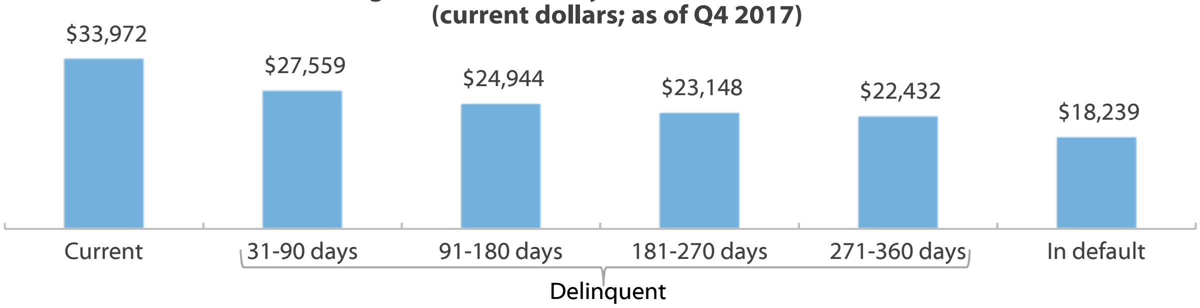
Students Who Borrow More Are Less Likely to Default

Concerns over student debt tend to focus on two trends: high default rates and high loan balances. Default rates have been slowly declining in recent years, but far too many student loan borrowers continue to default. Nationally, about one in nine student loan borrowers who entered repayment in fiscal year 2014 defaulted in that year or the next two (a three-year cohort default rate [CDR] of 11.5 percent), but lifetime default rates are much higher. The federal Office of Management and Budget predicts that 20 to 25 percent of undergraduate Direct Loan borrowers who entered repayment in FY 2016 will default over the next 20 years, and a recent study of students who began postsecondary education in 2003-04 found that 27 percent of borrowers had defaulted within 12 years.

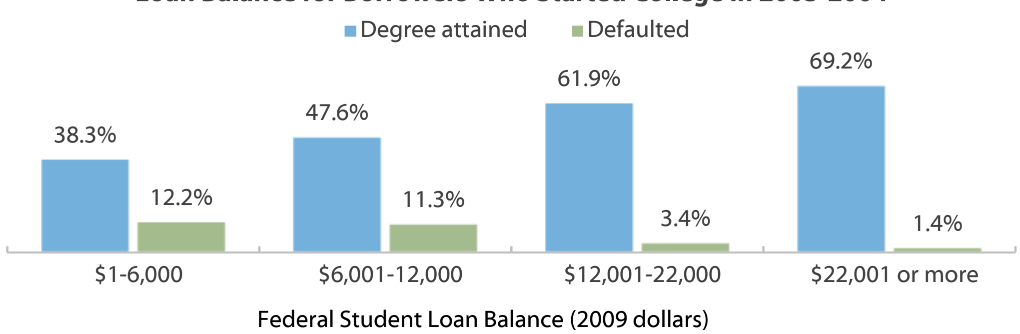
Although the average loan balance continues to climb, the relationship between this trend and default rates is not straightforward. In fact, borrowers who are current on their loans tend to have higher balances, while those in delinquency or default tend to have lower balances.

National Average Loan Balance by Loan Status for Federal Direct Loans (current dollars; as of Q4 2017)



As shown in the chart above, the most severely delinquent and defaulted loans tend to have smaller balances than loans that stay current. This counterintuitive pattern has one key cause: Borrowers incur higher debts by staying in school longer.

Degree Attainment and Default as of 2009 by 2009 Federal Student Loan Balance for Borrowers Who Started College in 2003-2004



The common explanation for the inverse relationship between borrowing and default is that persisting to graduation requires more borrowing but also leads to higher incomes, such that the loan payments are actually more affordable. Data support this explanation, but it is incomplete. Provisions like deferments and income-driven repayment plans offer borrowers effective means to avoid defaulting on federal student loans regardless of income. Helping borrowers acquire the knowledge and skills to navigate the repayment process early on can be an effective default prevention strategy for all borrowers, especially those more likely to drop out and be at greatest risk of default.

Sources: Cohort default rate: U.S. Dept of Education, "Official Cohort Default Rates for Schools", (http://www2.ed.gov/offices/OSFAP/defaultmanagement/cdr.html); Lifetime default projection: U.S. Office of Management and Budget, FY 2017 Budget for Dept of Education, (https://www.whitehouse.gov/sites/default/files/omb/budget/fy2017/assets/edu.pdf); 12-year default study: Woo, J. *et* al (2017). Repayment of Student Loans as of 2015 Among 1995-96 and 2003-04 First-Time Beginning Students. NCES. (https://nces.ed.gov/pubs2018/2018410.pdf); Attainment and default: Author's analysis of U.S. Dept of Education, National Center for Education Statistics, 2003-04 Beginning Postsecondary Students Longitudinal Study (BPS:04/09).