

Unrealistic optimism, shifting priorities and intangible debt

BY JUSTIN DRAEGER

The current student loan system is inherently challenging to student borrowers. With shifting priorities, students often find themselves distracted when they ought to be paying better attention to an accumulating debt. The intangibility of a student loan to many of them adds to the difficulty. Students also bring unrealistic expectations of their future earnings to the borrowing table.

There are ways that loan providers and colleges can work together to tackle these challenges.

Kennon Rothchild is chairman of the board for Northstar Education Finance, and he understands why students sometimes forget about their loans. Students are distracted throughout the entire process, he contends. They must shop for a college and select one. They may also have to leave home, transporting belongings and personal concerns a long distance. They must register for classes, buy books, make friends and establish themselves in a completely new environment. What time and attention remain for figuring out the student loan system?

When it's time for repayment, the distraction intensifies. They focus on the ceremony and related activities, finding their first job and where they will live next. Amid that hustle and bustle, is it surprising that student loans take a back seat?

When surveyed, many borrowers claim their loans are burdens that cramp their lifestyles. But Sandy Baum, senior policy analyst at the College Board, has found inconsistencies between what students say and what students actually do. Baum's research shows that student loan debt has not

stopped students or graduates from taking on other forms of borrowing — or diminished their lifestyles.

Such inconsistencies are evidence of shifting priorities. During college "students are most concerned about paying the tuition bill," says National Council of Higher Education Loan Programs president Brett Lief. After college, borrowers are getting on with their lives, which often results in additional debt regardless of their outstanding student loan debt.

Out of sight, bottom of mind

It's not helpful that students can forget about their loan debt — often for extended periods. Payments can be deferred until after graduation. "On top of not making payments while in school, students are given a grace period of six months in which to forget their loans," comments Todd Mosko, vice president at American Education Services.

Detaching students further, they are systematically removed from much of the loan process. "They never see the check or any funds, which go directly to the school," remarks Rothchild. Also, the multi-year promissory note (MPN) is a model of processing efficiency that does little to reinforce a student's debt awareness.

Then there is tangibility, or the lack of it. An auto loan borrower uses the car regularly. A home loan borrower lives in the asset each day. Rothchild, who has more than 40 years experience in the mortgage industry, claims that assets tie people directly to their debt. "Student loans on the other hand are quite indirect," he says. And when the student loan bills come due, the borrower is often paying for a past experience.

Unrealistic expectations

Most students with large debt accumulated in college believe that the money will begin pouring in soon after they graduate. In "Personality Factors, Money Attitudes, Financial Knowledge, and Credit-Card Debt in College Students," author Jill Norvilitis calls it "unrealistic optimism." She found that students with large amounts of debt consistently overestimate their future earnings and underestimate their debt. Regardless of where a college graduate's career is heading, it usually starts at the low end of the pay scale.

This is no small matter. The college promise includes rosy future earnings. "Consumer loans are based on a borrower's *current ability* to repay. Student loans are based on futures," says Lief.

Work within the framework

What do student loan practitioners suggest to improve things?

1. **Increase focus**—When students are distracted, help them focus. Mosko explains that at American Education Services, they don't wait for students to come to them for help. They go to the students. "We reach students through campus newspapers, radio and web sites like Monster, CareerBuilder, MySpace and Facebook to help them focus

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learners drop in and out with no perceived path to a degree or certificate.

The Lumina report also suggests that postsecondary providers can be more adult learner friendly by:

- Providing childcare services
- Improving online course delivery
- Providing coaching to keep students on a track to success, with awareness of the resources available to help them get there

“The statistics on who is completing and not completing continuing ed are sobering, to say the least,” says Katie Bailey, assistant vice president of the Education Finance Council.

This group of students is a profitable one for colleges to seek. The marketing costs are far less expensive than the traditional student. Perhaps investing in this large group of diverse students makes sense for everyone. ■

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on their debts. Mosko says that if an AES staffer can talk to a borrower who is having trouble making payments, that borrower’s issues are fixed 86 percent of the time.

1. **Help them see reality**—The more financial knowledge a person consumes, the more realistic will be his or her view of the financial future. “We have career centers to help students find jobs; we have health centers to help students that are sick; but we lack a financial counseling office to help students increase their financial literacy,” says Norvilitis. She believes that such an office should be staffed by professional financial counselors, and it should be separate from the financial aid office. Lief contends that such financial education should start in secondary school. By the time

a student gets to college and the tuition bill, it may be too late.

2. **Increase collaboration**—Given the current loan system, Rothchild admits the college bears a lot of the cost and responsibility of informing students about their loan debts. But he suggests that lenders too are concerned about successful student loan repayment. “Even in FFEL loans, where there is almost no risk, a lender will have a greater return on investment if the student repays the loan,” Rothchild observes. Lief says that loan providers have a moral and ethical responsibility to work with schools to provide students as much information as possible to help them make good financial decisions. Both Rothchild and Lief express concern about the political climate that is unintentionally destroying collaborative efforts between loan providers and schools. ■



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