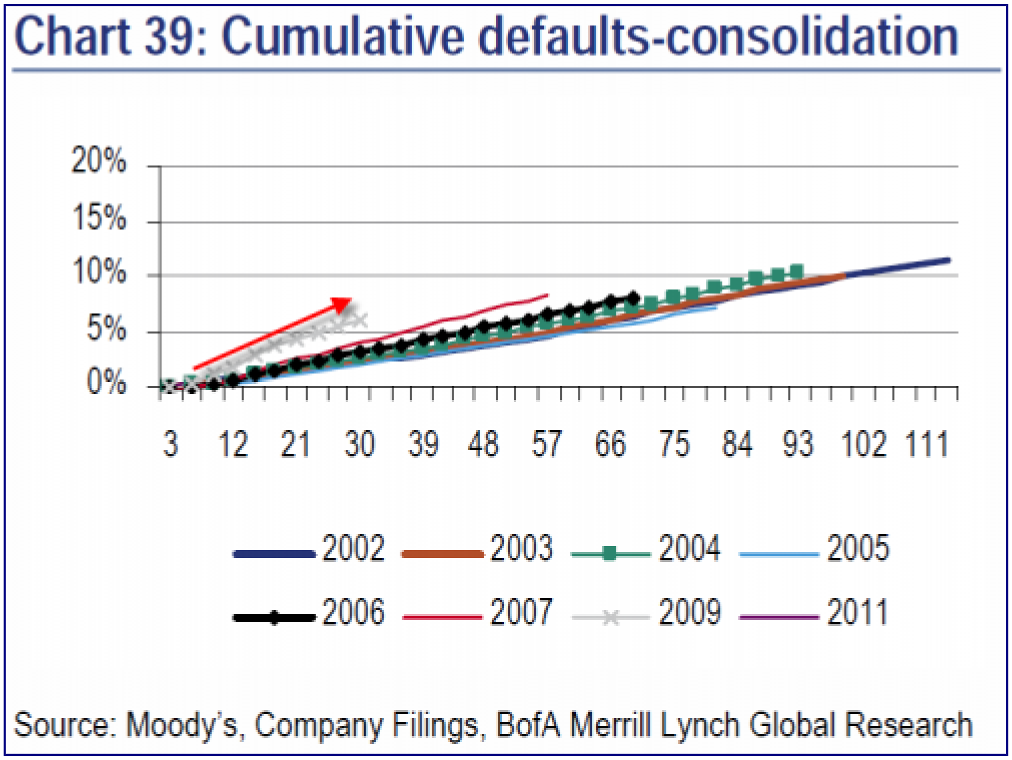

There will likely be lasting effects on the economy from the high cost of education and large debt burden. About 68% of students in private four-year schools have taken on debt, 60% in public four-year and nearly 85% in for-profit four-year. The average debt for an undergraduate upon graduation is $25,000; more than half of the average starting salary. Under utilization in the labor market and high student debt has delayed life decisions such as household formation and discouraged new credit creation. **Graduating during a recession leads to permanently lower earnings growth, making it that much harder to service the debt burden.**

Source: BofAML

Web Source: http://www.zerohedge.com/news/2012-09-28/student-loan-bubble-19-simple-charts