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**Article**

## Increasing Access to Higher Education Through Student Loans

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## INCREASING ACCESS TO HIGHER EDUCATION THROUGH STUDENT LOANS<sup>1</sup>

ADRIAN ZIDERMAN<sup>2</sup>

### Four aspects of ‘access’

While an accepted, generic definition of access is “a process of enabling entry into higher education” (Harvey 2004, 13), this paper approaches the issue of access more widely, from four differing perspectives. It then moves on to consider how the availability of government-sponsored student loans may impinge, positively, on access.

### *Broadening of access*

Firstly, let us consider the broadening of access. This aspect of access relates to policies facilitating the entry of larger numbers of potential students into higher education. Many countries around the world have long-term policies aimed at increasing the percentage of the relevant age cohort (say 18–24 years old) that enrolls in higher education. Underlying this trend is the recognition of the importance of a larger higher-educated population for economic and social development, particularly in the context of a more competitive, global environment. The focus is not so much on the socio-economic composition of the student population, but rather on the relative size of this enrollment. Some sixty years ago, the fear that a substantive expansion of the higher education system in the UK would lead to falling academic standards (“more means worse”) was countered by the view that there was a large “pool of untapped ability” that was not attached to tertiary learning at the time (Robbins Report: Committee on Higher Education 1963).

### *Deepening of access*

In contrast, we may define the deepening of access as “ensuring that significant proportions of students from non-traditional areas (such as working class, ethnic minorities) enter higher education (Harvey 2004, 13). Here the emphasis shifts from the need to increase the number of students in higher education, to that of changing their composition in order to achieve a more socially acceptable balance amongst the various socio-economic groups. This is achieved through reaching out to those, usually disadvantaged, groups who do not customarily pursue higher education studies. The central motivation here is clearly social, and aimed at improving the life-chances of these groups.

### *Retention and successful completion*

More widely, the “concept of ‘access’ is understood to encompass not only entry into higher education, but also retention and successful completion” (National Office of Equity of Access to Higher Education 2008). Dropout from learning is not only (or perhaps mainly) the result of academic weakness. Unforeseen financial difficulties may play a role in many cases, particularly when brought on by such factors as tuition fee increases or a downturn in the economy (with less student employment opportunities). In such circumstances, the availability of student loans (for tuition fees or for living expenses, as appropriate) may be important in mitigating potential student dropout.

### *Maintaining freshman enrollment levels*

Similarly, the advent of tuition fee increases or an economic slowdown may persuade many potential students to decide against enrolling in higher education. Student loans can offset these financial barriers.

### **Access and student loan schemes**

What role may the availability of student loans play in facilitating these forms of access? Government-sponsored student loan schemes around the world differ in the central objective pursued. Identifying the under-



<sup>1</sup> This paper draws heavily on the author’s previous writings, particularly Ziderman (2013).

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lying objective of a particular loan scheme is therefore important because this will have implications for many central aspects of the scheme. These include: whether loans are offered for tuition, living expenses or both; the appropriate level of loan subsidy (if any); the need for targeting (confining eligibility to particular student categories); loan allocation and rationing procedures where loan funding is limited. But the objective of a given scheme, and how this effects the operation of a scheme, will also have strong implications for the effect of the loans on access.

We may distinguish three types of loan schemes: cost sharing, social targeting and student independence.<sup>3</sup>

#### *Cost-sharing model*

We begin with an elaboration of the cost-sharing model. In many parts of the world, university systems are facing a financial crisis. Resources available to universities have been eroded due to a combination of a dramatic and continuing expansion of student enrollments unmatched by public expenditure on higher education. Universities have attempted to alleviate these financial pressures through the development and extension of non-government sources of funding. Cost-sharing, (or, greater cost-recovery), where a larger and significant share of the costs of university education is shifted onto the main beneficiaries of university education – students and their families – is the dominant path that is pursued for revenue augmentation. In particular, this has taken the form of the introduction of tuition fees or of raising them to realistic levels; in fewer cases, cost sharing takes the form of charging for hitherto highly subsidized dormitory and living costs.

Due to the fact that substantially higher tuition fees will cause hardship for enrolled students and are thought likely to impede university access, tuition hikes have been accompanied by the introduction of a state-sponsored student loan scheme in many countries. The disincentive effects of up-front tuition fee increases may also be offset by the availability of loans for students that will cover these augmented costs. Loans enable student-borrowers to avoid up-front payments for higher education (whether for tuition or living expenses) by delaying payment, which will be rendered in manageable installments out of enhanced earnings after graduation. State intervention is necessary because banks are loath to make commercial loans to students to finance tuition

costs, given the higher risk, lack of collateral and the nebulous nature of the human capital asset that the loan will generate.

The availability of student loans helps to make tuition fee increases more acceptable, both politically and socially. In Singapore, the 1988 university tuition fee rises were accompanied by subsidized loans equivalent to about half the value of the new tuition fees. The much-discussed Australian loan scheme was introduced in tandem with the imposition of university tuition fees in 1989. In the early 1980s, large tuition fee increases in Chile were accompanied by the introduction of student loans administered by the universities.

#### *Social targeting mode*

Student loan schemes may serve the more deliberate role of increasing the accessibility of the poor and of other marginal groups to higher education. When targeted specifically at such disadvantaged groups, loan schemes (particularly in cases where they are substantially subsidized), may lead to greater access of the poor to university education, thus contributing to social equity. In many countries the relatively low enrolment of poor and disadvantaged youth in tertiary education (and also in non-compulsory secondary education) is a cause of social concern. Increasing the access to university education among these segments of the population has become a major element in educational and social policy. While the cause of low access of the poor is multi-faceted (and a full discussion is beyond the scope of this paper), financial constraints evidently play a role. There is now a broad consensus on the need to offer clear financial incentives to poor, potential students, not only to overcome the burden of fee payment and living expenses, but also to offset both parental resistance to reductions in family income and the fear that the benefits of the educational process may not be sizeable. The provision of financial aid therefore may be regarded as a necessary, though not sufficient condition for achieving greater participation of the poor.

But what form should this financial assistance take? The traditional, and most effective, method of enhancing the educational access of the poor has been through the provision of means-tested grants to cover tuition fees (where schooling is not free) and, often, to cover living expenses as well. However, a widespread grants scheme is likely to be expensive. The use of loans, rather than grants, proactively targeted at the poor, offers a method that may both increase access for the poor and reduce, or

<sup>3</sup>See Ziderman (2002) for a fuller taxonomy of loan scheme objectives.

at least contain, public expenditure on student support over the longer term, as loan repayments build up. To be effective in increasing the higher education access of the poor, loans may need to be made available under “soft” lending conditions.

Subsidized loan policies can have a limited effect on raising access of the poor; but this role needs to be complemented by appropriate action far earlier on in the education process. Insufficient academic preparation and the lack of willingness of large numbers of the poor to enroll in higher education have their roots much further upstream in the education system.

### *Student independence model*

Even when tuition fees are minimal, students (both the more affluent and the disadvantaged) may face considerable financial burdens: potential earnings are foregone while studying, and living expenses may be sizeable, especially when the student does not attend a university near home. Financial pressures may have negative effects on a student’s academic performance (and thus compromise the process of human capital investment); the fear of such pressures will act negatively on decisions to enrol in tertiary education. These pressures can be mitigated by the broad availability of student loans for living expenses. While such burdens may fall relatively heavily on the poor, in principle loans for this purpose could be made broadly available, to more affluent as well as poorer (current and potential) students, as long as these loans are not unduly subsidized.

Eligibility, and the extent of loan support, is determined by parental income in many loan schemes. The concept of parental support is a central element in loan schemes in many European countries, including Austria, Germany, France, Italy, Portugal, Spain, and the UK. However, parents are not legally required to make the designated “parental contribution”. Thus many students, including those from non-poor backgrounds, may face financial difficulties during study, while potential students may not enroll if they feel that the parental contribution will not be forthcoming. A very different approach is taken in a number of countries, which base student support on the concept of student financial independence; student entitlement to loan support is based on student, not parental, income. Such arrangements exist in Denmark, Finland, Norway and Sweden; in these Nordic countries, where tuition is free, grants and loans are made for living expenses only.

Table 1 provides a matrix of selected national loan schemes, in which loan scheme coverage is mapped against loan scheme purpose (i.e., the three types of loan models, outlined above). The cost-sharing model is illustrated, principally, from experiences of how the Australian scheme and the new scheme in England work. Examples of the social targeting model are drawn from five UNESCO-supported Asian case studies.<sup>4</sup> The student independence model is illustrated mainly from a cluster of European countries where typically no tuition fees are charged and loans cover living expenses only.

<sup>4</sup> The regional study, a joint endeavor of UNESCO-Bangkok and the International Institute for Educational Planning in Paris, consisted of five in-depth studies on the functioning of student loan schemes in Asia: China, Hong Kong, the Republic of Korea, the Philippines, and Thailand. A synthesis study is provided in Ziderman (2004).

**Table 1**

#### **Type of access and loan scheme objective / coverage, country examples**

Loan scheme objective	Loan scheme coverage		
	Tuition fees only	Living expenses only	Tuition and living expenses
Cost-sharing	Australia		England, New Zealand
Student independence	Hong Kong (NLS) <sup>a)</sup> Korea (GECP) <sup>b)</sup>	Denmark, Finland, Hungary, Norway, Sweden	Canada
Social targeting	The Philippines	Hong Kong (LSFS) <sup>c)</sup> Korea (MOE) <sup>d)</sup>	China, South Africa Thailand <sup>e)</sup>

<sup>a)</sup> Hong Kong: non-subsidized scheme (NLS), <sup>b)</sup> Korea – Government Employees scheme, <sup>c)</sup> Hong Kong: subsidized scheme (LSFS), <sup>d)</sup> Korea – Ministry of Education scheme, <sup>e)</sup> Thailand – Student Loan Scheme (SLS)

Source: Ziderman (2013).

**Loan scheme objective and expectations**

A clear distinction may be drawn between the cost-sharing model and the other two models (Table 2). While loan schemes conforming to all three objectives will have implications for access, it is only the social targeting model that focuses predominantly on increasing access. Cost-sharing is concerned mainly with facilitating tuition fees increases and generating funding for the university sector; it has constituted the major rationale for the spread of student loan schemes in industrialized countries. The other two objectives are not concerned with augmenting university funding as such, but are wider in scope, with a clear social perspective. Loan schemes aimed at cost recovery would be restricted to universities in the public sector, while in meeting the other two objectives loans should, in principle, be available to students enrolled in public and private universities, on an equal basis. Most loan schemes are highly subsidized, mainly because they are offered at below market interest rates; however, in most cases, such subsidization cannot be justified (loan subsidization is dealt with subsequently). While the aim should be near full loan recovery, loan schemes targeted at the poor may constitute an acceptable exception.

In Table 3, type of access (as discussed in section *Four aspects of 'access'*) is mapped against loan scheme objective. Cost sharing and student independence loan scheme affect positively the broadening of access, while social targeting schemes may lead to the deepening of access. All three loan scheme categories affect student retention positively, while cost sharing loan scheme may

also help maintain new student enrolment levels when fees increase.

**Financial viability**

Almost all government-sponsored student loans schemes are highly subsidized by governments. This means that, unlike commercial loans, a sizeable proportion of the total loans outlay by the loans body, be it government department, loan scheme authority or commercial bank, will not be received back in repayment. A large and sustained gap between disbursements and recovery implies continuing governmental financial support for the scheme. Given pressures on government budgets, the continuation of these subsidies may not be assured, thus compromising the viability of these schemes over the longer term.

**Loan repayment and loan recovery**

But why (unlike commercial loans) do government-sponsored student loans schemes fail to recover the sums loaned out through the scheme? A number of factors militate against full recovery of loans.

Firstly, there are built-in subsidies, incorporated into the design of the loan scheme. While these lighten the burden of repayment falling on the individual student-borrower, they reduce repayment income accruing to the lending body. These “soft” loan conditions include zero or below-market interest rates on the loan, periods in which no interest is levied on outstanding debt (both

**Table 2**

Student loan schemes: objectives and expectations			
Expectations	Loan scheme objective		
	Cost-sharing model	Social targeting model	Student independence model
Loans will facilitate increased tuition fees	Yes	No	No
Loans will generate additional university funding	Yes	No	No
Loans are restricted to public universities	Yes	No	No
Loans are highly subsidized	No	Probably	No
Loans are confined to a target group	No	Yes	No

Source: Ziderman (2013).

Table 3

Loan scheme objective	Type of access and loan scheme objective			
	Type of access			
	Broadening access	Deepening access	Student retention	Maintaining freshmen enrollment levels
Cost-sharing	X		X	X
Student independence	X		X	
Social targeting		X	X	

Source: The author.

during study and in grace periods after study completion) and repayments not linked to the rate of inflation. The effect of these built-in subsidies is amplified where amortization periods are long. The *loan repayment ratio* indicates how much of the loan an average borrower is required to repay. It is measured by the ratio of total (discounted) required payments for each borrower, to total (discounted) loan sums received.<sup>5</sup>

Secondly, there are inefficiencies in running the scheme as a whole, in terms of substantial repayment default and high administration costs that are not passed on to the borrower. The repayment ratio relates to the typical borrower; it fails to show the full extent of recovery to the loan fund, from the overall perspective of the scheme as a whole. Even if student loans were not subsidized, and the individual student was required to repay in full, not all of the sums loaned would be recouped by the loan authorities.

Thus, overall loan recovery depends not only on the total of all individual cash repayments. It also takes account of administrative costs that are not passed on to the student borrowers and of the extent of non-repayment, including both default and 'loan forgiveness', for reasons like low graduate earnings that fall below a designated income threshold, disability, death, academic performance (South African, Norwegian and Dutch schemes) and the encouragement of graduates to enter skills-shortage occupations (Korean Ministry of Education Scheme for Engineering graduates) or to practice in underserved geographical areas (teachers and doctors in the US).

The *loan recovery ratio* is measured by the ratio of total (discounted) repayments to total (discounted) loan scheme outlays. Clearly, the recovery ratio is always

lower than the repayment ratio, because the latter takes no account of the probability of repayment default and does not include general administration costs.

#### ***Repayment and recovery ratios: international comparisons***

How large are these gaps in practice? A joint paper by the author probes this issue for 44 loan schemes in 39 countries (Shen and Ziderman 2009, updating Ziderman and Albrecht 1995). The analysis shows considerable variation in the size of the repayment and recovery ratios across schemes. Many loan schemes exhibit sizeable built-in subsidies accruing to student borrowers. The average repayment ratio is 61 percent (so that, on average, borrowers are required to repay only about 60 percent of the total loan received).

The distribution of repayment ratios across the 44 schemes is shown in Table 4. 13 schemes (about 30 percent of the sample) have relatively high repayment ratios, in excess of 80 percent. However, most schemes contain large built-in subsidies: the repayment ratio in 18 schemes (over 40 percent of the loan schemes examined) is less than 60 percent.

Overall loan recovery is considerably lower. No scheme has a loan recovery ratio exceeding 80 percent. Only five programs (above 20 percent of the sample) display recovery ratios higher than 60 percent, for the most part loan recovery is not high; 80 percent of the schemes display recovery ratios of 60 percent or less. In a third of the cases, loan recovery does not rise above 20 percent. Overall, the average recovery ratio is 39 percent.

Two noteworthy points emerge from the results reported in Table 4; both dispel prevalent myths about the financing of loan schemes. The first relates to the shortfall from full recovery in almost all government-sponsored

<sup>5</sup> Both measured in terms of present values.



Table 4

**Loan repayment and recovery ratios: international comparisons**

Ratio	Number of schemes	
	Repayment ratio	Recovery ratio (with default and administration costs)
Above 80 percent	13	0
61–80 percent	13	5
41–60 percent	8	11
21–40 percent	7	2
20 percent or less	3	8
Total number of schemes	44	26
Average repayment ratio: 61%, average recovery ratio, overall 39%		

Source: Shen and Ziderman (2009).

loans (and the very heavy losses in some). The implication of this is that government subsidization is to be seen as an enduring feature of these schemes; the widely-held view that loan schemes can act as a revolving fund which, once capitalized, will finance themselves through repayments of earlier loans, is not consonant with the facts in almost all cases. The second relates to the supposed dominant role played by repayment default and high administrative costs in accounting for low loan recovery. As shown in the bottom section of Table 4, the major factor, by far, accounting for recovery loss is the large, built-in, interest rate subsidy element in most schemes. Excluding default and administration charges, recovery from the amount that graduates are required to repay (i.e., the repayment ratio) is surprisingly low on average. The average repayment ratio is 61 percent, representing a hidden grant to the student and a loss to the scheme of some 40 percent. The addition of default and administration costs reduces recovery by only a further 20 percentage points (ten percent in each case). The following section looks at the issue of whether such large interest rate subsidies can be justified.

#### Can student loan subsidies be justified?

In loan schemes where either cost recovery or student independence constitutes the central objective, the case for heavy built-in student loan subsidies is not strong. For current students, the intended effect of student loans in both of these cases is to reduce the financial burden on students during study and to delay fee payment (through borrowing) until after graduation, when payment is more readily made from the expected enhance-

ment of earnings. For potential students, the availability of a loan programme will encourage access, under the concept of “study now, pay later”.<sup>6</sup> Since the aim should be near-full loan recovery in these two cases, the level of built-in subsidy is often excessive in practice.

It is only where loan schemes are aimed directly at social targeting that a clearer case for sizeable built-in subsidies can be made. However, such subsidies, as we have noted, will entail considerable budgetary costs. Since a grant offers a stronger and more direct incentive for access than a (partially) repayable loan, the apparent advantage of loans over grants is less clear-cut. This highlights a central conundrum in loan policy: at what level of in-built loan subsidy does a grant become a more cost-effective instrument for helping the poor than a subsidised loan (with hidden grants)? This suggests that, in country settings where state budgets are constrained, a more appropriate financial aid program to encourage access of the poor is likely to involve a combination of both loans and grants, with a relatively larger overt grant element for the very poor. This is common practice in the LFS Hong Kong scheme, in England and in many other loan schemes.

In the comparative study of loan schemes in South East Asia, most of the schemes studied were shown to conform to the social targeting model (Ziderman 2004). Yet the evidence did not indicate any high degree of success in increasing the university access of the poor. A number of essential conditions for success were lacking. These included a sufficiently high level of individual support to cover necessary expenses; a broad coverage of poor students to achieve national impact, and careful and deliberate loans targeting so that loans do indeed reach the poor and other disadvantaged groups, otherwise the central objective of the scheme is compromised. Loan schemes aimed at greater participation of the poor are often not effective because these ingredients for success are missing.

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<sup>6</sup>This is the name of the Philippines national loans scheme, a social-targeting scheme that is so limited in coverage that it has little effect in increasing access of the poor. Little attempt is made at collecting due loan repayments, so recovery is minimal; thus the scheme is often (and appropriately) dubbed the “Study Now, Repay Never” scheme.

The upshot of this discussion is that the levels of built-in subsidies, resulting in low repayment ratios, are often excessive. High subsidies may be either unnecessary (cost sharing and student independence models) or not very effective in practice in achieving objectives (social targeting). Since the level of built-in subsidy is fixed by government, these subsidies may be reduced, as appropriate, by government decision. However, vested interests may militate against these desirable changes.

### The repayment burden

Finally, we consider the concern that many student loans schemes saddle graduates with an inordinately heavy level of debt. In particular, it is argued that the fear of entering into student-loan debt acts as a disincentive for prospective students from lower socio-economic backgrounds to apply for university studies.<sup>7</sup> However, the approach adopted here is not concerned with the total size of the debt facing a student on graduation (nor with prospective students' perception of this debt), but rather with the extent to which repayment of the loan does, in practice, constitute a financial burden. The *repayment burden* falling on the borrower each year may be measured by the required annual loan repayment expressed as a percentage of annual income.

In the case of loan schemes where repayment is a fixed percentage of income (income-contingent repayment schemes), this percentage is defined by the conditions of the loan. In the case of the Hungarian loan scheme, this stands at six percent; in the South African scheme repayment varies from between three to eight percent depending on annual income, in New Zealand at ten percent and in the current scheme in England at nine percent. Since the repayment percentage out of income is built into income-contingent schemes, the repayment burden may, by design, be kept within acceptable limits and is the same for all borrowers. Furthermore, low income earners and the unemployed are protected by a minimum income threshold for repayment.

With mortgage-type loan schemes (where the periodic *sum* to be repaid is fixed), the situation is very different. While all borrowers repay the same annual amount, the repayment burden falls over time, as incomes increase. The size of the repayment burden will depend not only

on graduate annual incomes and loan size, but also on the size of loan subsidies and the length of the repayment horizon.

Chinese loans schemes do not carry high subsidies, resulting in heavy repayment burdens. Subsequent loan scheme reforms, notably through increasing the number of years over which loans must be repaid, have led to lower repayment burdens. In the early years of loan scheme operation, the short four-year repayment horizon resulted in a heavy repayment burden of 24 percent on average over each repayment year and high repayment default. The number of repayment periods was subsequently increased to six in 2004, together with a two-year grace period; currently the repayment horizon is ten years, resulting in a more acceptable repayment burden of 8.8 percent in the first year and falling steadily to 2.6 percent.

High levels of state subsidy in the Thai Student Loan scheme (SLS) – aimed at increasing access of the poor – imply a low repayment ratio of only 21 percent and moderate annual repayment obligations. Consequently, the repayment burden is very light: some 2.5 percent for males and, because of their lower earnings, around 3.5 percent for females. However, a recent paper (Chapman et al. 2010) argues that such average estimates are misleading because they do not show the considerably higher repayment burdens borne by low-earning graduates. The repayment burden for graduate borrowers falling in the lowest decile of earners is shown to be nine percent for males and 13.9 percent for females. This may not only enhance repayment default, but may also act as a disincentive for access of those potential students who are pessimistic about their future earnings. The policy response to these findings is to incorporate measures into mortgage-type loan design, to protect low earners from excessive repayment burdens; this may be achieved by the introduction of sufficiently high income repayment thresholds, as is common in income-contingent schemes.

### A concluding comment

Student loans can have a positive, yet limited, role in augmenting access, as defined in this paper; but the general case for heavy loan subsidisation is weak. When the central loan scheme objective is access deepening – reaching out to the poor and other disadvantaged groups – student loans (probably subsidised) can constitute an important element in the available policy toolbox for

<sup>7</sup> This is strongly argued by Callender and Jackson (2005) in the English context; but is not supported from studies in Australia (Andrews 1999) and the Netherlands (Vossensteyn 2005).



increasing access. However, loan schemes need to be well-designed to avoid an excessive repayment burden and default.

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