DECADE OF DEBT

THE COST OF INTEREST-FREE STUDENT LOANS

KHYAATI ACHARYA
WITH ERIC CRAMPTON

THE
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2016

The New Zealand Initiative is an independent public policy think tank supported by chief executives of major New Zealand businesses. We believe in evidence-based policy and are committed to developing policies that work for all New Zealanders.

Our mission is to help build a better, stronger New Zealand. We are taking the initiative to promote a prosperous, free and fair society with a competitive, open and dynamic economy. We develop and contribute bold ideas that will have a profound, positive, long-term impact.

TABLE OF CONTENTS

FIGURES AND TABLES

ABOUT THE AUTHORS

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FOREWORD

Just over a decade ago, the government stopped charging interest on student loans. Before 2006, student debt drew interest after the borrower left school. The Labour-led government argued that loan repayment times were too long and that interest payments were burdensome for too many graduates. And so, from 2006, student loan debt would carry no interest until the loan was repaid.

A decade on, the policy has proven rather expensive with no substantial benefits.

Removing interest payments from existing student loans cost the government over $1.4 billion in 2006. The costs have mounted since then.

Every year, the government issues new loans to student borrowers. And every year, the government writes off a substantial part of the value of that debt. Debt that pays no interest has a real value to the lender well below the amount lent out. Last year alone, the government lent over $1.5 billion to students and immediately wrote off $602 million.

While students and former students collectively owe the government $14.8 billion, the fair value of that debt is much lower. The fair value represents the government's best estimate of what its loan portfolio would be worth to an external buyer. As of June 2015, the government estimated that a private buyer might be willing to pay just under $9.3 billion for the flow of future student loan repayments under the zero-percent scheme. The difference, over $5.5 billion, reflects the costs of lending at zero-percent interest.

Despite the rather high cost, the programme has not proven particularly effective at achieving its stated goals.

In 2005, before the zero-percent loans scheme started, a quarter of all student borrowers paid off their loans within 3.5 years, half after 6.7 years, and three-quarters after 10.6 years.[1] Repayment times *increased* slightly under zero-percent loans: a quarter of borrowers are forecast to repay their loans after 3.6 years, half after 7 years, and three-quarters after 12.1 years.[2]

That graduates are in less of a hurry to pay off interest-free debt when they may also be saving for a house deposit, or starting to pay off a mortgage, should be surprising to no one.

Students now pay more in mandatory minimum loan payments than they did prior to zero-percent loans. In 2005, students earning over $16,588 were required to pay at least 10 cents on each dollar earned over that threshold. In 2013, the minimum repayment obligation increased to 12 cents on each dollar earned over a $19,084 threshold. If loan payments were burdensome for students in 2005, they take an even larger chunk out of each graduate's paycheque today.

And total student debt is well up on pre-2005 levels.

Internationally, subsidised student loan schemes tend to be highly regressive. Simply put, kids from richer families who would be going to university regardless of the subsidy are the main beneficiaries. Those coming from poorer families and worse schools do not make it to university because they lack the necessary educational background.

While no New Zealand data exists on student loan uptake by students from richer and poorer backgrounds, what data exists on enrolment in tertiary education suggests New Zealand is well within international norms. Interest-free student loans are bad economics but good politics precisely because they provide a regressive transfer to the already well-off, or those soon to be well-off, while dressed as a policy intended to help the poor.

A decade on is a good time to pause and reflect on the zero-percent student loans policy. This report

1 Education Counts, "Student Loan Scheme Annual Report 2005" (Wellington: Ministry of Education, 2005).

2 Education Counts, "Student Loan Scheme Annual Report 2015" (Wellington, Ministry of Education, 2015). Estimates are for students graduating in 2011, the most recent year for which estimates are available.

traces the path to 2005's election promise and what has followed since. It surveys international practice and makes recommendations for change.

While there is a defensible case for the government's backing of student loans, there is little justification for providing those loans at highly subsidised interest rates.

In systems where student loan repayments are made through the tax system and are conditional on earning enough to make those payments, interest charges are no barrier to participation in tertiary education. The real barrier to more equitable access to tertiary education comes earlier, in primary and secondary schools, where too many students do not receive the training they need to succeed in post-secondary schooling.

In this respect, our report echoes the findings of the 1994 Ministerial Consultative Group report, "Funding Growth in Tertiary Education and Training". That report presented two options for change in the tertiary sector. Under Option A, students would bear a greater part of the burden of financing higher education, with their share rising from 20% to 25% of the cost of providing tertiary education. Option B went farther, recommending shifts in funding from tertiary tuition subsidies towards targeted improvements in primary and secondary school. Students' share of the burden of tertiary study, under Option B, would have reached 50% by 2000 – for those students earning higher incomes after graduation.[3]

In reality, students' share of the direct costs of tertiary education fell to 16% by 2010, due largely to the subsidy provided through interest-free loans.[4]

Where the main barrier to accessing tertiary study, whether at university or polytech, happens before a student completes NCEA, improving access requires earlier intervention. Funding can and should shift accordingly.

Charging market interest rates on student loans and devoting some of the hundreds of millions in annual savings to enhancing lower decile students' preparation for university, and to needs-based student assistance, would do much more good for students who really need the help.

Dr Eric Crampton

Head of Research
The New Zealand Initiative

3 Ministerial Consultative Group, "Funding Growth in Tertiary Education and Training", (Wellington: Ministry of Education, 12 May 1994),18-21.

4 Rachel Baxter, "Sharing the Private and Public Costs of Tertiary Education", Policy Quarterly 8:2 (May 2012), 49. See also the New Zealand Productivity Commission "New Models of Tertiary Education" (Wellington: New Zealand Productivity Commission, February 2016), 57, which puts the ratio at 18% private to 82% public.

KEY POINTS

- The zero-percent student loans policy has cost the government nearly $6 billion in its first decade.
- In 2014/15 alone, the government wiped $602 million from the value of the $1,529 million in student loans it issued. This write-down largely reflects the cost of lending money at zero percent rather than at a market rate of interest. These costs are expected to increase in coming years.
- In 2015, subsidies provided through the student loan scheme cost the government almost a hundred million dollars more than it spent on means-tested student allowance and accommodation benefits targeted at low income students.
- As at 30 June 2015, New Zealand had 728,348 student loan borrowers owing just over $15 billion. To put this in context, total mortgage debt in New Zealand stands at just over $200 billion.
- At June 2015, 110,594 borrowers were based overseas and owed $3.2 billion, according to Inland Revenue.
- With low eligibility restrictions, zero interest, and high universal tuition subsidies, New Zealand's student loan scheme is generous compared to similar schemes in many other countries.
- There is little compelling evidence that interest-free loans have achieved what cabinet papers at the time claimed they would, given declining participation rates and tertiary enrolment, increases in borrowing, higher implicit level of public funding, and high overseas debt.
- Government-backed loans are a plausible response to market imperfections – students cannot use education as collateral for a loan. Interest rate subsidies are not similarly justified.
- Sharing the costs of tertiary education between students and taxpayers reflects the shared social benefits of tertiary education.
- Tuition caps add to the budgetary pressures on tertiary education providers. Caps may reduce costs for students, but they also reduce the quality of education students can purchase. The government benefits from tuition caps through decreased loan disbursements.
- This report recommends restoring interest on future loans and using the savings to fund programmes to improve tertiary preparation in high school and earlier, and to provide means-tested tuition aid. Increasing the private share of tertiary costs would better reflect the shared benefits of tertiary education.

CHAPTER ONE
THE ROAD TO ZERO

> It's not politically sustainable to put interest back on student loans … It may not be great economics, but it's great politics.
>
> — John Key (2012)[5]

New Zealand's tertiary education sector – including student loans – has changed substantially since the 1980s. Student numbers have grown, funding systems have changed, and universities no longer monopolise degree provision. Demand for skills continues to evolve, reflecting global changes and digital advances. Fierce international competition means universities compete for the best and brightest students across the world, not just within national borders.

UNDERSTANDING THE BASICS

In the early 1980s, New Zealand's tertiary education sector was largely state-funded and much smaller than it is today.[6] The average fee was around $129 per annum, with a basic arts course the least expensive and medicine and dentistry the most expensive.[7] Admission was restricted to the most academically qualified, leaning more heavily towards well-off families who could afford a good school education for their children.[8] All tertiary students received a government grant, and they contributed minimally to the costs of tuition. Support was focused on a rather small number of full-time tertiary students.

Tertiary education sector reforms in the late 1980s were part of Labour's wider restructuring.[9] From 1990, tertiary education institutions were defined as universities, polytechnics, colleges of education, specialist colleges, and wananga (Maori educational institutions). Polytechnics and colleges were placed on an equal footing with universities and bulk-funded according to a formula based on the number of equivalent full-time students (EFTS) enrolled.

THE INTRODUCTION OF TUITION FEES

High per-student funding became unsustainable as the number of EFTS enrolled in tertiary education institutes increased from 69,092 in 1984 to 100,796 in 1989.[10] Increased enrolment put pressure on government finances while popular support for tertiary funding wavered.[11]

In 1990, a centrally determined annual flat fee of around $1,250 was introduced across all tertiary institutions – a ten-fold increase on the $129 tuition

5 Adam Bennett, "Govt ready to rein in student loans 'in big way': Key," *The New Zealand Herald* (13 March 2012).

6 Sharon Biggar and Darren Butterworth, "Student Loans in New Zealand," in Mick Fletcher (ed.), *Loans for Lifelong Learning* (London: Learning and Skills Development Agency, 2002), 63–75, 63.

7 Katie Kenny, "The Birth of Student Loans," www.critic.co.nz.

8 Maureen McLaughlin, "Tertiary Education Policy in New Zealand," Ian Axford (NZ) Fellowships in Public Policy (2003), 7.

9 A government-commissioned report in 1988 recommended all tertiary institutions be made independent legal entities led by a chief executive and held accountable by individual charters; competition between institutions be encouraged; and universities lose their monopoly over degrees. These suggestions were implemented through the *Education Amendment Act 1990*. Encyclopaedia of New Zealand (Te Ara), "Tertiary Education: Tertiary Sector Reform from the 1980s," Website.

10 Education Counts, "Student Loan Scheme Annual Report 2000" (Wellington: Ministry of Education, 2000), 3.

11 Sharon Biggar and Darren Butterworth, "Student Loans in New Zealand," op. cit., 63.

fee students were paying.[12] No government-backed student loan scheme was yet in place.

In early 1992, the Jim Bolger-led National Government removed the tuition cap on universities in a bid to foster greater competition and differentiation between providers.[13] Strengthening higher education was then seen as a way of improving productivity and stemming declines in living standards relative to other similar countries.[14]

Tuition fees for all courses consequently increased substantially from 1992, particularly for medicine and dentistry. The upfront costs for tertiary students were suddenly much higher than previously, and neither students nor their parents were financially prepared. Table 1, tallies the annual tuition fees for a Bachelor of Arts degree from 1993 through 2000.

THE ORIGINAL SCHEME

To offset the potentially negative impacts of higher course fees[15] (e.g. fewer enrolments) and to ensure financial barriers did not deter participation in tertiary education,[16] a government-backed loan scheme was introduced in 1992.[17] The scheme was designed to overcome credit market realities and "facilitate participation in tertiary education by overcoming the immediate financial burden of fees" rather than increase or restore tuition subsidies for students.[18]

The *Student Loan Scheme Act 1992*, administered by the Ministry of Education, provided bulk loans to students at lower-than-market interest rates for course fees, course-related costs, and living costs.[19] Students could defer paying their share of tertiary education costs until after graduation.[20]

The repayment scheme is income-contingent, so students are not required to make any repayments until they earn more than a set threshold.[21] A percentage of every dollar earned above the repayment threshold is collected by Inland Revenue and applied to the borrower's student loan. The minimum repayment threshold was $14,769 in 2000 and is $19,084 today.[22]

Income-based repayment schemes have two effects. Most obviously, they make student loan repayments more affordable for recent graduates. But they can have a less obvious effect on student choices of whether to study, and what to study. If a graduate's degree does not lead to employment, the government bears the risk of loans not being repaid.

Degree pathways yielding personal enjoyment for students, but with a strong risk of low future earnings, are more feasible under income-contingent loan repayment schemes. While perhaps few students leaving secondary school would choose degrees likely to lead to poor

12 Norman LaRocque, *Who Should Pay?: Tuition Fees and Tertiary Education Financing in New Zealand* (Wellington: Education Forum, 2003), 15.

13 Sharon Biggar and Darren Butterworth, "Student Loans in New Zealand," op. cit., 67.

14 Rachel Baxter and Stuart Birks, "The Student Debt Debate: An Economic Investigation of the Issues," Student Paper No. 5 (Palmerston North: Centre for Public Policy Evaluation, Massey University, 2004), 6.

15 Larry L. Leslie and Paul T. Brinkman, "Student Price Response in Higher Education: The Student Demand Studies," *Journal of Higher Education* 58:2 (1987), 181–204.

16 The government believed the lack of assets and short, or non-existent, credit histories would deter students from borrowing in the private capital market. Sharon Biggar and Darren Butterworth, "Student Loans in New Zealand," op. cit., 67.

17 Ministry of Education, "Student Support Package for Budget 2011," Regulatory Impact Statement (Wellington: New Zealand Government, 29 March 2011), 2.

18 Sharon Biggar and Darren Butterworth, "Student Loans in New Zealand," op. cit., 67.

19 Ibid., 71. "The resulting interest rate is less than a student would pay in a market setting, but is significantly higher in both nominal and real terms than the zero real rate of interest students face in the UK." Ibid., 68.

20 Education Counts, "Student Loans," Website.

21 Education Counts, "Student Loan Scheme Annual Report 2000," op. cit., 4.

22 Ibid., 4; Inland Revenue, "Thresholds for Student Loan Repayments," Website.

Table 1: Nominal annual fees for a Bachelor of Arts degree (1993–2000)

	1993	1994	1995	1996	1997	1998	1999	2000
Auckland University	1400	1792	1848	2128	2464	2884	3080	3360
Waikato University	1365	1675	1825	2195	2575	2875	3205	3541.5
Massey University	1307.5	1645	1680	2025	2376	2476	2776	3126
Victoria University	1410	1830	1920	2250	2490	2586	2754	3000
Canterbury University	1300	1500	1700	2200	2400	2800	3210	3410
Lincoln University	1184	1296	1384	1672	2000	2104	2704	3040
Otago University	990	1250	1520	1700	1960	2220	2650	2950

Source: Universities NZ

employment outcomes,[23] mature students nearing retirement could see tertiary study as a free option: loans cover course costs, and low post-retirement incomes mean little need ever be paid back.

Nevertheless, the system in the late 1990s had many desirable properties. As Nicholas Barr, an economist from the London School of Economics, put it:

> New Zealand is a sad story. The country had the world's best system between 1993 and 2000. Loans covered fees and living costs. Income contingent repayments were collected as a payroll deduction. The interest rate was one per cent above the government's cost of borrowing. The NZ authorities calculated that a risk premium of two per cent would cover the entire loss on the portfolio, so the effect of charging one per cent above the cost of finance was that half of the estimated loss was paid by the cohort of borrowers and half by taxpayers.
>
> A mistake was political failure to explain the system properly, leading to the introduction of very expensive interest subsidies.[24]

A 1994 Ministerial report into tertiary education and training found that fees then accounted for approximately 20% of tuition costs.[25] Students in 2010 paid 16% of the direct cost of tertiary education, after accounting for the subsidy provided through the revised student loan

23 The Ministry of Business, Innovation and Employment's (MBIE) employment outlook handbook notes that 200 students per year complete a bachelor's degree in drama and theatre studies; total employment of actors, across the entire country, is 1,475, with projected employment growth of between 31 and 48 actors per year. An actor achieving employment can expect earnings of $40,400 after five years. At a repayment threshold of $19,084 and a 12% student loan repayment on earnings over that threshold, annual loan repayments at that point would be only $2,558. Course fees alone for a three-year degree in drama are $19,300.

24 Nicholas Barr, "Income Contingent Loans and Higher Education Financing: Theory and Practice" (Chapter 5), in Bruce Chapman, Timothy Higgins and Joseph E. Stiglitz (eds), Income Contingent Loans: Theory, Practice and Prospects (Palgrave Macmillan, 2014), 63–75.

25 Ministerial Consultatitve Group, "Funding Growth in Tertiary Education and Training" (Wellington: New Zealand Government, 12 May 1994), 10.

scheme.[26] The Ministerial Consultative Group recommended reducing the per capita tuition subsidy, with one option recommending strong increases in the private share of tertiary funding. The report cogently noted:

> As an illustration, the present value of the additional income earned by an average male graduate is around $150,000. Currently, such a graduate would typically contribute no more than 20 per cent of tuition costs which is an average contribution of around $6,000 or 4% of the asset's financial value. The balance of tuition costs is met by the taxpayer. In effect, the taxpayer confers a large capital grant on graduates. Similar grants are not made available to people who wish to establish a business. For example, a young person buying a herd to become a sharemilker could not expect the taxpayers to meet 80% of the costs.[27]

The Report's Option B, which recommended the most substantial increases to the private share of tertiary funding, also recommended improving resourcing for pre-schools, primary and secondary schools serving students under-represented at tertiary level.[28]

POLITICAL WIN OR FINANCIAL GRAVE-DIGGING?

In 2000, the Fifth Labour Government wanted to further cut tuition costs for tertiary students[29] through changes to the loan scheme.[30]

Times Higher Education reported in September 2000 that the student loan system was responsible for an exodus of graduates – the number of graduates living overseas doubled from 1999 to 2000, and nearly doubled the amount of student debt owed by graduates overseas. Though some of this increase could have been due to improved counting of those students leaving the country, the combination of high student debt, higher potential earnings abroad, and a high top marginal tax rate in New Zealand made a plausible case for policy change.

But simply wiping off all existing student debt (valued at $5.2 billion in December 2000) was unrealistic because of the considerable fiscal loss it would represent.[31] The compromise was to write off all interest charges on loans while students were studying, and impose a temporary tuition fee freeze on tertiary education providers.[32] By the end of 2001, more than 76,400 borrowers had received $68.5 million in interest write-offs.[33]

By the 2005 general election, the two-term Labour-led Government had eliminated interest on loans for all students during study; limited tuition fee increases through a new centrally mandated

26 Rachel Baxter, "Sharing the Private and Public Costs of Tertiary Education", Policy Quarterly 8:2 (May 2012), 49.

27 Ministerial Consultative Group, "Funding Growth in Tertiary Education and Training", (Wellington: Ministry of Education, 12 May 1994),110.

28 Ministerial Consultative Group, op. cit., 112.

29 Dita De Boni, "The great student loan blow-out," *The New Zealand Herald* (3 April 2002).

30 The Student Loan Scheme Amendment Bill was introduced into Parliament by Dr Michael Cullen on 13 June 2000. The amendment waived interest for full-time, full-year students as well as low-income, part-time students, while they were studying. The waiver was also applied retrospectively to loans taken after 1 January 2000. Any accumulated interest for loans taken before that date was deleted from the loan balance dating back to 1 April 2000.

31 Education Counts, "Student Loan Scheme Annual Report 2000," op. cit., 20.

32 Dita De Boni, "The great student loan blow-out," op. cit.

33 Ibid.

fee caps policy; and increased parental income thresholds for student allowance eligibility.[34] It had also introduced bonded scholarships to encourage study in strategic fields (e.g. science and engineering) to reward high academic performance and to improve participation in the tertiary sector from traditionally under-represented groups, such as Maori, Pasifika, and those from poorer backgrounds.[35]

But the biggest policy change came with Labour's decision to keep its 2005 campaign promise to extend interest-free student loans to all borrowers residing in New Zealand beyond the study period.[36] Labour aimed to make tertiary education more affordable and encourage graduates to remain in New Zealand, promising lower student debt and faster repayment times.[37]

NEW GOVERNMENT, OLD IDEAS

The National Party opposed interest-free loans during the 2005 general election campaign, criticising it as an "election bribe"[38] and an irresponsible policy move that would impose too great a burden on public finances.[39] But with the change in National leadership prior to the 2008 general election, policy too changed. Incoming National leader John Key told his party:

> We will keep interest-free student loans for tertiary students. Half a million New Zealanders have a student loan. Many have made long-term financial decisions on the basis of the current policy and we want to ensure they can plan with certainty.[40]

National claimed the policy would enhance New Zealand's overall performance. "Education is a hugely important part of our pathway forward".[41]

Politics typically, and rightly, prevents rapid changes to legislation that would impose substantial and unexpected financial burdens on families. But other options, like restoring interest charges for future student loans, were not explored. Key did pledge incentives aimed at encouraging students to pay off their loan balances sooner.

> One of our concerns has been that the scheme offers no incentive for New Zealanders to repay any earlier. That means loan holders are likely to have their debt for longer, which has implications for other areas of their lives like buying a house or starting a family.[42]

It is somewhat difficult to see how a graduate can be worse off by taking longer to pay off a loan that comes without interest charges, but it is fairly obvious that longer repayment terms hurt the government's budget.

On being elected in 2008, the Fifth National Government introduced relatively minor policy changes to improve repayment rates and introduce sector-wide incentives, partly due to the 2008 global economic crisis.[43] A voluntary

34 Helen Clark and Trevor Mallard, "Student Support: Policy, Factsheet and FAQ" (Wellington: New Zealand Government, July 2005), 1.

35 Ibid.

36 New Zealand Government, "Interest free student loan costings," Press Release (Wellington: New Zealand Government, 19 December 2005).

37 Helen Clark and Trevor Mallard, "Student Support: Policy, Factsheet and FAQ," op. cit.

38 Claire Trevett, "National to keep Interest-free student loans despite initial opposition," *The New Zealand Herald* (31 January 2008).

39 Ibid.

40 John Key, "National offers bonus to student loan borrowers," Press Release (National Party, 31 January 2008).

41 Ibid.

42 Ibid.

43 Education Counts, "Student Loan Scheme Annual Report 2014" (Wellington: Ministry of Education, 2014), 9.

repayment incentive was introduced in 2009[44] and abolished in 2013,[45] when minimum repayment rates increased from 10% of above-threshold income to 12%. Enforcement of repayment obligations on overseas-based debtors became more stringent with a reduction in the repayment holiday for overseas borrowers;[46] better information sharing both across agencies[47] and between governments[48] to track overseas borrowers with outstanding obligations;[49] and stronger enforcement of repayment obligations on overseas borrowers.[50]

THE NEW ZEALAND INITIATIVE

44 "One of our concerns has been that the scheme offers no incentive for New Zealanders to repay any earlier. That means loan holders are likely to have their debt for longer, which has implications for other areas of their lives like buying a house or starting a family." John Key, "National offers bonus to student loan borrowers," op. cit.

45 Inland Revenue, "Former Voluntary Repayment Bonus," Website.

46 The move signalled accountability for overseas-based borrowers and ensuring borrowers realised their individual debt obligations and responsibilities to taxpayers. New Zealand Press Association, "Student loan repayment holiday cut back," *The New Zealand Herald* (19 May 2011).

47 Ministry of Education, "Student Support Package for Budget 2013," Regulatory Impact Statement (Wellington: New Zealand Government, 22 March 2013), 2.

48 Inland Revenue, "Information Sharing Arrangement with Australia for the Recovery of Student Loan Debt," Regulatory Impact Statement (Wellington: New Zealand Government, 10 February 2015), 2.

49 Ibid., 3 [44–46]. "[44] The Arrangement supports one-way information exchanges between Australia and New Zealand to assist New Zealand in the recovery of its student loan debt held in Australia. However, the nature of an Arrangement means that it is able to be amended in the future for the purpose of supporting a reciprocal information exchange. [45] This service is to be provided on a cost-recovery basis. Australian officials have provided Inland Revenue with an indicative cost of $1,143,600 (AUD) over five years ... [46] Entering into the Arrangement is considered to be preferable to the status quo because it ultimately supports an information exchange with the ATO to assist in the recovery of New Zealand student loan deb, while the status quo does not support this."

50 NBR, "Arrested student loan defaulter claims to be Cook Island PM's relative," *National Business Review* (22 January 2016). Radio New Zealand reported in early April that as a result of the high profile arrest, Inland Revenue had seen a 31% increase in the number of student loan repayments from overseas-based borrowers between January and February 2016. Tom Furley, "Student loan arrest prompts overseas repayments," Radio New Zealand (4 April 2016).

CHAPTER TWO
INTEREST-FREE LOANS – A DECADE ON

While television footage of students in makeshift soup kitchens, in cardboard box "cities" and in student loan debt "shackles" makes for great theatre, it does far less for advancing serious debate on the issue of tertiary education financing in New Zealand.

— Norman LaRocque[51]

Student loans help make tertiary education more accessible.[52] In the absence of government-backed student loans, students could find it difficult to convince a private lender to provide a loan backed by no tangible collateral. The basis for government-backed loans will be explored in more depth in Chapter 3.

Interest-free loans act as a subsidy for tertiary study. Where government-backed but interest-bearing loans plausibly correct a failure in credit markets, forgone interest payments under government subsidised interest schemes represent a transfer from the government to students taking on loans.

51 Norman LaRocque, "Zero fees and a universal student allowance for New Zealand?" Speech to the Hamilton East Rotary Club (16 April 2008).

52 Bruce Johnstone, "Higher Educational Accessibility and Financial Viability: The Role of Student Loans," in *World Report on Higher Education: The Financing of Universities* (Basingstoke, UK: Palgrave Macmillan, 2006), 22.

THE STATE OF AFFAIRS

Three government agencies oversee and administer student loans. The Ministry of Education is primarily responsible for the scheme and providing policy advice. StudyLink, an agency of the Ministry of Social Development, is responsible for information, assessment and payment. Lastly, Inland Revenue is responsible for loan management and collection once a student leaves tertiary study and starts earning.

Since student loans were introduced in 1992, more than 1 million students[53] have borrowed $21.8 billion;[54] nearly 450,000 students have repaid their loans in full; and Inland Revenue has collected $10.3 billion in repayments.[55] As of 30 June 2015, there were almost 730,000 borrowers with outstanding student loans.[56]

The nominal value of the student loan scheme hit $15 billion on 2 March 2016, making national headlines.[57] It is projected to be almost $17 billion by 2020.[58]

Because student debt owed by domestic graduates does not draw interest, the value of students' future payments to the government is much less today than the amount students will later repay. Similarly, from the students' perspective, the burden of the debt they owe is less than that debt's face value when no interest applies.

53 Bruce Johnstone, "Higher Educational Accessibility and Financial Viability," op. cit., 23.

54 Education Counts, "Student Loan Scheme Annual Report 2015," op. cit., supplementary data tables, SLS17.

55 Ibid., 32.

56 Ibid., 36.

57 Radio NZ, "Student debt a ticking bomb – Labour," Radio New Zealand (2 March 2016).

58 The Treasury, "Half Year Economic and Fiscal Update," Note 14 (Wellington: New Zealand Government, 2015), 115, B.6.

There are two ways of measuring the difference between the nominal value of student debt and that debt's real value. The first, called carrying value, reflects the interest rates that prevailed when the loan was issued. The second, called the fair value, reflects the amount the government expects it could receive were it to sell the stream of future loan payments to a private buyer; it then reflects current interest rates. As of 30 June 2015, the carrying value of the government's loan asset was $8.9 billion, while the fair value was $9.3 billion. The difference between the nominal value of the loan portfolio, which stood at $14.8 billion in 2015, and the real value is then $5.5 billion to $5.9 billion.

BOX 1: SHORT FACTS ABOUT THE INTEREST-FREE STUDENT LOAN SCHEME IN 2016

- Eligibility for student loans is not means-tested
- Loans are available to New Zealand citizens, permanent residents, and refugees for courses approved by the Tertiary Education Commission[59]
- Student loans are available for course fees, where they are paid directly by StudyLink to the tertiary education provider. Loans are also available for course-related costs (maximum $1,000 per year) and living costs (maximum $176.86 per week)[60]
- The lifetime limit for obtaining a student loan in New Zealand is 7–8 years of full-time study (7 EFTS)[61]
- Repayments are income-contingent for New Zealand-based borrowers to be paid directly to Inland Revenue through the PAYE system. The current minimum repayment rate is 12% of pre-tax income
- Debt is forgiven in case of a borrower's death or bankruptcy[62]
- No interest is charged for students still studying, or for graduates residing in New Zealand
- Borrowers residing overseas for more than six months are charged interest on any remaining loan balance. The interest rates (currently 4.8%) are reviewed at the start of each financial year and any changes are made effective from 1 April[63]
- Inland Revenue stipulates annual repayment obligations for overseas-based borrowers based on total loan balance.

59 StudyLink, "Who Can Get a Student Loan," Website.

60 StudyLink, "How Much Student Loan Can You Borrow?" Website.

61 Ibid. "The Tertiary Education Commission decides if a course is either full-time or part-time by applying what is called an EFTS value to each course. The EFTS value is a measure of the amount of study or the workload involved in undertaking a course. A year of full-time study is usually between 0.8 EFTS and 1.2 EFTS." StudyLink, "EFTS (equivalent full-time student) – General Definition," Website.

62 Ibid. Provisions within the student loan contracts hold that in the event of death or bankruptcy of a student loan borrower, the debt will be written off. Debt obligations will not be passed on to the next of kin of a deceased borrower.

63 Inland Revenue, "Interest and Other Charges," Website.

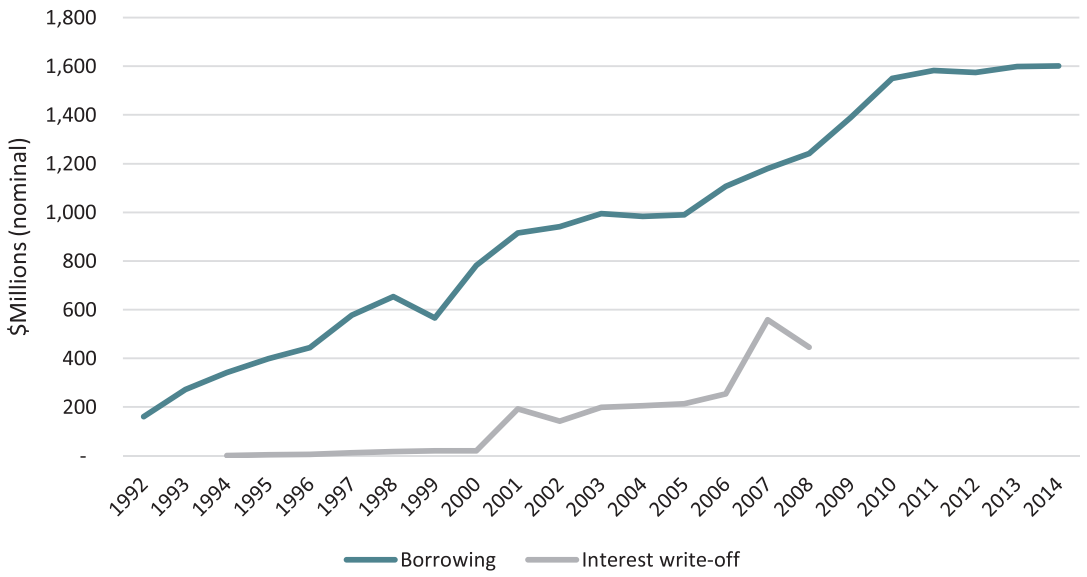
The most obvious cost of the scheme is the interest write-off.

Because the zero-percent student loan policy applied not only to new student loans but also to existing student loans, the shift to zero-percent loans required an immediate write-down of $1,415 million from the total value of the student loan portfolio.[64] It is simplest to think of that amount as a gift to those who, in 2005, held student loan debt. The policy change reduced the amount those borrowers would need to pay back by $1,415 million.

Prior to 2009, annual reports for the student loan scheme tallied the value of the interest rate write-down on new lending. Annual reports from 2009 onwards do not separately tally the cost of the interest rate subsidy, bundling it instead into the initial write-down on all new lending. Figure 1, below, traces the value of new lending and of the interest rate subsidy provided for those years where data is available. The cost of the initial write-down is not included here. Note further that the drop in the interest rate subsidy in 2008 was due to the government's discovery that many of its borrowers were overseas and, consequently, were required to pay interest.[65]

Because the value of interest write-offs has not been tabulated separately from 2009 onwards, it is more difficult to place a value on the current costs of the zero percent scheme. We must look instead to the initial write-down on new lending, which reflects not only the substantial subsidy provided by interest-free loans but also expected non-repayments due to death, bankruptcy, failing to meet the income threshold for repayment, or failing to repay while overseas. In 2014/15, for example, $35 million was written off due to death or bankruptcy.

Figure 1: New borrowing and interest write-off



Source: Student Loan Scheme Annual Reports. Interest data from the 2008 Annual Report. Borrowing data from the 2015 Annual Report.

64 The Treasury, "Table 6.9 – Tertiary education expenses," Core Crown Expense Tables in Budget Economic & Fiscal Update 2007 (Wellington: New Zealand Government, 2007).

65 Education Counts, "Student Loan Scheme Annual Report 2008" (Wellington: Ministry of Education, 2008). See discussion of the data at note 4, Table 26 of the linked spreadsheet.

Since 2005, the annual immediate write-down of the value of new loans has ranged from $328 million to $728 million. In the decade from 2005/06 to 2014/15, the government has written off $5.75 billion from the $13.4 billion in new lending it has extended to student borrowers.[66] In 2014/15 alone, $602 million out of $1,529 million borrowed was written off. And matters are not forecast to improve. The immediate write-down is expected to reach $723 million in 2018/19. To provide some context, the government spent $504 million in 2015 on means-tested student allowance and accommodation benefit programmes.[67]

In 2005, when interest was deferred only while borrowers were studying, the carrying value of the student loan portfolio was 86.2% of its nominal value. The difference reflected both the smaller interest subsidy provided by deferring payment and interest while borrowers were in study, and expected losses from non-repayment. That carrying value dropped from 86.2% to 66.5% in 2006 with the adoption of the zero-percent loans policy and has declined since then to 59.7% in 2015. Similarly, the fair value of the student loan scheme dropped from 79.9% of the nominal value in 2005 to 62.5% in 2015. The current nominal value of the student loan portfolio is $14.8 billion. If the carrying value of that portfolio had stayed at 86%, the current carrying value of the loan book would be $3.9 billion dollars higher.

Current low market interest rates have meant that the real current value of the subsidy provided by zero-percent loans, per dollar borrowed, is smaller than it was in the late 2000s. In 2007, the Official Cash Rate stood at 8.25%; as of mid-2016, it sits at 2.25%. If interest rates rise again, so too will the cost of the zero-percent loans scheme.

The full value of the annual subsidy currently provided by the government through the student loan scheme is the $602 million initial write-down on new lending. The $5.6 billion to $6 billion difference between the nominal value of the student loan scheme and its fair or carrying values, respectively, provide a measure of the current value of the accrued subsidies. While some of this write-down reflects non-performing loans, the cost of non-performing loans in other lending markets is borne through higher interest rates on all borrowers.

In 1999/2000, when interest applied both after study and, for some borrowers, also during the period of study, the government still needed to write down the value of its loan portfolio for non-performing loans. In that year, the government reduced the value of its $3.5 billion dollars in outstanding student loans by $110.5 million due to write-offs and changes in provisions for doubtful debt. $701.3 million was lent to students that year, and $223 million in interest accrued on prior lending.[68]

Interest-free student loans appear to have had little impact on participation.

Removing interest from student loans does not seem to have increased tertiary participation. In fact, tertiary participation fell over the past decade, from a peak of 14% (454,193 total enrolled students) in 2005 to 10.2% (363,644 total enrolled students) in 2014.[69]

While longer term participation rates will decline as the population ages, the decline in participation rates even in the midst of the great recession is striking. Participation rates peaked in the year prior to the implementation of zero-percent loans.

Education Counts provides age-standardised participation rates from 2008 through 2015.

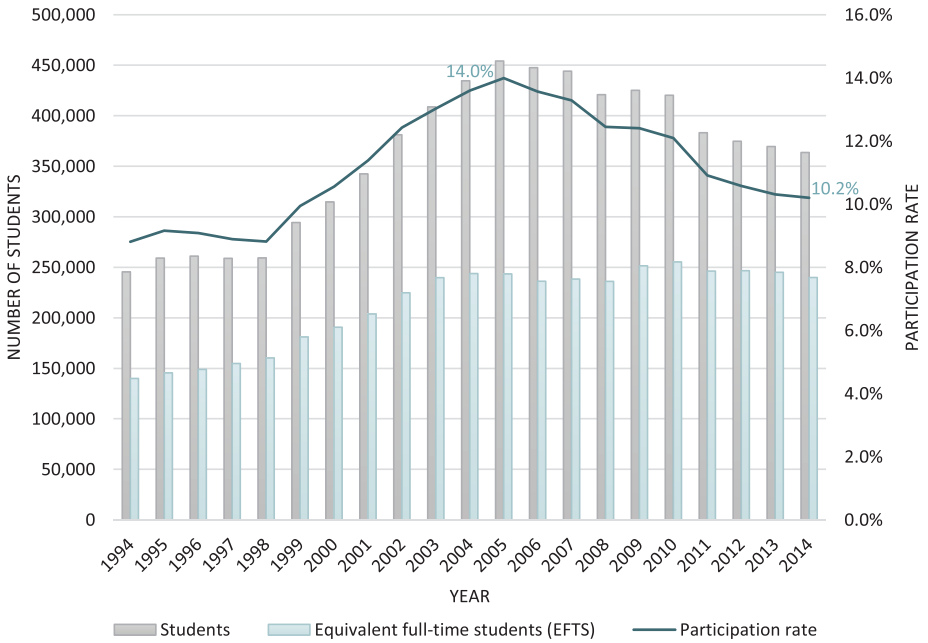
66 Calculated from annual write-downs on new lending from Education Counts, "Student Loan Scheme Annual Report 2015" (Wellington: Ministry of Education, 2015), Figure 27, 43.

67 StudyLink, "Amounts Paid Out for Student Allowance and Accommodation Benefit Payments," Website.

68 Education Counts, "Student Loan scheme Annual Report 2000". Appendix Table A-1.

69 Education Counts, "Student Loan Scheme Annual Report 2015," op. cit., data tables, SLS1. The participation rate is calculated from the number of enrolments, in a calendar year, as a percentage of Statistics New Zealand's estimate of the population aged 15 and over at 31 December each year.

Figure 2: Tertiary participation rates (1994–2014)



Source: Figures derived from Education Counts, "Student Loan Scheme Annual Report 2015" (Wellington: Ministry of Education, 2015), supplementary data tables.

Note: The participation rate is the number of enrolments, in a calendar year, as a percentage of Statistics New Zealand's estimate of the population aged 15 and over at 31 December each year.

Age-standardised rates tell us what tertiary participation rates in prior years would have been if the overall age distribution matched 2015's age distribution. Age-standardised tertiary participation rates dropped from 12.4% in 2008 to 9.8% in 2015.[70] While data prior to 2008 is not available, the drop in standardised rates since 2008 is consistent with the decline in unadjusted participation rates over that period.

We also consulted OECD data on educational attainment. The OECD reports on the proportion of the population in each age bracket that has completed a bachelor's degree or equivalent. Few students today aged 35–44 years would have benefitted from the zero-percent student loan policy during study for a bachelor's degree, but many today aged 25–34 years could have. The cohort aged 35–44 in 2015 would have been at least 25 years old in 2005; the cohort aged 25–34 in 2015 would have been 15–25 years old in 2005 and so could have been affected.

Table 2: Proportion of the population holding a bachelor's degree or equivalent

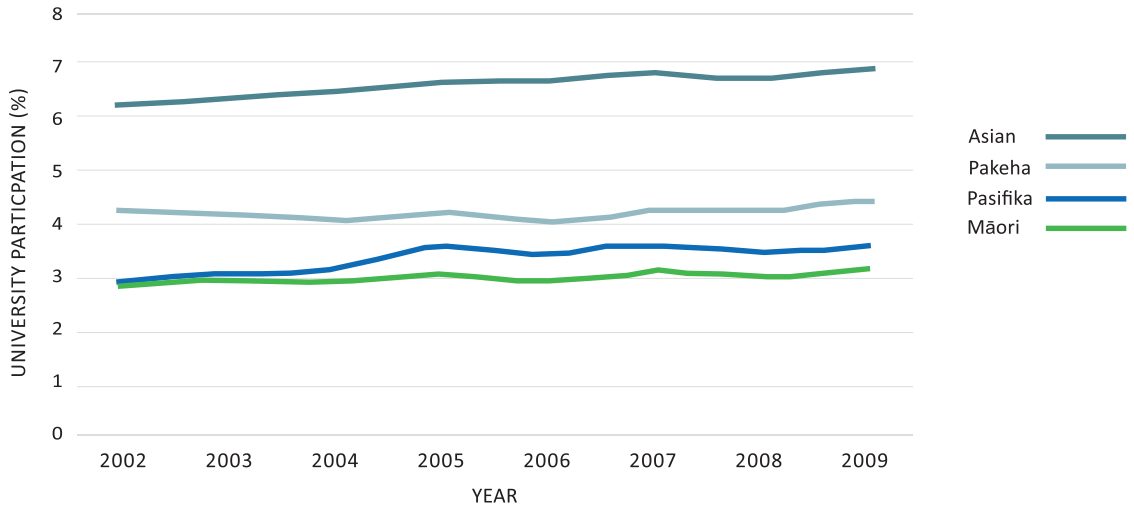
	25–34 years old	35–44 years old
New Zealand	32%	30%
OECD average	21%	17%

Source: OECD, Education at a Glance 2015 (Paris: OECD Publishing, 2015), Table A1.3a.

The proportion of today's 25–34 year-olds with a bachelor's degree is higher than the proportion of 35–44 year-olds with a bachelor's degree. However, the increase in bachelor's degree attainment among younger cohorts is higher in other OECD

70 Education Counts, "Participation Rates", table PPN.10. The same source, at Table PPN.11, shows that age-standardised university enrolment rates dropped from 4.4% to 4% over the period; enrolment at institutes of technology and polytechnics dropped from 5.4% to 3.6% over the same period.

Figure 3: Age-standardised university participation rates by ethnicity (2002–09)



Source: Nigel Healey and Philip Gunby, "The Impact of Recent Government Tertiary Education Policies on Access to Higher Education in New Zealand," *Journal of Educational Leadership, Policy and Practice* 27:1 (2012), 29–45.

countries. Again, the data is not particularly consistent with increases in participation rates due to zero-percent loans.

Failure to increase participation rates might be less of a concern if zero-percent loans encouraged participation among otherwise under-represented groups. Work by Nigel Healey and Philip Gunby suggests otherwise (see Figure 3).

The zero-percent loans policy came into effect in 2006. The rise in Pasifika participation came prior to the implementation of zero-percent loans and has been unchanged since. Neither has there been any particular change in Maori participation with the shift to zero-percent loans.

Reduced participation consequent to the introduction of zero-percent loans should have been predicted. If a student loan holder fails to graduate, or graduates into a profession with low earnings, or fails to enter the labour market, the government can expect little if any repayment under income-contingent loans. In order to reduce that burden, the government would wish to introduce policies restricting tertiary access to those at higher risk of failure. Healey and Gunby[71] highlight policy changes since 2008 that have limited open entry. The government capped overall enrolment and penalised universities for lower pass rates, encouraging universities to prevent failing students from pursuing further study. Universities responded by tightening progression rules from first-year to further study and implementing selective entry policies.

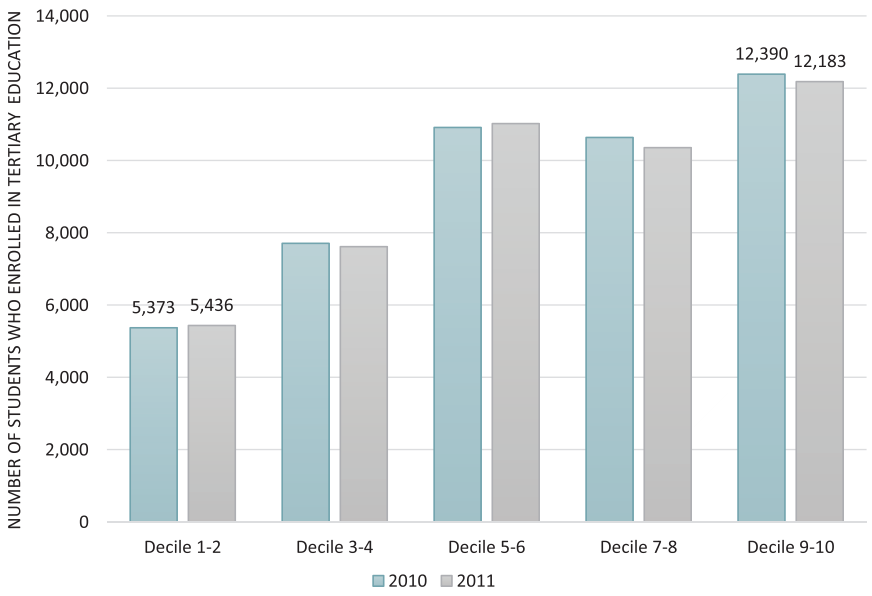
While Healey and Gunby do not discuss any link between the tightening of university access and the costs of the zero-percent loans policy, Barr warns that the expense to the government of interest subsidies directly impedes access:

> Interest subsidies are a major potential pitfall for a system with income contingent repayments. The central point is that an interest subsidy for everybody is enormously expensive; it therefore interferes with the quantity of places and/or the quality of higher education; it impedes access (since if loans are expensive, they will be rationed for fiscal reasons) ...[72]

71 Nigel Healey and Philip Gunby, "The Impact of Recent Government Tertiary Education Policies on Access to Higher Education in New Zealand," *Journal of Educational Leadership, Policy and Practice* 27:1 (2012), 41.

72 Nicholas Barr, "Income Contingent Loans and Higher Education Financing," op. cit.

Figure 4: Transition from high school to tertiary education by decile (2010 and 2011)



Source: Education Counts, "Transition from School to Tertiary," Website.

Note: The Ministry of Education has no data for transitions occurring earlier than the statistics already published on Education Counts. This is because the National Student Number (NSN) was applied to school students for the first time in 2003. The earliest possible transitions to tertiary education could have occurred in 2007, and Education Counts has published data on transitions for school leavers from this date. Without the NSN, there was no way to track progress between the different education sectors; the NSN was in fact introduced to solve this problem.

The government's moves to restrict access to universities should plausibly be seen as a direct response to the fiscal cost of zero-percent loans.

The flow-on consequences have yet to be fully explored. Victoria University of Wellington economists Harold Cuffe and Luke Chu, for example, are investigating the effects of one of these rule changes.[73] In 2009, the government restricted access to loans to those students who failed to pass at least half their courses after approximately two years of study. Students slightly below the threshold might then be disadvantaged relative to students slightly above the threshold: a failing student could be less likely to recover if that student needed to take on extra part-time work to fill the gap. But students likely to fail are students less likely to make income-contingent repayments, and the programme's overall costs require rationing.

Interest-free loans are very likely regressive, certainly more so than targeted support.

Internationally, poorer families tend to have lower levels of education compared to wealthier families. New Zealand is little different. Sholeh Maani found in 1997 a strong correlation between family income and tertiary participation.[74] Interest-free student loans then risk a strongly regressive effect unless they substantially increase participation by poorer cohorts. But even if a subsidised loan scheme did substantially improve access to higher education by under-represented cohorts, targeting the subsidy to those students in greater need of support would achieve that improvement in access at lower overall cost. Targeting would then allow greater support where it is most needed, a reallocation of funds to other areas, or a combination of both.

73 See Statistics New Zealand, "How Researchers Are Using the IDI," Website. Further details on the study were obtained through correspondence with the authors; no results were yet available at the time of writing.

74 Sholeh Maani, *Investing in Minds: The Economics of Higher Education in New Zealand* (Wellington: Institute of Policy Studies, 1997), as cited in Rachel Baxter and Stuart Birks, "The Student Debt Debate," op. cit., 12.

No New Zealand data exists showing whether richer or poorer students are more likely to benefit from subsidised student loans. As student loans are not means-tested, and students are not required to provide data on family or parental wealth when filling out loan application forms, it is difficult to link student borrowers to their family background. It can be done through Statistics New Zealand's Integrated Data Infrastructure, and could usefully form a part of StudyLink's future annual reports, but it is not possible in this report.[75]

Nevertheless, the Ministry of Education does have some data on the transition from high school to tertiary education, detailing the absolute number of students who progress to tertiary education from high school, by decile.[76] Though not a perfect measure, it does give a rough insight into tertiary participation by socioeconomic status. Figure 4 shows that during 2010 and 2011, more students from higher decile schools enrolled in tertiary education, as compared with students from lower decile schools.

New Zealand's decile system provides a rough proxy for the socioeconomic background of families within a school's catchment. Students from families on the lower rungs of the socioeconomic ladder may be less likely to see tertiary education as a priority, have insufficient guidance on pathways to tertiary study,[77] or simply not have enough peers in tertiary education to make it a consideration.

While a smaller number of students are enrolled in lower decile schools compared to higher decile ones, and so the proportionate differences are smaller than the absolute differences, the skew in tertiary support towards students from richer schools is stark. Based on the raw numbers contained in Figure 4, more than twice as many students from decile 9 and 10 schools (12,183 in 2011) enrol in tertiary education than those from decile 1 and 2 (5,436 in 2011). Even if every student in the lowest two deciles took up student loans, and only half of all students from the highest two deciles took up student loans, students from wealthier schools would still attract a higher proportion of overall student loan funding.

Families within deciles can vary considerably from one another. If tertiary uptake among students from low decile schools is highest for those with relatively wealthier backgrounds, then the figures above understate the programme's regressivity.

Without data on transitions from secondary school to tertiary study by decile prior to interest-free student loans, or data on whether richer or poorer families have greater uptake of student loans, we cannot say the programme failed to improve tertiary access among poorer cohorts. But the available data is not consistent with any progressive effect of the zero-percent student loan programme.

International evidence suggests interest rate subsidies have regressive effects. While loans in general can strongly promote access to tertiary education, the interest rate subsidy acts as a non-means tested grant to all students who borrow.

Ross Finnie argues that loans should be preferred to grants as loanable funds provide a stream of future payments that can fund future loans. If repayment difficulties emerge for some borrowers after graduation, targeted interest rate relief at that point for those borrowers can achieve the objectives desired under interest rate subsidies but without the regressive character of indiscriminate student grants.[78]

75 Correspondence with the Ministry of Education and Statistics New Zealand confirms that while it is possible to link borrowers to family background to determine the distributional characteristics of the student loan programme, such statistics have not been compiled.

76 Education Counts, "Transition from School to Tertiary," Website.

77 Alexandria Walton Radford, "No point in applying: Why poor students are missing at top colleges," *The Atlantic* (16 September 2013).

78 Ross Finnie, "Student Loans: Empirical Evidence and Policy Implications," Queens University School of Policy Studies Working Paper No. 7 (2000).

Interest subsidies can be particularly regressive when combined with income-contingent loan repayments. As Barr puts it:

> … worst of all, interest rate subsidies are targeted with considerable precision at exactly the wrong group of people. They are regressive in the extreme.[79]

Barr singles out New Zealand's current system as particularly expensive and badly targeted, noting that the primary beneficiaries of interest rate subsidies where repayment is income-contingent are mid-career professionals.

Overseas-based borrower compliance remains problematic.

It is similarly difficult to conclude that the zero-percent loans policy discouraged graduate emigration. The fraction of overseas-based borrowers out of total student loan borrowers has only decreased very slightly over the past decade. In 2005, out of 154,411 student loan borrowers, 25,091 were overseas-based, or roughly 16%.[80] In 2014, out of 728,300 student loan borrowers, 110,600 were overseas-based, or 15%. As of June 2015, overseas-based borrowers owed more than $3 billion, most of which is overdue.[81] It is always possible things would have been even worse but for the policy, but there is little evidence on which to base such claims.

Student Loan Scheme Annual Reports show the value of overdue overseas-based student debt has increased vastly from 7,857 borrowers owing $34.5 million[82] (45% of total overdue debt) in 2002[83] to more than 80,000 borrowers owing more than $800 million[84] (90% of total overdue debt) in 2015.[85] The total number of overseas-based borrowers, including those making regular repayments, increased from 82,337 in 2009 (owing $1.9 billion)[86] to 110,594 in 2015 (owing $3.1 billion). Because of the difficulties inherent in keeping track of overseas-based borrowers, it is arguably easier to avoid making repayments towards a student debt.

Non-compliance of overseas-based borrowers has been a problem since the student loan scheme began in 1992. Improving repayment rates among overseas-based borrowers requires having their up-to-date contact details, which is not easy. Inland Revenue holds contact details for around 30% of overseas borrowers, but many of these may be incomplete or incorrect.[87] Inland Revenue is trying to make better information-sharing arrangements with other agencies, particularly the Australian Taxation Office.[88]

Complicating the problem further is that New Zealand graduates have a tradition of travelling and living overseas in the years after study.[89]

79 Nicholas Barr, "Income Contingent Loans and Higher Education Financing," op. cit.

80 Education Counts, "Student Loan Scheme Annual Report 2015," op. cit., data tables, SLS1; Education Counts, "Student Loan Scheme Annual Report 2005," op. cit.

81 Education Counts, "Student Loan Scheme Annual Report 2015," op. cit., 32–34.

82 Education Counts, "Student Loan Scheme Annual Report 2004" (Wellington: Ministry of Education, 2004), 30.

83 How can a person with a student loan who is resident in New Zealand become an 'overdue' borrower? Most New Zealand-based borrowers repay their student loan through employer deductions using the same mechanisms as PAYE tax deductions. As long as employees get their tax code right, it is impossible to fall back on repayments. However, the self-employed and IR3 tax filers have their repayment obligations calculated from their tax return. So people who have been assessed in these instances may be late in making their repayments and become overdue. Inland Revenue, "Income Types and Adjustments for Working for Families Tax Credits and Student Loans," Website.

84 Education Counts, "Student Loan Scheme Annual Report 2015," op. cit., 34.

85 Ibid., 34.

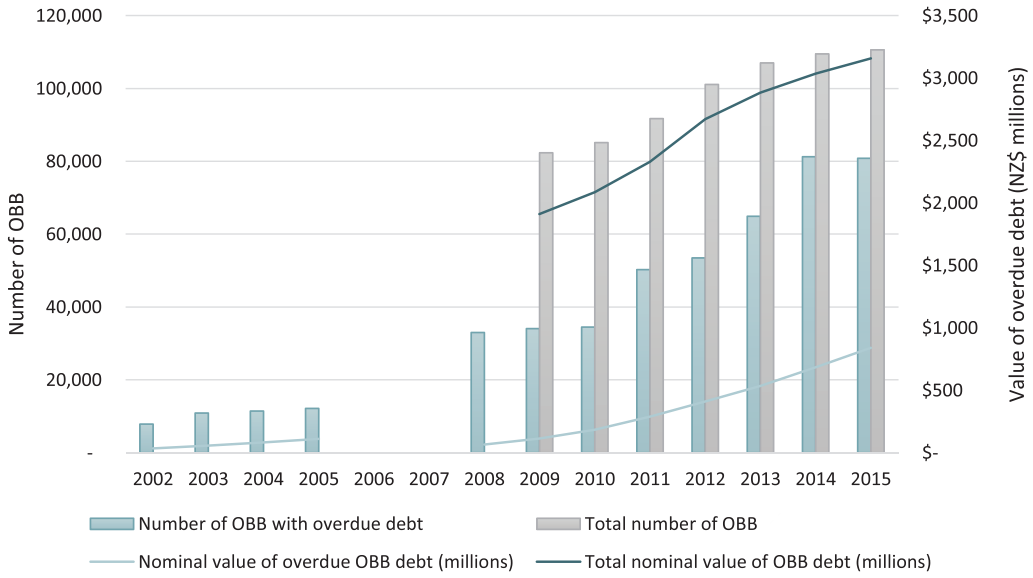
86 Education Counts, "Student Loan Scheme Annual Report 2009" (Wellington: Ministry of Education, 2009), 32.

87 Inland Revenue, "Information Sharing Arrangement with Australia for the Recovery of Student Loan Debt," op. cit., 2.

88 Ibid., 3.

89 Education Counts, "Student Loan Scheme Annual Report 2005," op. cit., 34.

Figure 5: Student loan debt owed by overseas based borrowers (2002–15)



Source: StudyLink, Student Loan Scheme Annual Reports.

Note: The relevant figures for both 2006 and 2007 are not available in the Student Loan Scheme Annual Reports.

Interest-free student loans, for those remaining in New Zealand, are likely not enough of a deterrent to graduates intent on seeing what the wider world has to offer. That the government should discourage graduates from seeking overseas experience before returning home is itself rather debatable.

Interest-free student loans discourage repayment.

Interest-free student loans induce more students to borrow, while reducing the incentives to repay loans voluntarily[90] by reducing the effective cost to students. Students face a negative real interest rate and have a strong incentive to repay loans as slowly as possible. Figure 6 traces new borrowings and repayments per year. New lending continues to increase, and annual repayments are still not matching net cash out, where repayments are equal to new lending. The 2014/15 Student Loan Scheme Annual Report projects an excess of lending over repayments for 2018/19, at $266 million compared with $404 million for 2014/15.[91] The upward spike in the 2012/13 repayments was likely motivated by the announcement that government would be ending the voluntary repayment bonus (see Chapter 1).

A Regulatory Impact Statement released in 2011 noted the dramatic increase in the uptake of loans following the introduction of the interest-free scheme – from 56% in 2006 to 71% in 2009.[92] But voluntary repayment rates fell from 9.5% in 2005 to 7.3% in 2010. In 2011, the difference between new loans issued and annual repayments (which work to lower both the nominal value and the book value of the student loan asset by the same amount, but by different proportions) was $770 million.[93] However, this was the peak year. The net difference was $404 million in 2014/15, and it is projected to decrease to about $266 million by 2018/19.[94]

90 Ministry of Education, "Student Support Package for Budget 2011," op. cit., 2.

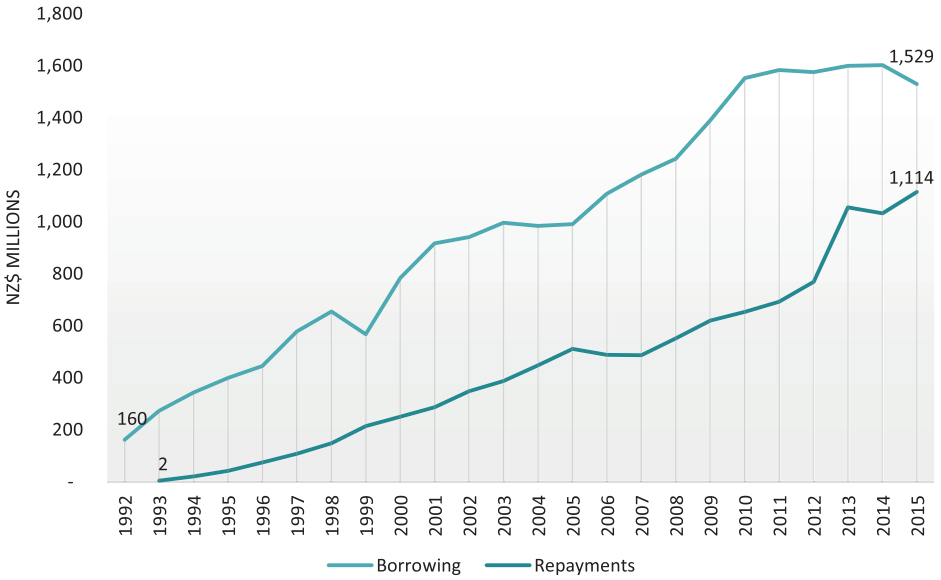
91 Education Counts, "Student Loan Scheme Annual Report 2015," op. cit., 45.

92 Ministry of Education, "Student Support Package for Budget 2011," op. cit., 2.

93 Ibid.

94 Education Counts, "Student Loan Scheme Annual Report 2015," op. cit., 45.

Figure 6: New borrowings and repayments per year (1992–2015)



Source: Education Counts, "Student Loan Scheme Annual Report 2015" (Wellington: Ministry of Education, 2015), supplementary data, Table 12.

Through greater borrowing and lower repayment, loan balances are higher than were projected when the zero-percent loans scheme was initiated. The 2006 Student Loan Scheme Annual Report projected aggregate nominal balances of $12.7 billion for the 2014/2015 year. The ending nominal balance of the student loan scheme at 30 June 2015 was $14.8 billion.

To summarise, the interest-free student loan scheme has not improved access to tertiary education, but has plausibly led to policy changes restricting access to universities. It has not reduced student debt or the repayment burden on graduates. It has not discouraged New Zealand graduates from moving overseas. But it has led to a $600 million annual transfer that largely benefits the segment of the population more likely to undertake tertiary study, which tends to be richer.

THE NEW ZEALAND INITIATIVE

CHAPTER THREE
STUDENT LOANS AND TERTIARY COSTS

Governments of all political persuasions have tinkered with every aspect of higher education, burying universities under dense sedimentary layers of conflicting rules and regulations.

— Steven Schwartz

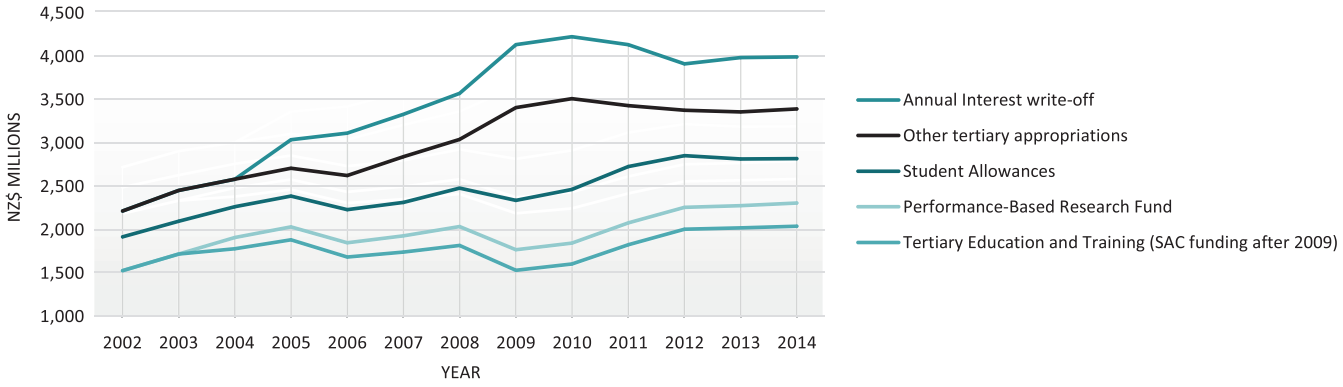
The interest-free student loan scheme has had substantial effects on overall government spending on tertiary education.

Figure 7 tallies overall tertiary expenditure from 2002 to 2014. The stacked line chart demonstrates each component's contribution to total expenditures. The lowest line is the roughly $2 billion per year allocated to tertiary education and training; from 2009 onwards, this line item was referred to as Student Achievement Component (SAC) funding and was conditional on student achievement. The next line up, the Performance Based Research Fund (PBRF), represents central government allocations rewarding tertiary institutions based on their faculty's research output. The distance between the PBRF and SAC lines, $269 million, represents total PBRF funding. The height of the PBRF line is the sum of the SAC and PBRF funding. And so on up the chart.

The uppermost line shows the annual interest write-offs as a result of the 2005 policy change; the $1.4 billion initial write-off is not included here. As interest write-offs grew, other core components of tertiary funding compressed. Compared to interest write-offs, tertiary sector core funding components appear to have followed a flatter course.

However, total student numbers peaked in 2005 and EFTS numbers peaked in 2010. The apparent compression in core funding components could have been due to the decline in student numbers from their peak. We consequently chart core student-related funding: Tertiary Education and Training (Student Achievement Component funding from 2009 onwards), Student Allowances, and interest write-offs on a per-EFTS basis.

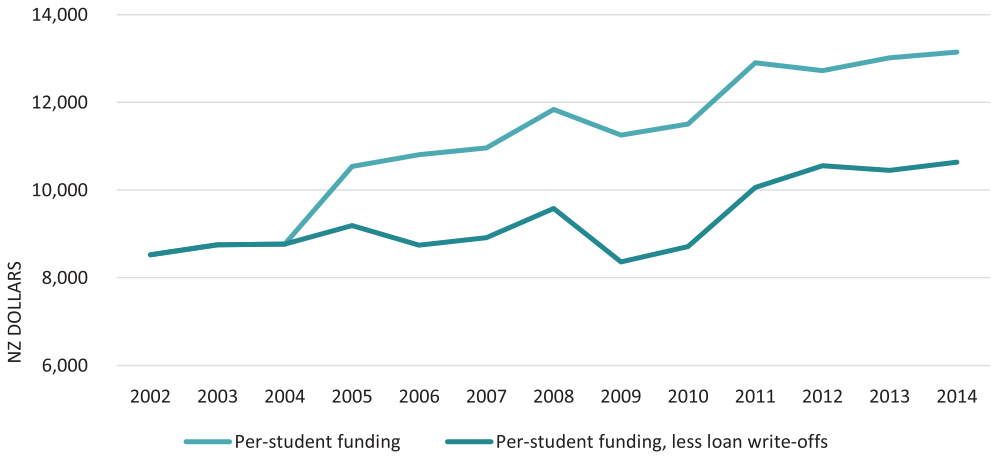
Figure 7: Annual appropriations to the tertiary sector (2002–14)



Source: All figures have been derived from The Treasury, "Vote Tertiary Appropriations" (Wellington, New Zealand Government) and StudyLink, Student Loan Scheme Annual Reports. Figures represent nominal values and are not inflation-adjusted.

Note: Funding accorded to the "Tertiary Education and Training" component ended in 2008 and was renamed the "Student Achievement" component.

Figure 8: Funding per EFTS



Source: Author's calculations from Figure 7, above, and from EFTS figures reported in Education Counts, "Student Loan Scheme Annual Report 2015" (Wellington: Ministry of Education, 2015), supplementary data, Table SLS1.

Government funding per student, barring interest write-offs, remained flat from 2005 through 2010 before increasing in 2011. Per-student funding, including the interest write-off, jumped substantially in 2005 and continued to increase. These figures do not include the initial $1.4 billion write-down on existing debt when the policy began.

While the interest-free loan policy increased the government's total cost of tertiary education, it could provide little benefit to tertiary institutions unless it allowed for increased tuition revenue.

TUITION CAPS, PAST AND PRESENT

> The fee spiral is over. This Government is committed to the ongoing stabilisation of fees, and then bringing them down over time.
>
> — Steve Maharey, Tertiary Education Minister (2005–07)

When students pay interest on student loans, the burden of any tuition increase falls on the students themselves. When loans are interest-free and students can borrow to meet any tuition increase, the government faces larger interest write-downs whenever tuition increases. If the government wishes to contain the costs it faces when student loans do not bear interest, it might seek to more tightly regulate tuition charges.

At the same time, if universities face more constrained funding lines than they otherwise might, the added imposition of capped tuition charges can strain overall funding.

Regulation of tuition charges pre-dates 2005's changes to student loans policies. In 1990, tuition was set by the government at $1,250 for all courses at all institutions. In 1992, tuition fees were deregulated. The nominal fees for a basic Bachelor of Arts degree across all seven universities increased annually by 2% in 1993 to almost 30% in 2000.[95]

In 2001, the Fifth Labour Government introduced a fee freeze that kept private tuition at 2000 levels. Tertiary institutions participating in this 'voluntary' fee-stabilisation programme received more funding in return for freezing all nominal tuition fees until 2003.[96] This form of tuition cap, which replaces forgone tuition revenue with government funding, can have regressive distributional characteristics. But if it is done properly, it need not constrain university finances.

95 These figures have been derived from comparing changes in nominal domestic tuition fees across all seven universities for a Bachelor of Arts (or other equal qualification) from 1993 to the present. Unfortunately, Universities New Zealand does not have information on tuition fees across domestic universities before 1993, which is why it is not possible to calculate a percentage change in nominal fees for 1993. Universities New Zealand, "Fees," Website.

96 Norman LaRocque, *Who Should Pay?* op. cit., 37.

ANNUAL MAXIMA FEE MOVEMENT

In 2002, a new fee maxima system was introduced to partially regulate tuition fees, effective from 2004.[97] The government could now set a maximum annual rate by which tertiary education providers could increase tuition fees. Providers had some flexibility to vary their fees (without exceeding the maxima), while increasing the affordability and certainty of the future costs of tertiary education for students.[98]

The New Zealand Vice-Chancellors' Committee, who feared tuition fee limits would restrict institutional self-management and reduce the quality or rankings of universities, where revenues per student were highly constrained by the government, vigorously opposed fee maxima.[99] The fee maxima was established in 2004, coinciding with a 3% increase in the tuition subsidy and additional tertiary funding increases announced the same year.[100]

The Annual Maxima Fee Movement (AMFM) was set at 5% from 2004 to 2006, a figure assessed by the reference group to best combine student affordability and provider flexibility.

From 2011 to 2015, the AMFM was reduced to 4%, although tertiary education providers could increase their fees by an additional 4% in exceptional circumstances.[101] The AMFM was set at 3% (on nominal fees) on 1 January 2016, the lowest since the policy was introduced in 2004.[102]

Figure 9 traces nominal tuition increases over the period from 2000 through 2016 for a Bachelor of Arts degree. The tuition cap is currently binding, with five major universities implementing the maximum fee increase from 2012 to 2016.

Figure 10 traces inflation-adjusted annual tuition charges for a Bachelor of Arts degree at five of New Zealand's main universities.

There is no particular evidence that fee maxima became more stringent with the introduction of zero-percent student loans. High inflation rates prior to 2008 eroded the real value of allowed tuition increases. The lower inflation environment that has persisted since 2011 has resulted in steady but low real increases in tuition charges. Before 2011, some universities refrained from setting fees at the annual allowed maximum; since 2011, university tuition increases have moved in lock-step.

THE COST OF TUITION CAPS

Tuition caps are intended to improve tertiary affordability. They are also intended to provide students with greater certainty about the total costs of their degree.

But when students are able to finance their education with student loans, and repayment is income-contingent, the desirability of tuition caps becomes more questionable. If tertiary institutions compete with one another strongly on price and degree quality, then tuition caps make no more sense than caps on what mechanics are allowed to charge on servicing vehicles. If, however, tertiary institutions act as local monopolists, tuition caps can act as a form of rates regulation, preventing local monopoly pricing problems.

Where student loans are interest free, sector competitiveness matters even more. If universities are local monopolists, and students are highly price insensitive, the main effect of switching to zero-percent student loans would be a sharp increase in tuition fees. If universities compete with one another, students who would go on to

97 Steve Maharey, "Fee maxima reference group appointed," Press Release (Wellington: New Zealand Government, 3 December 2002).

98 Ministry of Education, "Fee and Course Costs Maxima – Frequently Asked Questions and Answers" (Wellington: New Zealand Government).

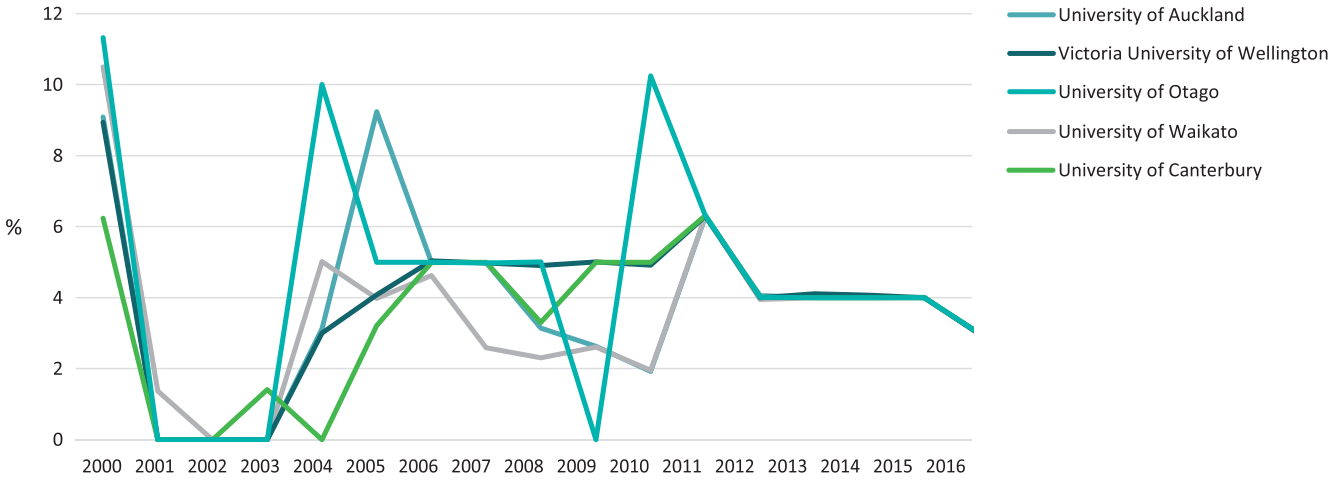
99 Norman LaRocque, *Who Should Pay?* op. cit., 37.

100 Ministry of Education, "Fee and Course Costs Maxima – Frequently Asked Questions and Answers," op. cit., 4.

101 Tertiary Education Commission, "SAC Level 3 and Above – Delivery," Website.

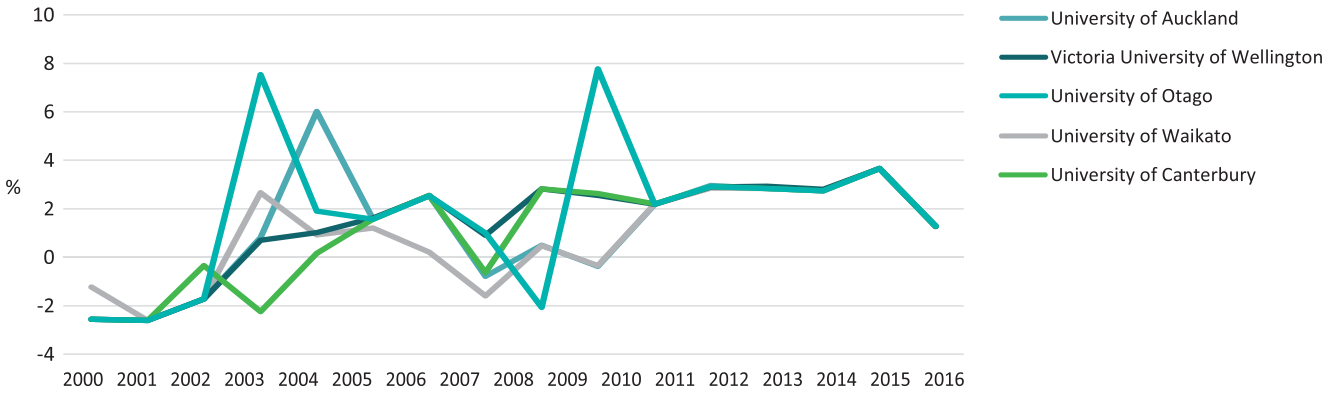
102 Ibid.

Figure 9: Nominal tuition increases (%) (2000–16)



Source: Author's calculations based on Universities New Zealand historical fees data.

Figure 10: Real annual fee changes, BA degree (2001–16)



Source: Author's calculations using RBNZ CPI data and Universities New Zealand historical fees data.

earn sufficient income to pay back their loans would be the primary beneficiaries.

The Ministry of Education found that almost 70% of undergraduate university courses in 2007 charged fees that were at or below 95% of the maximum allowed,[103] suggesting that the sector does involve some price competition. University marketing campaigns outside of their home catchments also suggest some market contestability.

In the worst case where universities faced little effective competition, do tuition caps really improve tertiary access and affordability?

Maani shows the close link between the demand for tertiary education and a student's socioeconomic background, which "operates significantly through students' academic performance and achievement".[104] Increasing the implicit per-student subsidy through tuition caps is not a "sufficient condition to increase the participation by the economically disadvantaged at the tertiary level".[105] This is because disadvantaged students not only lack the financial means to attend tertiary education, but also more frequently

103 Warren Smart, "Counting the Cost" (Wellington: Ministry of Education, 2009), Figure 8, 17.

104 Sholeh Maani, *Investing in Minds: The Economics of Higher Education in New Zealand* (Wellington: Institute of Policy Studies, 1997), as cited in Norman LaRocque, *Who Should Pay?* op cit., 35.

105 Sholeh Maani, *Investing in Minds: The Economics of Higher Education in New Zealand* (Wellington: Institute of Policy Studies, 1997), 186, as cited in Norman LaRocque, *Who Should Pay?* op cit., 36.

fail to have the requisite academic background to enter tertiary education.

Consequently, LaRocque also argues that tuition caps do less to encourage participation by low-income or at-risk groups than targeting financial assistance at the tertiary level or increasing incentives to complete secondary studies.[106]

Overall evidence that tuition fees deter enrolment seems weak where access to finance is in place and where students benefit from higher earnings. LaRocque notes there is "little hard evidence that New Zealand's tuition fee policies have unduly deterred participation in tertiary education".[107] Maani's comprehensive survey of the literature on the participation impact of tuition fees also finds that fees have not significantly affected participation in tertiary education.[108] Countries like Korea, Japan, the United States and Australia have high tertiary participation rates, despite requiring a comparatively high private contribution.[109] Even with the introduction of tuition fees in New Zealand, the number of EFTS places increased by around 73,000 between 1989 and 2000.[110] The decline in enrolment figures more recently has less to do with fees than with moves within the sector to limit entry through non-price measures.

But tuition caps also threaten the quality of teaching and research where other funding is constrained. Tertiary sector costs increase through competition for internationally mobile staff. And where productivity increases in tertiary education are weaker than in other sectors, the costs of tertiary education will outpace overall inflation.[111]

Competition for staff extends beyond other foreign universities to private sector employers in fields where productivity increases have led to higher salaries. Universities may have more limited opportunities for cost-saving forms of productivity increases. Greater productivity would typically be achieved by a higher student-to-staff ratio (larger classes). However, this could be expected to reduce the quality of the learning experience and would certainly hurt the international rankings of New Zealand universities.

Steven Schwartz argues that though advanced technology can be found all around universities today, much of it has little effect on university work. Tertiary education is still largely a "pre-industrial industry in which academics handcraft bespoke courses, deliver them to students and assess their learning".[112]

> Over the years, the acoustic of lecture theatres has improved, digital projectors have been installed, and air-conditioning has made them more comfortable but – as far as teaching is concerned – productivity gains have come mainly from increasing class sizes. As for its core teaching method it still takes one hour to deliver a one-hour lecture just as it did in the Middle Ages, when our oldest universities were founded. Over the centuries, productivity has surged in most parts of the economy, driving salaries even higher. To attract academics from alternative occupations, their wages rose as well.[113]

106 Norman LaRocque, *Who Should Pay?* op. cit., 37.

107 Ibid., 29.

108 Ibid., 29.

109 OECD, Education at a Glance 2015 (Paris: OECD Publishing, 2015).

110 Data from Ministry of Education and the most recent Student Loan Scheme Annual Report 2014/15. Including the increase of EFTS numbers enrolled at private tertiary education providers, the increase in EFTS numbers between 1989 and 2000 totals 96,000.

111 Steven Schwartz, "University Price Controls," in Christopher Coyne and Rachel Coyne (eds), *Flaws & Ceilings: Price Controls and the Damage They Cause* (London: Institute of Economic Affairs, 2015), 158–174, 166–167. Baumol's Cost Disease describes the phenomenon whereby less productive industries have to compete for workers against more productive industries and, as a result, are required to offer competitive wages, thus experiencing a rise in fixed costs despite no correlating increase in productivity.

112 Ibid., 166.

113 Ibid., 166.

Attracting reputable academics requires offering competitive wages, but competition also means salaries tend to rise faster than productivity. Tuition caps can prevent quality differentiation between universities, limiting their ability to invest in better but potentially more expensive labour and equipment. Over time, tuition caps could "adversely affect institutions' ability to attract and retain high-performing staff … and could threaten the quality of provision and lead to a running down of both human and physical capital in the tertiary sector".[114]

Tuition caps can nevertheless prove desirable if universities face little effective competition with one another. Measures to ensure greater sector competitiveness would then be desirable.

Having surveyed the state of play in New Zealand, we now see how other countries manage their student loan schemes.

THE
NEW ZEALAND
INITIATIVE

114 Norman LaRocque, *Who Should Pay?* op. cit., 37.

CHAPTER FOUR
TERTIARY EDUCATION FINANCING AROUND THE WORLD

Government-backed student loans are a common feature in most OECD countries, and help improve access to education where students might otherwise have difficulty accessing loans.

Tuition rates can vary greatly. Countries like Denmark, Finland, Iceland, Norway and Sweden combine low tuition rates with much higher income tax on graduation. Countries such as New Zealand, Australia, Canada, the Netherlands and the United States charge higher tuition, but offer substantial financial support, like the means-tested student allowances in New Zealand, to offset the high tuition fees. These latter countries also often have above-average levels of access to tertiary level education despite the comparatively high tuition fees.

Many OECD countries are torn between the conflicting challenges of increasing tertiary education enrolments and constrained budgets. Even highly subsidised systems like Denmark and Sweden look to bridge funding gaps by charging international students higher tuition rates.[115] Similar trends are being noted in New Zealand as well.

The highest private contributions towards tertiary education among OECD member countries are in South Korea, Japan, Chile, the United States and Australia.[116] In February 2016, the United Kingdom trebled undergraduate fees and cut public funding for teaching.

But what about nations like China that don't have a government-backed student loan system? How do they fix the market failure that can result where students do not have any collateral?

There is more than one way to provide student loans.

OECD'S *EDUCATION AT A GLANCE* 2015 REPORT

The OECD's *Education at a Glance 2015* report shows major differences in how various countries finance their tertiary education systems and distribute student loans.

Figures 11 and 12 compare the rate of return against the private and public tertiary tuition costs in 2011 for females and males. The rate of return on a student's investment in education depends on the tuition charged, the wages the student forgoes while studying, the wages the student can earn after graduation, and the taxes imposed on those post-graduation earnings. Low tuition rates and high after-graduation tax rates are not necessarily the best deal for students.

Sweden requires the lowest private contribution from both females and males, with the state contributing around US$97,000 per student. The public internal rate of return on investment, however, at just 0.3% per female and 3.1% per male, is a fraction of the internal rate of return on

115 OECD, "How Are Countries Around the World Supporting Students in Higher Education?" *Education Indicators in Focus* 2 (Paris: OECD Publishing, 2012), 1.

116 Private contributions towards higher education are 70.7% in South Korea, 65.7% in Japan, 65.4% in Chile, 62.2%, and 55.1% in Australia. John Morgan, "How to balance the public and private contributions to higher education," *Times Higher Education* (11 February 2016).

the private investment, at 7.3% per female and 8.3% per male.[117]

The United States and the United Kingdom require much higher private contributions of US$55,000 and US$25,000 per student, respectively. The private internal rate of return is around 12.2% per female and almost 16% per male in both countries. Despite the much higher tuition fees in both countries, graduating students there earn a higher return on their own private investments in their education.

The state contributes a share equal to the private contribution in both the United States and the United Kingdom, but the internal rate of return for the government is 4.6% per female and 7.5% per male in the United States, and 37.2% per female and 23.4% per male in the United Kingdom.

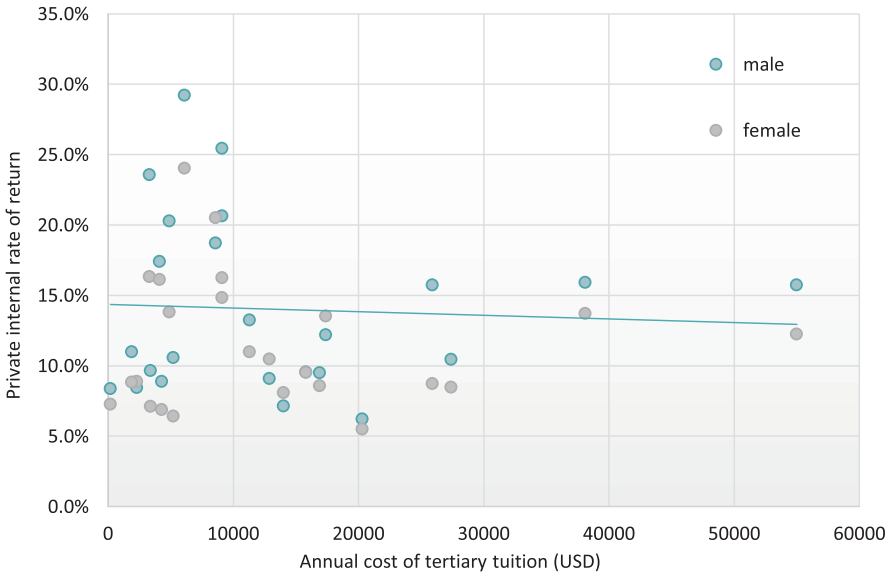
Figure 11 indicates no particular relationship between the tuition costs borne by students themselves and their internal rate of return on that private investment, though many countries whose students face annual tuition charges between US$5,000 and US$10,000 earn exceptionally high returns.

That there is little clear relationship between private internal rates of return and the tuition costs facing students is not as surprising as it might first appear. When the private costs faced by students are relatively low, many more students will enrol, thus reducing the average wage premium for college graduates. Many countries with tuition charges less than US$5,000 nevertheless have very low private returns to education. When private costs are high, the returns must be commensurately high to encourage enrolment, and fewer students might then attend.

The trend line in Figure 12 shows a clear negative relationship between the level of public per-student tertiary subsidies and the internal rate of return on that public investment.

Further data is available in the OECD data tables in Appendix A1.

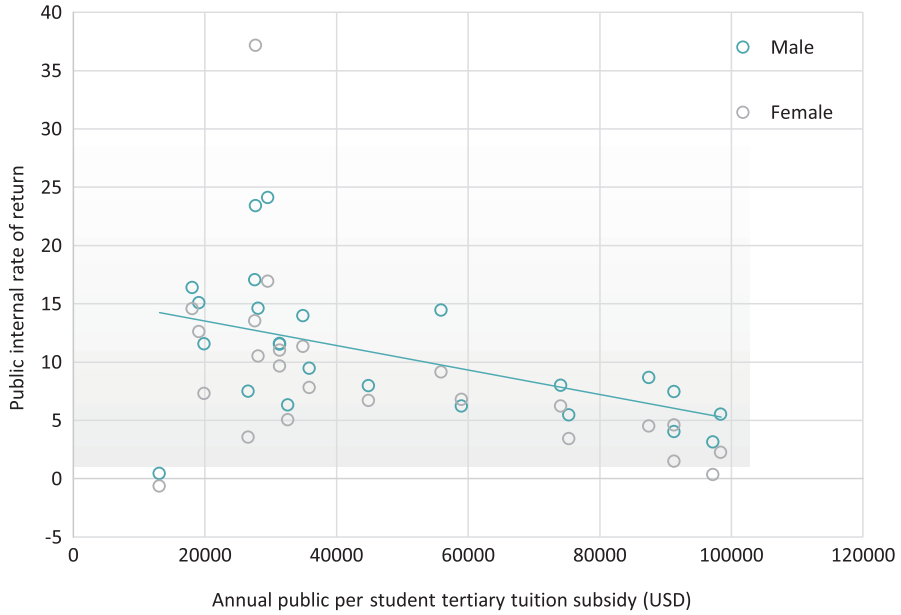
Figure 11: Internal rate of return on private investment in tertiary education among OECD member countries (2011)



Source: OECD, *Education at a Glance 2015* (Paris: OECD Publishing, 2015).

117 These calculations are based on the data provided by the OECD and the tables in Appendix A.1. The public returns on investment in tertiary education are calculated as the increase in the tax base resulting from a more educated population with higher earnings potential, the cost being public subsidisation of tertiary education. The private return on investment in tertiary education is calculated as the increased earnings as a result of acquiring more valuable human capital skills through tertiary education, the cost of that private investment including both the obvious tuition cost, in addition to the opportunity cost of lost earnings during the study period. One consideration is whether higher earnings by tertiary education graduates is a product of undertaking that higher education or a reflection of the innate ability of individuals.

Figure 12: Internal rate of return on public investment in tertiary education among OECD member countries (2011)



Source: OECD, *Education at a Glance 2015* (Paris: OECD Publishing, 2015).

STUDENT LOAN SCHEMES AROUND THE WORLD

Table 3 provides a snapshot of some interesting student loan schemes around the world. Much of the information has been gathered from a far more comprehensive comparison matrix conducted by the State University of New York at Buffalo in 2009. Programmes introduced after 2009 have been incorporated into the table where applicable.[118] See Appendix A.2 of this report for more comprehensive details.

INTERNATIONAL EXAMPLES

While government-backed student loans are the norm, interest-free loans are not. Loans typically bear interest charges at least equivalent to the CPI. Loans that decrease in real value over time as inflation eats away the value of the principal are not cheap to run, and most countries choose not to do so. Appendix A.2 provides further details on other countries' systems.

Two countries have parties other than the government backing student loans.

In Mexico, many universities are responsible for 20% of the cost if their students default on their loans. This means Mexico's universities have an incentive to accept academically capable students likely to repay their debt, and to ensure their programmes lead to employment.

In China, government-backing of student loans is means-tested. Families sufficiently wealthy to back their children's student loans do so. Needs-based scholarships and means-tested government-backed student loans are available for high-performing, poorer students.

Means-testing access to government-backed student loans, or asking universities to share in the risk if their graduates fail to earn enough to pay back their loans, are interesting ideas – but likely to be less politically popular than restoring interest on student loans. Both would allow a greater focus of public resources on those in greatest need, but

118 ICHEFAP, "Government Student Loan Programs: An International Comparison 2009," The International Comparative Higher Education Finance and Accessibility Project (Buffalo: State University of New York at Buffalo, 2009).

Table 3: Student loan programmes in selected countries

Country	Student loan programme	Eligibility	Source of capital	Risk bearer	Means-tested	Interest	Total student debt owed to government	Terms
Australia	Higher Education Loan Programme (HELP)	Available to most domestic undergraduate students enrolled at university	Government	Government	No	At inflation	AU$23 billion	▪ Income-contingent repayments ▪ Repayment required once income reaches a minimum threshold
China	General Commercial Student Loans Scheme (GCSL)	Available to students aged 18 and over enrolled in public and private sectors; parents/ guardians provide collateral	State-owned banks, commercial banks, credit-cooperative unions	Banks and co-signatories who provide collateral	Yes	Yes		▪ Not income-contingent ▪ As of 2009, interest was not subsidised by government and the repayment period was flexible
Japan	Dai-isshu Loans (JASSO)	Available to academically competent students at public post-secondary institutions	Government	Co-signatory or a guarantee agency	Yes	No		▪ Not income-contingent ▪ Maximum repayment period of 20 years ▪ Debt forgiven on occasion of a borrower's death or bankruptcy
Mexico	The National Program for Financing Higher Education	Available to students at private universities	NAFIN, federal development bank	NAFIN (80%), private universities (20%)	No	Yes		▪ Relatively new programme, so little information available on repayment schedules
The United Kingdom	Student Loans Company (SLC)	Available to all domestic and some EU students; financial aid available for tuition and living expenses	Government	Government	No	Yes	Around £65 billion in 2014/15	▪ Income-contingent repayments
The United States	Federal Perkins Loans	Available to needy undergraduate and graduate students	Split evenly between government and higher education institution	Split evenly between government and higher education institution	Yes	Yes	US$1.2 trillion in 2013	▪ Not income-contingent ▪ Maximum repayment period is 10 years based on total amount owed
	Subsidized Stafford Loans	Available to needy students enrolled at least part-time in eligible post-secondary institutions	The Federal Family Education Loan (FFEL), or the US Department of Education	Government	Yes	Yes		▪ Income-contingent repayment plan available

politics often is not about helping those in greatest need.

But we can draw some lessons from the international experience. Charging interest on student loans does not harm access to tertiary education. Rather, it allows government to focus limited resources on those in real need. Further, tuition charges higher than those that prevail in New Zealand can come with benefits at least as strong as those enjoyed by Kiwi students.

BOX 2: THE MEDIEVAL ORIGINS OF SCHOLARLY LOANS

The beginnings of scholarly loans coincided with the establishment of the first institutions of higher learning in medieval Europe in the late 11th century. Some of the world's first universities – the University of Bologna, the University of Paris, Oxford University and Cambridge University – offered degrees to young men, preparing them for positions in the Catholic Church or in government.

In 1240, Robert Grosseteste, the Bishop of Lincoln and a prominent figure in English intellectual circles, established the first documented student loan system.

St Frideswide's Chest (literally an embellished chest) was bound by two locks and each key held by a different university faculty member. The chest was kept in a religious house in central Oxford, near the college halls and student apartments.

To obtain a loan, a scholar had to be of modest means, taking an oath to that effect, and deposit a valuable object into the chest as collateral.

Objects included anything from silver spoons to gold plates, but more often than not, textbooks. These textbooks, which included works by Aristotle, the Bible, law codes and medical tracts, were quite different from the textbooks students are familiar with today. Created from animal skins and painstakingly hand-scribed, medieval textbooks were valuable objects.

These hand-scribed books often have lines on the final page recording the loans taken out by the scholar. Commonly, the value of the collateralised item was far greater than the actual value of the loan. While Petrus Lombardus' *Sententiae*, a staple in the Oxford curriculum, cost approximately 40 shillings, an entire series of lectures in the 15th century would cost a scholar around 6 shillings.

As a result, some scholars simply walked away from their debt, and the chest manager would put whatever item had been used to secure the loan back into the market.

In the early 1400s, around 20 loan chests worth millions in present dollar terms were located in the grounds of Oxford. It was mostly the nobility who either "wanted to support scholars or liked the thought of having their name associated with a chest" who loaned money to scholars. Later, loan chests were funded by professionals rather than the nobility, and opened borrowing to all scholars rather than just to those of modest means.

The demise of the chest loan system came with the invention of the printing press in the late 15th century. Books became much less valuable, and not worth collateralising. In 1624, England legalised interest-bearing loans by bankers.

With no specialised loan system, scholars in 17th century England and Europe found they were no different from other borrowers. No longer able to simply walk away from a loan, they risked suffering the same consequences as other debt defaulters, like being sentenced to a debtors' prison.

Source: Jenny Adams, "The history of student loans goes back to the Middle Ages," *The Conversation* (23 March 2016).

CHAPTER FIVE
WHERE TO FROM HERE?

It is well-meaning, [but the interest-free student loan scheme] is also one of the most expensive examples of unintended policy consequences in New Zealand's modern history.[119]

— Timothy Hazledine, University of Auckland

Maintain broad access to tertiary education through the student loan scheme …

The standard market failure argument for government-backed student loans holds that because youths entering tertiary study generally have no tangible collateral, they would be unable to obtain student loans on private markets.

Leaving the funding of tertiary education entirely to the market might lead to under-investment in the sector.[120] Collateral removes much of the risk associated with lending. If a borrower defaults on a home loan, the bank can seize the house. But students may not have collateral that could be seized in the event of a default: a bank cannot appropriate an education. Indentured servitude is illegal. Capital market imperfections that limit students' access to borrowing to finance their studies might then lead to an under-provision of tertiary education.[121]

But government-backing of student loans can also cause problems. As economist Luigi Zingales warns, where private lenders issue credit backed by government guarantees, they may be insufficiently cautious in deciding to whom to lend,[122] causing a different kind of failure.

Purdue University in the United States is experimenting with venture capital as an alternative to student loans. Investors purchase the right to a portion of a student's income for a period after graduation in return for funding the student's study.[123] The graduate's future earnings then serve as collateral. If earnings after graduation are low, investors bear that cost, which is otherwise borne by students under traditional student loans. On the upside, investors would see strong returns where graduates fare well after graduation.

New Zealand should not shift away from government-backed, income-contingent student loans. But it should watch international developments carefully. If peer-to-peer equity financing schemes like those trialled by Upstart in America[124] or venture capital schemes like Purdue's prove successful, government backing may no longer be necessary.

… but charge interest on future student loans …

Accepting the market failure case for government-backed student loans does not require interest on those loans be subsidised. Interest-free student loans seem reasonably regressive. The interest subsidy acts as a grant to all students. Under

119 Richard Meadows, "Bitter pill should be swallowed," BusinessDay.co.nz (19 January 2013).

120 Norman LaRocque, *Who Should Pay?* op. cit., xi.

121 Norman LaRocque, *Who Should Pay?* op. cit., ix.

122 Luigi Zingales, "The college graduate as collateral," *The New York Times* (13 June 2012).

123 Danielle Douglas-Gabriel, "Investors buying shares in college students: Is this the wave of the future? Purdue University thinks so," *The Washington Post* (27 November 2015).

124 *The Economist*, "Graduate Stock" (22 August 2015).

income-contingent repayment schemes, this grant is especially poorly targeted.[125]

Rapid policy change could be undesirable, and changes affecting existing loans would break existing loan contracts. A potentially attractive way forward would be to restore interest on new student borrowing beginning in a future year – say, from 2018 onwards.

Interest charges on student borrowing would allow public funding to be better targeted. It would also allow a rebalancing between public and private contributions towards tertiary education. The Productivity Commission reports that despite tuition levies, students bear only some 18% of the cost of their education, with the government providing the remaining 82%.[126]

… while increasing targeted support to remove barriers to tertiary participation.

Restoring interest on student loans would allow government to strengthen its funding of means-tested student support programmes like student allowances. But making student allowances more generous or improving needs-based scholarships (University of Auckland alone has nearly 80 different financial hardship scholarships across all levels of study[127]) for undergraduate students will have little effect if students fail academic entry requirements.

A substantial fraction of the government's savings under a return to interest-bearing student loans should be devoted to improving preparation at secondary and primary school. Enhanced numeracy and literacy preparation should be targeted at schools with more students at risk of failing to either complete National Certificate of Educational Achievement (NCEA) or progress to tertiary study. This would benefit not only those students then able to progress to tertiary study, but also students moving into the labour force directly from secondary school.

The Ministry of Education finds substantial differences in tertiary participation rates, by school decile, among students with comparable scholastic achievement.[128] Improving preparation for appropriate tertiary study is appropriate.

Even greater targeting could be achieved by means-testing student loans

The case for government-backed student loans is weaker where students have access to family resources that could provide collateral backing private loans for study. Government-backed loans would still be available to better support high-performing students whose parents do not have sufficient financial collateral for a private loan.

Restricting government-backed loans to students from households with less wealth would free up more government resources for targeted assistance and enhanced pre-tertiary preparation. It could also encourage greater competition among universities. Parents risking having to cover their child's loans in case of low post-graduate earnings would demand more information about a tertiary programme's record such as the programme's graduation rate and those graduates' job placements. However, this move could also encourage families to engage in accounting strategies to hide wealth; further study would be needed before this option could be recommended.

125 Ross Finnie, "Student Financial Aid: The Roles of Loans and Grants," Queen's University School of Policy Studies Working Paper No. 37 (2004). Absent income-contingent loan repayment schemes insuring students against the risk of low earnings after graduation, interest subsidies can reduce debt aversion among poorer students.

126 New Zealand Productivity Commission "New Models of Tertiary Education" (Wellington: New Zealand Productivity Commission, February 2016), 57.

127 For scholarships available at New Zealand's main universities, see Universities New Zealand, "Scholarships," Website. For awards available at the University of Auckland for undergraduate students in financial hardship, see University of Auckland, "Search for Scholarships and Awards," Website.

128 Ralf Engler, "School leavers' progression to bachelors-level study," (Wellington: Ministry of Education, 2010), see Figure 1, 22.

Tertiary institutions could help back student loans

Currently, taxpayers are at risk for 100% of student loan defaults. The lack of penalties for both students and universities skews the incentives for the two main parties involved in tertiary education. The current system means government needs to tighten access to student loans and impose costly monitoring regimes on universities to ensure programmes lead to loan-repaying employment.

Alternatively, tertiary institutions could accept some of the cost of their students' loan defaults as condition of enrolling students with government-backed student loans. Universities would then have stronger incentives to design programmes likely to lead to employment.

Without improvement in tertiary preparation in schools serving poorer communities, shifting the risk of default onto tertiary institutions would work against equity objectives. In other words, universities may be reluctant to take on the risk of promising students from schools known to be failing. We consequently recommend first improving tertiary preparation in schools that have historically sent few students on to tertiary study.

Ease or lift the current fee cap policy

Tuition caps can prevent quality differentiation between tertiary education providers by limiting their ability to invest in better, but potentially more expensive, labour and equipment. They also prevent tertiary institutions from maintaining quality in the face of cost pressures.

Fee caps can make sense where universities only compete weakly and where students are highly price insensitive. Zero-percent student loans covering all the costs of any tuition increase mean students only bear a fraction of the real cost when tuition rises. These together provide a case for tuition caps.

Easing or removing the fee cap would best be combined with removing the interest rate subsidy. Students facing the full costs of any tuition increase would be more price-sensitive shoppers than those facing only a portion of those costs; price competition across universities would then be stronger.

Students should also be made more aware of the extent of public subsidisation of their education. A 2012 study conducted by Victoria University found that most tertiary students substantially underestimated the degree to which taxpayers subsidised the direct costs of their education.[129] Given the substantial private benefits that accrue to students, there is room to expand the private share of costs and free up funding for other uses that might generate greater benefits.

THE NEW ZEALAND INITIATIVE

129 Rachel Baxter, "Sharing the Private and Public Costs of Tertiary Education," *Policy Quarterly* 8:2 (2012), 48–53.

CONCLUSION

Education helps equip New Zealanders from all backgrounds with the skills to succeed in life. It spurs social mobility and leads to higher future earnings, better employment opportunities, and even longer and healthier lives. Continued learning is how we shape and nurture a cultured society. Education provides us with the tools to reason against the illogical, to keep up with the constant evolution around us, and to understand trade-offs.

Equitable access to education is a key foundation for any free, fair and prosperous society. But interest-free student loans are not the best way of achieving those goals.

A decade on, tertiary participation rates are lower, student debt is higher, and loan eligibility requirements are tighter. The policy continues to cost Kiwi taxpayers millions, with little to show for it. More than $600 million was written off in 2015 alone. While government-backed student loans are defensible, subsidised interest rates are poorly targeted. Rather than focus support where it is most needed, interest subsidies benefit those graduates who go on to earn more than the loan repayment threshold.

The government should reinstate interest on student loans while improving means-tested financial assistance for academically capable students and trialling programmes to encourage higher academic achievement among at-risk groups earlier in their schooling careers.

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APPENDIX

A.1. OECD DATA TABLES

Table 4: Private costs and benefits for a woman attaining tertiary education (2011)

	Direct costs	Foregone earnings	Total costs	Earnings benefits decomposition				Total benefits[1]	Net financial returns	Internal rate of return
				Gross earnings benefits	Income tax effect	Social contribution effect	Transfers effect			
	(1)	(2)	(3) = (1) + (2)	(4)	(5)	(6)	(7)	(8)	(9) = (8) + (3)	(10)
Australia[2]	- 27 400	- 53 500	**- 81 000**	321 200	- 112 300	0	0	**207 500**	**126 500**	8.5%
Austria	- 1 900	- 61 000	**- 62 900**	432 400	- 120 400	- 81 600	0	**227 500**	**164 600**	8.8%
Belgium	m	m	**m**	m	m	m	m	**m**	**m**	m
Canada[3]	- 17 400	- 38 200	**- 55 600**	328 800	- 73 600	- 25 100	0	**227 600**	**171 900**	13.5%
Chile	- 38 100	- 32 100	**- 70 200**	463 000	- 25 900	- 75 800	- 1 300	**356 300**	**286 100**	13.7%
Czech Republic	- 3 300	- 26 600	**- 29 900**	282 400	- 56 800	- 31 100	- 3 700	**191 700**	**161 800**	16.3%
Denmark	- 4 300	- 54 400	**- 58 700**	236 600	- 98 300	0	- 13 000	**120 800**	**62 100**	6.9%
Estonia	- 4 900	- 21 000	**- 25 900**	133 200	- 27 200	- 3 700	0	**102 500**	**76 600**	13.8%
Finland	- 3 400	- 72 100	**- 75 400**	290 100	- 95 500	- 21 700	- 2 600	**169 800**	**94 300**	7.1%
France	q	q	**q**	q	q	q	q	**q**	**q**	q
Germany	- 5 200	- 72 500	**- 77 700**	326 000	- 83 300	- 68 000	0	**175 600**	**98 000**	6.4%
Greece	m	- 21 900	**m**	235 300	- 16 700	- 38 100	0	**152 900**	**m**	m
Hungary	- 9 100	- 22 200	**- 31 300**	323 200	- 93 800	- 56 600	0	**171 200**	**139 800**	16.2%
Iceland	m	m	**m**	m	m	m	m	**m**	**m**	m
Ireland	m	m	**m**	m	m	m	m	**m**	**m**	m
Israel	- 11 300	- 31 600	**- 42 900**	225 300	- 31 700	- 25 800	0	**168 400**	**125 600**	11.0%
Italy[3]	- 15 800	- 38 900	**- 54 700**	316 800	- 102 900	- 30 100	0	**179 300**	**124 600**	9.5%
Japan	m	m	**m**	m	m	m	m	**m**	**m**	m
Korea	- 20 300	- 35 000	**- 55 400**	131 600	- 900	- 10 600	0	**117 000**	**61 700**	5.5%
Luxembourg[3]	m	- 65 200	**m**	721 500	- 223 400	- 89 100	0	**407 200**	**m**	m
Mexico	m	m	**m**	m	m	m	m	**m**	**m**	m
Netherlands[3]	- 16 900	- 95 300	**- 112 200**	479 300	- 189 100	- 6 900	0	**281 600**	**169 400**	8.6%
New Zealand	- 14 000	- 55 100	**- 69 100**	206 300	- 44 100	0	- 3 300	**156 900**	**87 800**	8.1%
Norway	- 2 300	- 57 600	**- 59 900**	304 100	- 85 100	- 23 700	0	**196 300**	**136 400**	8.9%
Poland[3]	- 6 100	- 17 000	**- 23 100**	316 400	- 28 000	- 56 400	0	**233 800**	**210 700**	24.0%
Portugal	- 8 600	- 22 500	**- 31 100**	413 600	- 119 700	- 45 500	0	**248 300**	**217 200**	20.5%
Slovak Republic	- 9 100	- 24 400	**- 33 500**	233 600	- 38 400	- 31 300	0	**168 700**	**135 200**	14.8%
Slovenia	- 4 100	- 32 800	**- 36 900**	463 800	- 110 500	- 102 500	0	**246 700**	**209 800**	16.1%
Spain	- 12 900	- 46 400	**- 59 300**	284 200	- 73 100	- 18 000	0	**190 600**	**131 200**	10.5%
Sweden	- 200	- 52 100	**- 52 100**	190 400	- 43 300	- 13 300	0	**132 900**	**80 800**	7.3%
Switzerland	m	m	**m**	m	m	m	m	**m**	**m**	m
Turkey	m	m	**m**	m	m	m	m	**m**	**m**	m
United Kingdom	- 25 900	- 43 100	**- 69 000**	422 200	- 93 000	- 50 700	- 80 300	**195 600**	**126 600**	8.7%
United States	- 55 000	- 49 200	**- 104 200**	566 600	- 139 100	- 32 000	0	**390 200**	**286 000**	12.2%
OECD average	- 13 200	- 43 900	**- 57 200**	332 600	- 81 800	- 36 100	- 4 000	**208 300**	**145 200**	11.5%
EU21 average	- 8 200	- 43 900	**- 52 100**	338 900	- 89 600	- 41 400	- 5 500	**199 800**	**137 700**	12.2%

Notes: Values are based on the difference between women who attained a tertiary education compared with those who have attained an upper secondary or post-secondary non-tertiary education. Values have been rounded up to the nearest hundred.

1. Total benefit is a weighted sum of gross earnings benefits (4), income tax effect (5), social contribution effect (6) and transfer effects (7), taking into account the probability of employment and the unemployment benefits in case of unemployment. For further details, please refer to the *Methodology* section.

2. Australia: Year of reference 2009.

3. Canada, Italy, Luxembourg, the Netherlands, Poland: Year of reference 2010.

Source: OECD. See Annex 3 for notes (www.oecd.org/education/education-at-a-glance-19991487.htm).

Please refer to the Reader's Guide for information concerning symbols for missing data and abbreviations.

Table 5: Private costs and benefits for a man attaining tertiary education (2011)

	Direct costs	Foregone earnings	Total costs	Earnings benefits decomposition				Total benefits[1]	Net financial returns	Internal rate of return
				Gross earnings benefits	Income tax effect	Social contribution effect	Transfers effect			
	(1)	(2)	(3) = (1) + (2)	(4)	(5)	(6)	(7)	(8)	(9) = (8) + (3)	(10)
Australia[2]	- 27 400	- 52 200	**- 79 600**	483 700	- 172 400	0	0	**302 800**	**223 200**	10.4%
Austria	- 1 900	- 61 000	**- 62 900**	559 500	- 181 100	- 73 200	0	**306 500**	**243 600**	11.0%
Belgium	m	m	**m**	m	m	m	m	**m**	**m**	m
Canada[3]	- 17 400	- 36 800	**- 54 200**	395 000	- 121 300	- 6 400	0	**260 600**	**206 400**	12.2%
Chile	- 38 100	- 33 900	**- 71 900**	766 000	- 70 400	- 83 600	- 1 300	**587 100**	**515 100**	15.9%
Czech Republic	- 3 300	- 27 100	**- 30 400**	488 800	- 98 300	- 53 800	0	**331 900**	**301 500**	23.5%
Denmark	- 4 300	- 52 400	**- 56 700**	421 500	- 214 700	0	- 10 800	**189 900**	**133 200**	8.9%
Estonia	- 4 900	- 20 100	**- 25 000**	220 400	- 45 000	- 6 200	0	**172 200**	**147 200**	20.3%
Finland	- 3 400	- 69 200	**- 72 600**	466 100	- 177 700	- 34 000	0	**252 800**	**180 200**	9.6%
France	q	q	**q**	q	q	q	q	**q**	**q**	q
Germany	- 5 200	- 71 300	**- 76 500**	576 000	- 189 800	- 97 700	0	**295 600**	**219 100**	10.6%
Greece	m	- 26 800	**m**	234 100	- 35 900	- 37 900	0	**151 400**	**m**	m
Hungary	- 9 100	- 22 200	**- 31 300**	620 900	- 156 300	- 108 700	0	**346 900**	**315 600**	25.4%
Iceland	m	m	**m**	m	m	m	m	**m**	**m**	m
Ireland	m	m	**m**	m	m	m	m	**m**	**m**	m
Israel	- 11 300	- 31 800	**- 43 100**	371 300	- 82 900	- 44 600	0	**239 300**	**196 300**	13.2%
Italy[3]	- 15 800	- 40 200	**- 56 000**	487 500	- 184 400	- 48 600	0	**248 800**	**192 800**	9.5%
Japan	m	m	**m**	m	m	m	m	**m**	**m**	m
Korea	- 20 300	- 33 700	**- 54 000**	154 200	- 2 800	- 12 400	0	**137 200**	**83 200**	6.2%
Luxembourg[3]	m	- 61 900	**m**	946 300	- 327 000	- 110 800	0	**496 700**	**m**	m
Mexico	m	m	**m**	m	m	m	m	**m**	**m**	m
Netherlands[3]	- 16 900	- 95 000	**- 111 900**	615 300	- 273 200	- 1 300	0	**336 400**	**224 500**	9.5%
New Zealand	- 14 000	- 54 400	**- 68 400**	240 500	- 73 500	0	0	**165 500**	**97 100**	7.1%
Norway	- 2 300	- 55 900	**- 58 200**	419 100	- 152 700	- 32 700	0	**234 700**	**176 500**	8.4%
Poland[3]	- 6 100	- 18 000	**- 24 100**	495 800	- 43 900	- 88 400	0	**362 200**	**338 200**	29.2%
Portugal	- 8 600	- 24 500	**- 33 100**	522 100	- 177 300	- 57 400	0	**279 500**	**246 400**	18.7%
Slovak Republic	- 9 100	- 24 500	**- 33 600**	390 700	- 64 700	- 49 900	0	**280 900**	**247 300**	20.6%
Slovenia	- 4 100	- 33 600	**- 37 700**	593 000	- 155 900	- 131 100	0	**291 900**	**254 200**	17.4%
Spain	- 12 900	- 45 900	**- 58 800**	242 500	- 61 700	- 15 400	0	**161 500**	**102 700**	9.1%
Sweden	- 200	- 51 900	**- 51 900**	303 600	- 117 000	- 12 400	0	**169 600**	**117 700**	8.3%
Switzerland	m	m	**m**	m	m	m	m	**m**	**m**	m
Turkey	m	m	**m**	m	m	m	m	**m**	**m**	m
United Kingdom	- 25 900	- 40 700	**- 66 600**	538 400	- 121 000	- 58 100	- 1 800	**353 600**	**287 000**	15.7%
United States	- 55 000	- 46 200	**- 101 300**	861 000	- 261 800	- 48 600	0	**547 600**	**446 300**	15.7%
OECD average	- 13 200	- 43 500	**- 56 700**	477 400	- 137 000	- 46 700	- 500	**288 600**	**229 000**	14.0%
EU21 average	- 8 200	- 43 700	**- 51 800**	484 600	- 145 800	- 54 700	- 700	**279 400**	**222 000**	15.5%

Notes: Values are based on the difference between men who attained a tertiary education compared with those who have attained an upper secondary or post-secondary non-tertiary education. Values have been rounded up to the nearest hundred.

1. Total benefit is a weighted sum of gross earnings benefits (4), income tax effect (5), social contribution effect (6) and transfer effects (7), taking into account the probability of employment and the unemployment benefits in case of unemployment. For further details, please refer to the *Methodology* section.

2. Australia: Year of reference 2009.

3. Canada, Italy, Luxembourg, the Netherlands, Poland: Year of reference 2010.

Source: OECD. See Annex 3 for notes (www.oecd.org/education/education-at-a-glance-19991487.htm).

Please refer to the Reader's Guide for information concerning symbols for missing data and abbreviations.

Table 6: Public costs and benefits for a woman attaining tertiary education (2011)

	Direct costs	Foregone taxes on earnings	Total costs	Earnings benefits decomposition			Total benefits[1]	Net financial returns	Internal rate of return
				Income tax effect	Social contribution effect	Transfers effect			
	(1)	(2)	(3)=(1)+(2)	(4)	(5)	(6)	(7)	(8) = (7) + (3)	(9)
Australia[2]	- 31 400	- 6 000	**- 37 400**	112 300	0	0	**114 600**	**77 200**	9.7%
Austria	- 74 100	- 10 700	**- 84 800**	120 400	81 600	0	**197 100**	**112 400**	6.2%
Belgium	m	m	**m**	m	m	m	**m**	**m**	m
Canada[3]	- 44 900	- 3 700	**- 48 600**	73 600	25 100	0	**96 900**	**48 300**	6.7%
Chile	- 18 100	- 100	**- 18 200**	25 900	75 800	1 300	**101 600**	**83 400**	14.6%
Czech Republic	- 27 600	5 100	**- 22 400**	56 800	31 100	3 700	**104 100**	**81 700**	13.5%
Denmark	- 98 400	- 20 800	**- 119 200**	98 300	0	13 000	**112 800**	**- 6 400**	2.2%
Estonia	- 26 600	- 3 200	**- 29 800**	27 200	3 700	0	**31 300**	**1 600**	3.6%
Finland	- 91 300	7 200	**- 84 100**	95 500	21 700	2 600	**126 900**	**42 800**	4.6%
France	q	q	**q**	q	q	q	**q**	**q**	q
Germany	- 87 500	- 13 600	**- 101 100**	83 300	68 000	0	**158 600**	**57 500**	4.5%
Greece	m	- 5 200	**m**	16 700	38 100	0	**65 900**	**m**	m
Hungary	- 29 600	1 400	**- 28 200**	93 800	56 600	0	**162 500**	**134 300**	16.9%
Iceland	m	m	**m**	m	m	m	**m**	**m**	m
Ireland	m	m	**m**	m	m	m	**m**	**m**	m
Israel	- 19 900	100	**- 19 800**	31 700	25 800	0	**54 400**	**34 600**	7.3%
Italy[3]	- 35 900	- 8 000	**- 43 900**	102 900	30 100	0	**129 600**	**85 700**	7.8%
Japan	m	m	**m**	m	m	m	**m**	**m**	m
Korea	- 13 100	- 15 500	**- 28 500**	900	10 600	0	**13 600**	**- 14 900**	-0.6%
Luxembourg[3]	m	- 5 500	**m**	223 400	89 100	0	**287 300**	**m**	m
Mexico	m	m	**m**	m	m	m	**m**	**m**	m
Netherlands[3]	- 73 000	- 5 100	**- 78 100**	189 100	6 900	0	**192 700**	**114 600**	m
New Zealand	- 32 600	- 1 700	**- 34 300**	44 100	0	3 300	**51 100**	**16 800**	5.1%
Norway	- 75 300	- 11 800	**- 87 100**	85 100	23 700	0	**112 300**	**25 200**	3.4%
Poland[3]	- 19 100	- 5 600	**- 24 700**	28 000	56 400	0	**101 400**	**76 600**	12.6%
Portugal	- 31 400	- 2 700	**- 34 100**	119 700	45 500	0	**158 900**	**124 800**	11.0%
Slovak Republic	- 28 100	5 300	**- 22 800**	38 400	31 300	0	**76 800**	**54 000**	10.5%
Slovenia	- 34 900	- 9 700	**- 44 700**	110 500	102 500	0	**221 900**	**177 200**	11.3%
Spain	- 59 000	6 000	**- 53 000**	73 100	18 000	0	**105 800**	**52 800**	6.8%
Sweden	- 97 200	- 9 000	**- 106 200**	43 300	13 300	0	**65 000**	**- 41 200**	0.3%
Switzerland	- 91 300	- 18 300	**- 109 600**	73 300	28 900	0	**91 700**	**- 17 900**	1.5%
Turkey	m	m	**m**	m	m	m	**m**	**m**	m
United Kingdom	- 27 700	3 200	**- 24 500**	93 000	50 700	80 300	**225 300**	**200 800**	37.2%
United States	- 55 900	- 7 100	**- 63 000**	139 100	32 000	0	**178 300**	**115 300**	9.2%
OECD average	- 49 000	- 5 000	**- 53 900**	81 500	35 800	3 900	**123 600**	**65 500**	8.6%
EU21 average	- 52 600	- 3 900	**- 56 400**	89 600	41 400	5 500	**140 200**	**79 300**	9.9%

Notes: Values are based on the difference between women who attained a tertiary education compared with those who have attained an upper secondary or post-secondary non-tertiary education. Values have been rounded up to the nearest hundred.

1. Total benefit is a weighted sum of gross earnings benefits (4), income tax effect (5), social contribution effect (6) and transfer effects (7), taking into account the probability of employment and the unemployment benefits in case of unemployment. For further details, please refer to the *Methodology* section.

2. Australia: Year of reference 2009.

3. Canada, Italy, Luxembourg, the Netherlands, Poland: Year of reference 2010.

Source: OECD. See Annex 3 for notes (www.oecd.org/education/education-at-a-glance-19991487.htm).

Please refer to the Reader's Guide for information concerning symbols for missing data and abbreviations.

Table 7: Public costs and benefits for a man attaining tertiary education (2011)

	Direct costs	Foregone taxes on earnings	Total costs	Earnings benefits decomposition			Total benefits[1]	Net financial returns	Internal rate of return
				Income tax effect	Social contribution effect	Transfers effect			
	(1)	(2)	(3) = (1) + (2)	(4)	(5)	(6)	(7)	(8) = (7) + (3)	(9)
Australia[2]	- 31 400	- 5 800	**- 37 200**	172 400	0	0	**168 800**	**131 500**	11.6%
Austria	- 74 100	- 10 700	**- 84 800**	181 100	73 200	0	**260 100**	**175 300**	8.0%
Belgium	m	m	**m**	m	m	m	**m**	**m**	m
Canada[3]	- 44 900	- 3 600	**- 48 400**	121 300	6 400	0	**136 100**	**87 700**	8.0%
Chile	- 18 100	- 100	**- 18 200**	70 400	83 600	1 300	**149 200**	**131 000**	16.4%
Czech Republic	- 27 600	5 200	**- 22 300**	98 300	53 800	0	**156 600**	**134 200**	17.0%
Denmark	- 98 400	- 20 000	**- 118 400**	214 700	0	10 800	**226 200**	**107 800**	5.5%
Estonia	- 26 600	- 3 000	**- 29 600**	45 000	6 200	0	**56 100**	**26 500**	7.5%
Finland	- 91 300	6 900	**- 84 400**	177 700	34 000	0	**217 300**	**133 000**	7.5%
France	q	q	**q**	q	q	q	**q**	**q**	q
Germany	- 87 500	- 13 400	**- 100 900**	189 800	97 700	0	**306 500**	**205 600**	8.7%
Greece	m	- 6 400	**m**	35 900	37 900	0	**76 300**	**m**	m
Hungary	- 29 600	1 400	**- 28 200**	156 300	108 700	0	**271 200**	**243 000**	24.1%
Iceland	m	m	**m**	m	m		**m**	**m**	m
Ireland	m	m	**m**	m	m	m	**m**	**m**	m
Israel	- 19 900	100	**- 19 800**	82 900	44 600	0	**121 300**	**101 500**	11.6%
Italy[3]	- 35 900	- 8 300	**- 44 200**	184 400	48 600	0	**226 900**	**182 700**	9.4%
Japan	m	m	**m**	m	m	m	**m**	**m**	m
Korea	- 13 100	- 14 900	**- 27 900**	2 800	12 400	0	**17 200**	**- 10 800**	0.5%
Luxembourg[3]	m	- 5 200	**m**	327 000	110 800	0	**408 000**	**m**	m
Mexico	m	m	**m**	m			**m**	**m**	m
Netherlands[3]	- 73 000	- 5 100	**- 78 100**	273 200	1 300	0	**272 600**	**194 600**	m
New Zealand	- 32 600	- 1 700	**- 34 300**	73 500	0	0	**74 300**	**40 000**	6.3%
Norway	- 75 300	- 11 400	**- 86 800**	152 700	32 700	0	**192 600**	**105 800**	5.5%
Poland[3]	- 19 100	- 6 000	**- 25 000**	43 900	88 400	0	**143 100**	**118 100**	15.1%
Portugal	- 31 400	- 3 000	**- 34 300**	177 300	57 400	0	**211 800**	**177 500**	11.5%
Slovak Republic	- 28 100	5 300	**- 22 800**	64 700	49 900	0	**123 100**	**100 400**	14.6%
Slovenia	- 34 900	- 9 900	**- 44 900**	155 900	131 100	0	**284 300**	**239 400**	14.0%
Spain	- 59 000	5 900	**- 53 100**	61 700	15 400	0	**100 700**	**47 600**	6.2%
Sweden	- 97 200	- 9 000	**- 106 100**	117 000	12 400	0	**128 800**	**22 700**	3.1%
Switzerland	- 91 300	- 18 500	**- 109 700**	125 200	36 200	0	**161 900**	**52 200**	4.0%
Turkey	m	m	**m**	m	m	m	**m**	**m**	m
United Kingdom	- 27 700	3 100	**- 24 700**	121 000	58 100	1 800	**191 800**	**167 100**	23.4%
United States	- 55 900	- 6 700	**- 62 600**	261 800	48 600	0	**334 200**	**271 700**	14.5%
OECD average	- 49 000	- 5 000	**- 53 900**	136 600	46 300	500	**185 800**	**127 400**	10.6%
EU21 average	- 52 600	- 4 000	**- 56 400**	145 800	54 700	700	**203 400**	**142 200**	11.7%

Notes: Values are based on the difference between men who attained a tertiary education compared with those who have attained an upper secondary or post-secondary non-tertiary education. Values have been rounded up to the nearest hundred.

1. Total benefit is a weighted sum of gross earnings benefits (4), income tax effect (5), social contribution effect (6) and transfer effects (7), taking into account the probability of employment and the unemployment benefits in case of unemployment. For further details, please refer to the *Methodology* section.

2. Australia: Year of reference 2009.

3. Canada, Italy, Luxembourg, the Netherlands, Poland: Year of reference 2010.

Source: OECD. See Annex 3 for notes (www.oecd.org/education/education-at-a-glance-19991487.htm).

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A.2. INTERNATIONAL COMPARISONS

Australia

Government-backed student loans and tuition subsidies help relieve the costs of tertiary education in Australia. Income-contingent tertiary tuition loans were first introduced in 1989 by the Hawke-Labor Government through the Higher Education Contribution Scheme (HECS). All tertiary students were charged a flat fee of AU$1,800, and the government paid the balance. Like most income-contingent schemes, HECS allowed tertiary students to defer payment while studying and make repayments through the tax system once their income reached a threshold.

Between 2005 and 2006, university fees were deregulated under the Howard reforms, permitting universities to increase fees by up to a maximum of 25%. This was mainly to increase university revenue and promote competition between institutions. The HECS system was replaced by the Higher Education Loan Programme (HELP) for student loan disbursement.

HELP loans do not accrue interest like conventional loans and carry no administration charges, but are indexed to CPI on 1 June each year.[130] In 2007, access to student loans was restricted to seven years of full-time study.[131] By 2010, around 2.5 million Australian students had taken out HELP student loans, and average student debt stood at AU$13,600.[132] In 2013, the Australian government was owed approximately AU$23 billion in tertiary student debt.

Australian students take on average 8.4 years to repay their loan.[133] While New Zealand students pay 12% of pre-tax income after their income reaches NZ$19,084, Australian students pay 4% until they earn AU$51,309 and 8% when they make AU$95,288 or more.[134]

Canada

The Australian system is largely comparable to New Zealand's. Canada's is a little more complicated.

Canada Student Loans (CSL) are offered to full-time and part-time post-secondary students in most provinces and territories. Eligibility is restricted to Canadian citizens, permanent residents who have resided in a Canadian province for more than a year, and protected persons.[135]

The loans supplement rather than replace the financial contributions expected by students and their families. Loans are interest-free for full-time students for up to 340 weeks.[136]

Students must re-apply every year to receive loan funding. They are also required to give loan providers proof of enrolment (issued by educational institutions) within six months of finishing their last study period to maintain interest-free status while studying. Students may also qualify for Canada Study Grants, Canada

130 The percentage change in the Education CPI for 2014–15 was 5.5%. Australian Bureau of Statistics, "Consumer Price Index, Australia, Dec 2015," Website.

131 Study Assist, "FAQs – Which HELP Loan Am I Eligible For?" Website (Canberra: Government of Australia).

132 Leonie Doyle, "Trans-Tasman differences in student loans" Parliamentary Library Research Paper (Canberra: Government of Australia, 28 November 2013).

133 Ibid.

134 Ibid.

135 Service Canada, "Canada Student Loans Program," Website. The Canadian federal government is responsible for funding the Canada Student Loan Program (CSLP), the entity tasked with dealing with Canadian student loans.

136 Government of Canada, "Investing in Your Future – Canada Student Loans Program for Full-time Students," Website, 2. For first-time borrowers who have been granted a Canada Student Loan on or any time after 1 August 1995, interest-free assistance is restricted to 340 weeks or 6.5 years of study. Students in doctoral programmes are eligible for an additional 60 weeks. Students with permanent disabilities (400 weeks maximum), and those who received their first Canada Student Loan prior to 1 August 1995, are eligible for up to 520 weeks (or 10 years) of interest-free higher education assistance.

Access Grants, and Canadian Millennium Bursary – all non-repayable forms of student financial assistance. Canadian students looking to study full-time at certain designated institutions abroad may be eligible for a CSL.[137]

Repayments for all CSLs begin after a borrower graduates, leaves a tertiary institution (with or without a complete qualification), or exceeds the maximum lifetime limit available for obtaining a CSL – and continues until the total debt has been repaid regardless of degree completion, employment status, or satisfaction with education achieved.[138] However, borrowers are allowed a six-month grace period (during which interest still accumulates on the principal)[139] before the initial loan payment is due. This can help students budget and manage repayments responsibly. When starting repayments, borrowers may choose between a fixed (prime plus 5%) or a floating (prime plus 2.5%) interest rate.[140] Borrowers are required to finalise the amount owed, the interest rate, the bank accounts used to repay the loan, the monthly amount to be withdrawn, a date each month for automatic withdrawals, mode of monthly repayments, and the length of the repayment period.[141]

If no repayments are made, borrowers are considered delinquent and at risk of defaulting, with serious implications for the individual's credit rating. But students can receive debt management assistance from the National Student Loans Service Centre of Canada.

137 Service Canada, "Canada Student Loans Program," op. cit., 9.

138 Ibid., 14.

139 Government of Canada, "Paying Back Your Canada Student Loan," Website.

140 Government of Canada, "Investing in Your Future – Canada Student Loans Program for Full-time Students," op. cit., 15.

141 Government of Canada, "Paying Back Your Canada Student Loan," op. cit.

Chile

Since the early 1980s, participation in Chilean higher education has increased substantially – from 7.2% in 1981 to 27.8% in 1996 and 37.5% in 2005.[142] In 2012, more than 1 million students were enrolled in tertiary institutions, compared to fewer than 250,000 in 1990.[143]

Despite his deplorable human rights violations, Augusto Pinochet pursued a number of free-market policy reforms in Chile, particularly in higher education, under the guidance of Chicago-trained economists. In 1981, the tertiary education system was divided into three sectors (universities, professional learning institutes, and technical training centres) to better identify and train the professionals and technicians required by an emerging economy.[144]

Tuition fees were introduced along with a university loan system in 1981,[145] and measures to increase competition between universities and "emphasizing those careers of greater tradition and prestige".[146] Until 2007, the means-tested loan scheme covered tuition at traditional universities at 2% interest,[147] with income-contingent repayments beginning after a two-year grace period (during which no repayments were required nor interest charged). Repayment rates were 5% of the borrower's earnings for a maximum of 15 years, after which the balance was written off.[148]

142 ICHEFAP, "Higher Education Finance and Cost Sharing in Chile," The International Comparative Higher Education Finance and Accessibility Project (Buffalo: State University of New York, 2006), 1.

143 Gregory Elacqua, "Chile's Students Demand Reform," *Americas Quarterly* (Winter 2012).

144 ICHEFAP, "Higher Education Finance and Cost Sharing in Chile," op. cit., 1.

145 Ibid., 2.

146 Ibid.

147 Does not stipulate whether the interest rate levied on student loans in Chile is on top of the inflation rate. Inflation in Chile has exceeded 4% over the past two years. Trading Economics, "Chile Inflation Rate – 1951–2016," Website.

148 ICHEFAP, "Higher Education Finance and Cost Sharing in Chile," op. cit., 2–3.

In 2005, a new needs-based student loan system was introduced for all accredited institutions. The loans are guaranteed by the state (risk of non-repayment) and the higher education institution (risk of drop-outs).[149] Private financial institutions are responsible for financing the scheme, and payments are made directly to the institutions. Private financial institutions were also tasked with managing debt collection, beginning 18 months after graduation.[150]

Even though Chile's student loans are designed to help poorer students overcome the financial burden of attaining a post-secondary qualification, the costs of tertiary education are a significant financial burden for students even from middle-class families.[151] In 2014, Chile's newly elected socialist President Michelle Bachelet announced a series of multimillion-dollar education reforms and investment. "Chile needs and the people have clamoured for this reform, which must transform quality education into a right".[152] In 2015, Bachelet passed legislation granting free education for students from the poorest 50% of families. "Tuition-free university education will make Chile a more just and supportive country for all", said Bachelet.[153]

China

In 1999, China introduced an experimental student loan programme in eight cities (in 2001, the loan programme was labelled as still being "in transition").[154] However, these loans are not government-backed. Instead, students are required to have parents or other family members as co-signatories and pledge collateral towards private bank loans in case of default.[155] Such restrictions mean loans cannot be easily accessed by poorer students.

The interest rate levied on student loans was the main commercial rate (10.8% in 1999[156]), with half the interest paid by the Chinese government and the other half by the borrower. Despite the interest bonus, the maximum repayment period of four years is onerous for many potential borrowers.[157] As of 2009, no interest charges were subsidised by the government and the repayment period was flexible.[158]

However, a 2009 study comparing government student loan programmes around the world noted that China has bank loans available to help poorer students pay for tuition fees and living expenses if they are enrolled in regular higher education institutions.[159] Interest (at rates set by the People's Bank of China) is applied on the original loan balance right from the start, but fully subsidised by the government while a student is studying. Graduates are granted a two-year grace period before repayments are made, and there are full-balance write-offs if graduates work in economically under-developed areas of China.

Japan

Japan offers two types of student loans for higher education.

Also called a first-class loan, *dai-isshu* is issued by Japan Student Services Organisation (JASSO),

149 Ibid., 3.

150 Ibid.

151 Gregory Elacqua, "Chile's Students Demand Reform," op. cit.

152 Jonathan Franklin, "Chile students debt goes up in smoke," *The Guardian* (24 May 2014).

153 John Morgan, "How to balance the public and private contributions to higher education," op. cit.

154 Bruce Johnstone, "Student Loans in International Perspective: Promises and Failures, Myths and Partial Truths," Paper presented at the International Conference on the Financing of Higher Education in Eastern and Southern Africa: Diversifying Revenue and Expanding Accessibility (Dar es Salaam, Tanzania: 24–26 March 2002).

155 Ibid.

156 Inflation in China has fluctuated around the 2% or below mark over the past two years. Trading Economics, "China Inflation Rate – 1986–2016," Website.

157 Bruce Johnstone, "Student Loans in International Perspective: Promises and Failures, Myths and Partial Truths," op. cit.

158 ICHEFAP, "Government Student Loan Programs: An International Comparison 2009," op. cit.

159 Ibid.

an independent administrative institution[160] for public-sector education at the high-school, junior college, university and specialised training college levels.[161] *Dai-isshu* are means-tested and academically selective.[162] The loans carry no interest, and are approved for students with a high level of academic performance and a minimum 3.5 grade point average (out of a maximum 5). Eligibility is also determined by annual household income of less than 10 million yen (NZ$132,000). As in New Zealand, debt is forgiven in case of a borrower's death. But, unique to Japan, debt is also forgiven in case of disability or achievement of an outstanding academic result.[163] Like in Canada, there is a repayment grace period of six months after leaving school. The maximum repayment period is 20 years and JASSO calculates the repayment period according to the total loan amount. Repayments are automatically deducted from a borrower's bank account in monthly or semi-annual instalments. Overdue repayments are subject to a 10% annual interest penalty, pro-rated by the number of delayed days. In 2006, around 241,400 students enrolled in 2–4 year programmes received an interest-free loan.[164]

The second-class of interest bearing loan is called *dai-nishu*.[165] It is also means-tested and available for public sector tuition and maintenance expenses at junior colleges, universities and specialised training colleges.[166] However, unlike *dai-isshu*, this loan is not subject to academic standards and carries a 3% interest rate.[167] Debt is still forgiven in case of death or disability. The grace period and maximum repayment periods are identical to first-class loans, with JASSO calculating the approximate repayment period based on the total loan amount.[168] In 2006, 491,143 students had received an interest-bearing loan.[169]

Mexico

Mexico is one of "Latin America's last remaining bastions of state-funded higher education".[170] Around 3 million Mexican students are enrolled in public tertiary institutions, most of which are largely tuition-free. Mexico's public sector accounts for more than 90% of the country's research output, and public tertiary institutions are highly regarded as vehicles for national social advancement, having produced many of the nation's professionals and presidents.

The student loan system in Mexico is characterised by the presence of both private and public tertiary education providers.

In 2012, the Mexican government announced its first nationwide student loan programme of US$200 million for more than 23,000 students in 25 private tertiary institutions.[171] These loans were to be issued by private banks and guaranteed up to 80% by the federal development bank, NAFIN. The loans are not subsidised by the government and carry a 10% interest.[172] The programme is also not universal. Loans are restricted to a small group of private universities that have agreed to cover the 20% risk of potential default on student loans.[173]

The loan programme was introduced following an OECD review of Mexico's tertiary education system

160 Yen for Living, "Beware of bureaucrats bearing student loans," *Japan Times* blog (20 February 2012).

161 ICHEFAP, "Government Student Loan Programs: An International Comparison 2009," op. cit., 5.

162 Ibid., 5.

163 Ibid.

164 Inflation in Japan has been fluctuating at around 0.5% or lower over the past year, after falling from almost 4% in mid-2014. Trading Economics, "Japan Inflation Rate – 1958–2016," Website.

165 Yen for Living, "Beware of bureaucrats bearing student loans," op. cit.

166 ICHEFAP, "Government Student Loan Programs: An International Comparison 2009," op. cit., 5.

167 Ibid.

168 Ibid., 5.

169 Ibid.

170 Ibid.

171 Marion Lloyd, "The Dangers of Mexico's New Student-Loan Program," *The Chronicle of Higher Education* (30 January 2012).

172 Inflation in Mexico has been around 2–3% over the past year. Trading Economics, "Mexico Inflation Rate – 1974–2016," Website.

173 Ibid.

in 2008. The review recommended greater private-sector involvement to boost Mexico's tertiary enrolments, which are low by Latin American standards. The gross enrolment rate in Mexico in 2009 was 27%, far below the 37% in Latin America and 69% in Argentina.[174]

Proponents of Mexico's new loan programme say it will improve access to tertiary education for those it might "benefit the most".[175] However, opponents claim Mexico's loan system primarily benefits the banks. President Filipe Calderon (2006–12), who introduced the programme, insisted that the 10% interest rate was "highly affordable". However, this interest rate is much higher than in many other similar countries. The closest high interest rate is roughly 6% in the United States and South Korea.[176]

Nevertheless, private universities taking on a 20% risk of default is interesting. Shifting some of the default risk from government to tertiary institutions changes the incentives for universities. If universities are on the hook for 20% of a student's loan obligations, they are less likely to accept a student with a low academic record and who might not earn enough to repay that loan.

Sweden

Equity is the hallmark of the Swedish education system. With a population of just over 9.5 million, Sweden is known for maintaining a generous welfare system, providing compensation for life-changing events such as illness or retirement. The corollary is that Sweden's tax revenue, at 45.8% of GDP in 2010, is among the highest across all OECD countries. While Sweden enjoys high employment rates (around 82% for all levels of education), post-tax earnings are also relatively low compared to other OECD countries.[177]

Enrolment is very high in Sweden, with 90% of Swedish 3-year-olds attending school (the OECD average is 69%). At just 10%, Sweden also boasts one of the lowest percentages of young people neither in education nor employed (NEETS) (the OECD average for 2014 was 16.3%[178]). Around 91% of 24–35 year-olds have at least an upper secondary education (the OECD average is 82%).[179]

All pre-primary, primary, secondary and post-secondary non-tertiary education is publicly funded. While the rest of the world seems to be shifting towards a higher share of private funding in tertiary education over the past decade, Sweden has maintained its high level of public spending in higher education (89.8%), allocating around US$19,961 per tertiary student, per year (the OECD average is US$13,719).[180] Both public and government-dependent private tertiary institutions do not charge tuition fees for Swedish nationals; tertiary tuition has recently been introduced for some international students.[181]

As tertiary education is free in Sweden, financial aid primarily covers a student's living costs during study. Financial aid is also designed to "level out the differences between individuals and groups in the population so as to make society fairer".[182] The Swedish Board for Study Support (CSN) approves three kinds of financial aid for higher education: a student grant (1,050 kronor per month); a supplementary allowance (285–855 kronor per month); and a boarding supplement (1,190–2,350 kronor per month).[183] All students are eligible for the basic student grant as long as they are aged 16–20 years, enrolled in full-time tertiary study, and attending an approved institution. The supplementary allowance and boarding

174 Marion Lloyd, "The Dangers of Mexico's New Student-Loan Program," op. cit.

175 Ibid.

176 ICHEFAP, "Government Student Loan Programs: An International Comparison 2009," op. cit.

177 OECD, "Sweden – Country Note," *Education at a Glance 2012* (Paris: OECD Publishing, 2002), 1.

178 OECD, Education at a Glance 2015, op. cit., 378.

179 Ibid.

180 OECD, "Sweden – Country Note," op. cit., 3.

181 Ibid.

182 Government Offices of Sweden, "Financial Aid for Studies," Website.

183 CSN (National Board of Student Aid), "What is a Study Allowance," Website (Sweden: Ministry of Education and Research).

supplements are based on familial wealth and distance between a student's home and place of study.[184]

The interest applied to any financial aid loan is set by the government and based on its average borrowing costs over the past three years. The annual repayment amounts are adjusted upwards by around 2% annually. CSN calculates repayments using a "special instalment formula" that increases annual repayments until the loan is repaid in full.

The United Kingdom

The United Kingdom is renowned for its famous universities. With grounds that have graced countless movie sets and history books, many academics dream of being accepted into the likes of Cambridge, Oxford or University College London.

Higher education in the United Kingdom has traditionally catered to the elite. In the 1960s, only around 4% of the total eligible population attended a British university and almost all costs, for both teaching and research, were covered by the state. By the early 2000s, only 50 years later, 45% of the eligible UK cohort were participating in higher education.[185]

Higher education student loans and grants are primarily funded through the Student Loans Company (SLC), a non-departmental public body. Established in 1990, the SLC assists students with living costs through low-interest loans.[186] At the time it was introduced, though, higher education was largely tuition free, so students didn't have to borrow funds to pay for tuition.

In 1997, the National Committee of Inquiry into Higher Education, under Sir Ronald Dearing, studied the future of higher education in the United Kingdom. The committee recommended greater private contribution (25%) towards the costs of tertiary education given the high wage premium and private benefits enjoyed by graduates,[187] but also that grants should continue.[188] Education Secretary David Blunkett introduced means-tested tuition fees in 1997,[189] and the Labour Government, led by Tony Blair, passed the *Teaching and Higher Education Act 1998* to introduce annual tuition fees of £1,000.[190]

One of the most significant reforms to tuition fees since 1998[191] saw tuition fees increase from £1,000 per year to a maximum of £3,000 per year under the *Higher Education Act 2004*.[192] In 2012, however, the United Kingdom tripled the maximum annual tertiary fee to £9,000.[193]

Since 2012, domestic and many EU students studying in the United Kingdom have been eligible for tuition loans covering course fees and maintenance loans to help with living costs such as accommodation, bills and books. Full-time students can borrow up to £9,000 a year for tuition

184 Ibid.

185 Andrei Ruckenstein, Mark Smith and Nicola Owen, "How can we make UK higher education sustainable?" *Times Higher Education* (25 February 2016).

186 SLC, "Student Loans Company UK," Website.

187 Ron Dearing, "Higher Education in the Learning Society," *The Dearing Report* (London: Her Majesty's Stationery Office, 1997), 287–290.

188 Stuart Alley and Mat Smith, "Timeline: Tuition fees," *The Guardian* (28 January 2004).

189 Ibid.

190 Tuition fees were to be paid by all but the poorest students as of 1998/1999. Around 30% of tertiary pupils were not required to pay tuition fees because their income or that of their parents or spouses is too low. Another 30% with family incomes of less than £35,000 pay less than the maximum level for 1998/99 of £1,000. The maintenance grant for living expenses was replaced with loans from 1999/2000. Repayment of loans was at the rate of 9% of a graduate's income, once it is above £10,000. A supplementary hardship loan to the value of £250 was available. Changes also saw bursaries for students entering teacher training or health and social care courses; employers were invited to consider bursaries for other areas. BBC, "Teaching and Higher Education Act," Website.

191 Stuart Alley and Mat Smith, "Timeline: Tuition Fees," op. cit. This article contains a comprehensive list of changes to tuition fees in the United Kingdom between 1996 and late 2004.

192 Higher Education Act 2004 (UK).

193 Javier Espinoza, "University students in England 'pay the highest tuition fees in the world'," *The Telegraph* (24 November 2015).

fees and up to £7,675 a year for maintenance costs. If a student were to borrow the maximum amount available, the total loan debt would be just over £50,000.[194] The total value of outstanding loans owed to the British Government currently stands at around £65 billion, and is expected to reach £100 billion in 2018.[195]

Student loans in the United Kingdom are income-contingent, the minimum repayment threshold being a salary of £21,000 a year (before tax or National Insurance). The monthly repayments are 9% of income over £21,000, so, as is the case in New Zealand, the more you earn, the greater the personal repayment contribution towards your loan.[196]

Interest on the borrowing is calculated separately and starts accumulating while a student is studying, at a rate of RPI (Retail Price Inflation) inflation plus 3%. However, when a student graduates and begins earning a wage, interest is calculated according to the income on a sliding scale, so higher earners pay a higher rate of interest.[197] Graduates earning £21,000 or less pay interest at the rate of RPI inflation only. Those earning between £21,000 and £41,000 pay interest at RPI plus 0.15% per £1,000 of pre-tax salary. Those earning more than £41,000 pay RPI plus 3% interest, the maximum interest rate applied to a student loan. Interest continues to accumulate until the loan is repaid in full. Any unpaid debt after 30 years is written off.[198]

The United States

Tuition can vary substantially across tertiary institutions in the United States, with the most prestigious institutions charging premium tuition rates. In 2013, one year's worth of tuition at Harvard College could cost around US$57,950, although many students who do attend the likes of Harvard have tuition defrayed through scholarships.[199] By comparison, the average annual tuition for a first-year, full-time student living on campus, enrolled in a standard four-year degree, costs about $27,453.[200]

US media outlets frequently circulate stories of the country's crippling student debt burden, the nominal value of which reached US$1.2 trillion in late 2013.[201] But headlines depicting students drowning in debt of more than US$100,000 are often hyperbolised. *The Atlantic* reported in 2013 that of the total indebted students, 1.2% owe more than US$100,000, while the majority of borrowers (43%) owe US$1,000–$10,000.[202] Nevertheless, consistent with rest of the world and given the wage premium enjoyed by college graduates, higher education in the United States is considered a strong investment for individuals. The unemployment rate for an individual with no high school diploma is around 14%, and 5% for those with a bachelor's degree.[203]

At present, almost 20 million American undergraduate students are enrolled in post-secondary education.[204] In 2013, of total first-time, full-time undergraduate students, around 50% received student loans to help fund the costs of attending university.[205] The federal government system creates a slightly more complex system than in New Zealand, but student loans there can

194 Nicole Blackmore, "How the student loan scheme works," *The Telegraph* (24 August 2013).

195 House of Commons Library, "Student Loan Statistics," Briefing Paper No. 1069 (20 January 2016), 29.

196 Nicole Blackmore, "How the student loan scheme works," op. cit.

197 Ibid.

198 Ibid.

199 Nicole Allan and Derek Thompson, "The myth of the student-loan crisis," *The Atlantic* (March 2013).

200 Ibid.

201 Chris Denhart, "How the $1.2 trillion college debt crisis is crippling students, parents and the economy," *Forbes* (7 August 2013).

202 Nicole Allen and Derek Thompson, "The Myth of the Student-Loan Crisis," op. cit.

203 Ibid.

204 National Center for Education Statistics (US), "Undergraduate Enrollment," Website.

205 National Center for Education Statistics (US), "Student Loan Volume and Default Rates," Website.

broadly be split into federal loans and private student loans.[206]

Federal loans can be applied through Free Application for Federal Student Aid (FAFSA) and are of two types: subsidised (the government pays the interest while the student is studying at least half-time) and unsubsidised. Student loans may be used for any college-related expenses, including tuition, room and board, books, computers and transportation.

The federal government oversees and regulates three kinds of federal loans: Direct Loans (where the US Department of Education is the lender); Federal Family Education Loans (where private lenders make loans backed by the federal government); and Federal Perkins Loans.[207]

Federal Perkins loans are available to financially needy undergraduate and graduate students, the total value of the loan being split evenly between the government and the higher education institute. Undergraduates can borrow up to US$4,000 per year, with the loan made through participating schools to students who demonstrate great financial need. Loans are repaid by students directly to the higher education institute; the interest is 5%; and the maximum repayment period is capped at 10 years, dependent on the total amount owed.[208]

Subsidized Stafford Loans are available to all needs-based students enrolled at least half-time in an eligible post-secondary institution. A maximum amount of US$23,000 can be borrowed under this conventional loan. The interest rate is adjusted annually, but may not exceed 8.25%. The government pays all interest accruing on the principal while the borrower is studying, and for a six-month grace period after leaving the institution or graduation. Repayment depends on one of four plans chosen: standard repayment of up to 10 years; extended repayment from 12 to 30 years; graduated repayment with increasing monthly repayments from 12 to 30 years; and income-contingent repayment based on adjusted gross income.[209]

Unsubsidized Stafford Loans are non-needs based, and are available to all students enrolled in at least part-time study at an eligible post-secondary institution. The maximum borrowable amount is US$31,000, with no in-school grace period. Interest accumulates upon the loan being distributed. As with a Subsidized Stafford Loan, the interest rate is adjusted annually, but may not exceed 8.25%. Repayment of the principal begins after a six-month grace period, with the same repayment plans available as under Subsidized Stafford Loans.[210]

PLUS loans (Federal Parent Loan for Undergraduate Students) are available to the parents of undergraduate students and are not needs-based. There is no stated maximum borrowable amount, but the federal government advises parents it should not exceed a students' "unmet financial needs".[211] The PLUS loan is a conventional loan with an 8.02% interest. Repayment options are similar to those discussed above, but borrowers are not eligible for the income-contingent repayment plan option.

Private loans are available for undergraduate students not eligible for any type of federal loan. However, the Federal Trade Commission emphasises that these loans should be a last resort, as they have higher fees and interest rate charges. Additionally, private loans do not offer the opportunities for cancellation or loan forgiveness available under many federal loan options.[212]

206 Federal Trade Commission (US), "Consumer Information: Student Loans," Website.

207 Ibid.

208 ICHEFAP, "Government Student Loan Programs: An International Comparison 2009," op. cit.

209 Ibid.

210 Ibid.

211 Ibid.

212 Federal Trade Commission (US), "Consumer Information: Student Loans," op. cit.

Table 8: Student loan programmes in a wider selection of countries

Country	Student loan programme	Eligibility	Source of capital	Risk bearer	Means-tested	Interest rate	Student debt owed to government	Terms
Australia	Higher Education Loan Programme (started in 2005)	For eligible domestic students and most undergraduate students studying at university and enrolled in a Commonwealth-supported institute (Australia's version of an approved EFTS subsidised tertiary course)	Government	Government	No	No interest charges	AU$23 billion	Income-contingent repayments, minimum repayment rate of 4% when annual salary reaches AU$51,309 and 8% once annual salary reaches AU$95,288 or more
Canada	Canada Student Loans (CSL) Programme	For eligible Canadian citizens enrolled in an approved course at designated post-secondary institutes	Federal and provincial government loans	Federal and provincial government	No	Choice between fixed (prime + 5%) or floating (prime + 2.5%)	CA$15 billion in 2010	Borrowers agree to a repayment schedule provided by a loan provider. Interest charges on student loans are 100% subsidised by the federal government while a student is studying. There is a 6-month grace period post study where no repayments are required, but loans accumulate interest
Chile	University Credit Programme	Needs-based financial aid available for tuition in one of 25 traditional universities. Universities are responsible for collecting repayments	University credit solidarity funds	Government	Yes	2% during study and 5% post study	No data	Income-contingent repayments. Maximum repayment period is 15 years, after which any remaining balance is written off
	Credit to Finance Higher Education Studies	Available to needy students enrolled in accredited public and private institutions. Covers tuition.	Private financial institutions	Government guarantees up to 90% of the capital, plus interest through the Chilean Treasury and the higher education institution	Yes	Based on government's long-term borrowing rate		Not income-contingent. No interest charged on loan during study. Repayment begins 18 months post study, where it is separated into a series of 140 monthly instalments divided into three time periods. Maximum time period for repayment is 20 years
	Credito CORFO	Available to students from low-income families, who are enrolled in higher education institutions approved by the Ministry of Education. Financial aid available for tuition and a fraction of other related expenses	Commercial banks	Co-signatory	Yes	Interest rate set by banks		Not income-contingent. The bank from which a loan is obtained may determine which universities and majors they are willing to finance. Loans must be repaid within 15 years

Country	Student loan programme	Eligibility	Source of capital	Risk bearer	Means-tested	Interest rate	Student debt owed to government	Terms
China	General Commercial Student Loans Scheme (GCSL)	Available to students aged 18 and over enrolled in public and private sector educational institutes and their parents/ guardians (required for collateral). Loan covers tuition and living expenses	State-owned banks, commercial banks, credit-cooperative unions	Banks and co-signatories who provide collateral	Yes	Commercial interest rate	No data	Not income-contingent. As of 2009, interest was not subsidised by government and the repayment period was flexible
	Government Supported Student Loan (GSSL)	Available to poor students in approved higher education institutions. Loan covers tuition and living expenses	Banks	Banks	Yes	Less than 10%		Not income-contingent. The maximum repayment period is 6 years, and repayments are made on a monthly or quarterly basis. Interest rate set by People's Bank of China. Interest charges apply when loan is issued, but is fully subsidised by government while student is studying
	Student Resident Loan	Available to poor students in public and private higher education institutes. Covers tuition and living expenses	Commercial banks	Government and banks	Yes	Commercial interest rate		Not income-contingent. Interest rate set by People's Bank of China. Interest charges apply when loan is issued, but is fully subsidised by government while student is studying. The maximum repayment period is 14 years after loan is first issued. Maximum grace period is 2 years post-graduation
Japan	Dai-isshu loans provided by Japan Student Services Organisation (JASSO)	Available to academically competent students for education at public post-secondary (and some secondary) institutions. Covers tuition and maintenance expenses	Government	Co-signatory or a guarantee agency	Yes	No interest charges	No data	Not income-contingent. JASSO calculates repayment period according to loan value. Maximum repayment period of 20 years. Grace period of 6 months. Repayments are automatically deducted from the borrower's bank account on a monthly or semi-annual basis. Debt forgiven on occasion of borrower's death or bankruptcy. Interest penalties and other charges applied to overdue repayments
	Dai-nishu loans provided by Japan Student Services Organisation (JASSO)	Available to students enrolled in public post-secondary institutes. Covers tuition and maintenance expenses	Government	Co-signatory or a guarantee agency	Yes	Variable interest rate applied based on government borrowing rate		Not income-contingent. JASSO calculates repayment period according to loan value. Maximum repayment period of 20 years. Grace period of 6 months. Debt forgiven on occasion of borrower's death or bankruptcy

Country	Student loan programme	Eligibility	Source of capital	Risk bearer	Means-tested	Interest rate	Student debt owed to government	Terms
Mexico	The National Program for Financing Higher Education	Available to students in private universities	NAFIN, federal development bank	NAFIN and private universities (who cover 20%)	No	10%	No data	Relatively new programme, so little information available on repayment schedules
	Credito Educativo (Sonora State)	Available to private and public sector students in approved higher education institutes	Instituto de Credito, Sonora	Co-signatory	Yes	6%		Interest paid during study. Principal and interest paid following 6-month grace period post study. Repayment period stipulated in contract
	Credito Educativo (Tamaulipas State)	Available to private and public sector students	Instituto de Credito, Tamaulipas	Co-signatory	Yes	Not stipulated		Interest paid during study. Principal and interest paid following 6-month grace period post study. Repayment period stipulated in contract
	Credito Educativo (Guanajuanto State)	Available to university students who meet academic requirements	Educafin	Co-signatory	Yes	7%		While in study, borrower must pay off 10% of loan principal. Grace period of 6 to 12 months post study. Remaining 90% of loan must be repaid over a period equal to that during which student received loan
	El Credito Educativo SOFES	Available to private sector universities only. For needs and merit-based students	Federal government	Co-signatory; universities take over loan after 9 months of default	Yes	2% + inflation		Repayments made to universities. Interest only is paid during study. Repayment made in monthly instalments with repayment period twice the length of the loan period
New Zealand	Student Loan Scheme (administered by StudyLink)	For New Zealand citizens, or those who meet the residency requirements and are enrolled in a tertiary course, studying full-time or part-time. Available for tuition, living expenses and course-related costs	Government	Government	No	No interest charges	NZ$15 billion as of March 2016	Income-contingent repayments, where the minimum repayment rate is 12% of pre-tax income once annual salary reaches NZ$19,084. Interest charges are 100% subsidised by government for students while studying and for borrowers who reside in New Zealand
Sweden	The Swedish Board for Study Support (CSN)	Three types of financial aid available to Swedish citizens for higher education: student grants, supplementary allowance, and boarding supplements	Government	Government	Yes	Annual fixed interest rate determined by Swedish government	No data	Income-contingent repayments. Repayments made in the form of annuities and begin 6 months after final loan receipt. Maximum repayment period is 25 years

Country	Student loan programme	Eligibility	Source of capital	Risk bearer	Means-tested	Interest rate	Student debt owed to government	Terms
The United Kingdom	Student Loans Company (SLC)	Available to domestic and some EU students enrolled in university, college or other higher education institution offering approved courses. Financial aid available for tuition and living expenses	Government	Government	No	Interest charges while studying are applied at rate of Retail Price Inflation + 3%. Interest charges post study calculated based on a sliding income scale	Around £65 billion in 2014/15	Income-contingent repayments. Minimum repayment rate is 9% once annual salary reaches £21,000, paid in monthly instalments
The United States	Federal Perkins Loans	Available to needy undergraduate and graduate students	Split evenly between government and higher education institution	Split evenly between government and higher education institution	Yes	5%	US$1.2 trillion as of August 2013	Not income-contingent. Repayments made directly to the higher education institutions. Maximum repayment period is 10 years based on total amount owed
	Subsidized Stafford Loans	Available to needy students enrolled at least part-time in eligible post-secondary institutions	Federal Family Education Loan (FFEL), or the US Department of Education	Government	Yes	Adjusted annually, but may not exceed 8.25%		Income-contingent repayment plan available. Four different repayment plans available depending on the value of the loan and the plan chosen
	Unsubsidized Stafford Loans	Available to all students enrolled at least part-time in eligible post-secondary institutions	Federal Family Education Loan (FFEL), or the Federal Direct Loan (FDLP)	Government	No	Adjusted annually, but may not exceed 8.25%		Not income contingent. Interest charges accrue from when loan is first issued. Similar repayment options to a Subsidized Stafford Loan
	PLUS (Federal Parent Loan for Undergraduate Students)	Available to parents of undergraduate students	FFEL and FDLP	Government	No	8.02%		Similar repayment options as above, excluding the income-contingent option

Source: ICHEFAP, "Government Student Loan Programs: An International Comparison 2009," The International Comparative Higher Education Finance and Accessibility Project (Buffalo: State University of New York at Buffalo, 2009).

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