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Higher Education - US

Student Loan Burdens Present Modest Credit Risk for Moody's-Rated Universities

Student debt burdens contribute to the heightened scrutiny of higher education costs for US public and private universities that we rate.[1] This scrutiny and a continued focus on affordability constrain universities' ability to grow student charges, which represent 75% of median revenue for private colleges and 49% for public universities. However, the actual student loan burden for students that attend colleges and universities that we rate is moderate and will continue to stabilize as colleges supplement education costs with financial aid and tuition discounting. Student loan default rates are low and declining due to improved employment prospects and expanded repayment options.

» **Default and delinquency rates for colleges and universities that we rate are typically lower than national averages.** Low default and delinquency rates reflect relatively high completion and job placement rates as well as the availability of financial aid to reduce debt per student. Institutions with low graduation or degree completion rates, particularly for-profit colleges and some community colleges, face the highest credit risk related to high default rates.

» **Student loans are not deterring demand at Moody's-rated universities given the typically strong return on investment for education.** The majority of public and private institutions that we rate continue to have stable enrollment, sufficient brand recognition and financial resources to support continued student demand. The earnings disparity between college and high school graduates is widening, underscoring the value of a higher education degree over the course of a student's lifetime.

» **Growth in public university student debt burden will slow with stabilized state operating support and limited tuition increases.** Public university students increased student loan borrowing post-recession because many states cut operating appropriations and public universities responded with substantial tuition increases. Both of these trends have reversed in recent years, and the result is a slight decline in average debt per student for Moody's-rated public universities.

» **The average level of debt per student for students at Moody's-rated private universities is declining because these universities are absorbing more of the cost of education through tuition discounting.** We expect growth of average student debt burden for private universities to level. Net tuition revenue growth for private universities has slowed dramatically in recent years as universities continue to hold tuition rate increases low and are simultaneously increasing financial aid packages to families.

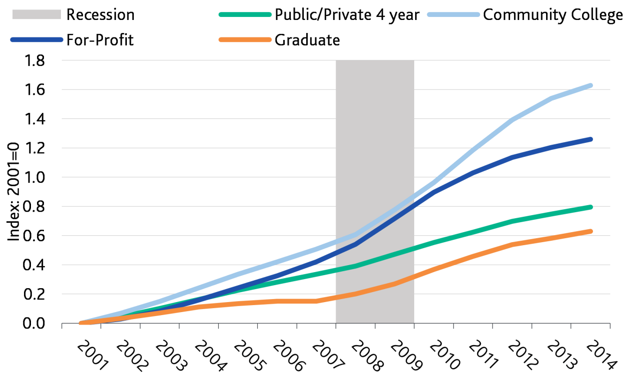
Post-recession student loan growth is in large part due to increased higher education participation

After the 2008 recession, enrollment in community colleges, for-profit institutions and graduate programs rose in tandem with unemployment rates, causing a surge in the number of student borrowers and total student debt burden (see Exhibits 1 and 2). In contrast, enrollment at public and private colleges and universities that we rate remained relatively stable (Exhibit 4). The number of borrowers for undergraduate (public/private four-year) and graduate programs also expanded post recession, but at a more moderate pace. With declining enrollments at for-profit institutions and community colleges in the last few years, we expect slower growth of the national student loan burden.

Exhibit 1

Growth Rate of Community College and For-Profit Borrowers Will Slow with Declining Enrollment After Recent Peak

Growth rate of federal student loan borrowers by degree type

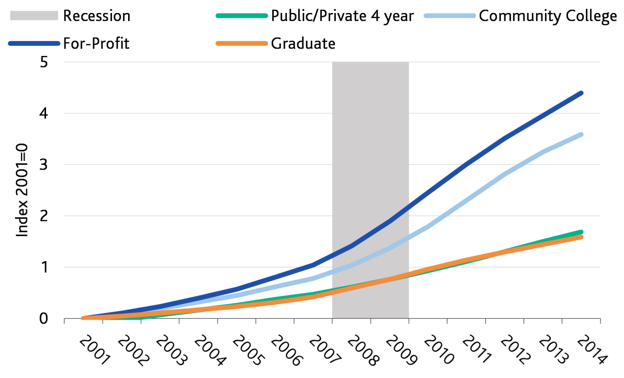


Public/Private four-year represents undergraduate borrowers in four-year programs. Total number of borrowers for all federal student loans: subsidized, unsubsidized, and Graduate PLUS and Parent PLUS loans (loan recipients include both students and parents).
Source: US Department of Education National Student Loan Data System

Exhibit 2

Number of For-Profit and Community College Loans Rose Steeply After Recession

Growth rate of federal student loans outstanding by degree type



Public/Private four-year represents undergraduate borrowers in four-year programs. Total number of borrowers for all federal student loans: subsidized, unsubsidized, Graduate PLUS and Parent PLUS loans (loan recipients include both students and parents). Measures growth rate of aggregate dollar amount outstanding.
Source: US Department of Education National Student Loan Data System

From 2000 to 2014, the number of for-profit and community college borrowers grew by 1.2 and 1.6 times, respectively. Concurrently, those two sectors had the largest growth rates for median federal debt per student, at 90% and 64%, compared to just 41% across all sectors. As seen in Exhibit 2, growth in these two sectors' share of aggregate federal student loans outstanding far outpaced that of traditional graduate and public and private four-year undergradate programs. That growth is a major driver of the rapid total debt burden growth since the recession. We expect the pace to slow dramatically going forward with continued enrollment declines in both subsectors. Enrollment for graduate students, who carry the highest median student loan burden at almost $46,000 per student, also grew substantially post-recession and is now stabilizing.

Default and delinquency rates for colleges and universities that we rate are typically lower than national averages.

Although media attention on student loan defaults contributes to a greater focus on higher education's affordability and value proposition, the direct credit risk for Moody's-rated institutions is low. Default rates for colleges and universities that we rate tend to be much lower than national averages, reflecting relatively high completion and job placement rates combined with greater availability of financial aid to reduce debt per student. Many colleges and universities have also implemented stronger counseling around loan repayment over the last several years. Credit risk related to high default rates is highest for institutions with low graduation or degree completion rates, particularly for-profit colleges and some community colleges.

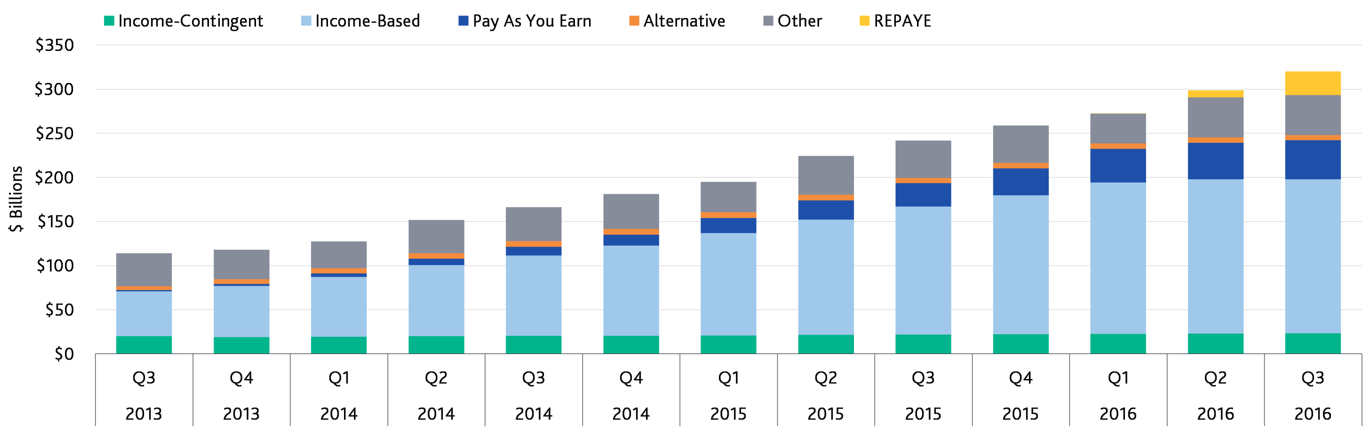
Of the US Department of Education's cohort default rate list, only 10 institutions were in jeopardy of losing their federal student aid status.[2] We do not rate any of them – nine for-profit colleges and one very small, local not-for-profit private college.

Delinquency and default rates continue to decline with improved federal repayment options and sustained macroeconomic improvement over the last several years. Strong US employment will contribute to continued improvement in these rates. Recent rapid declines in four-year for-profit enrollments will also contribute to declining default rates because students at for-profit institutions have traditionally had the highest default and delinquency rates. Enrollment at four-year for-profit institutions has declined a substantial 43% from spring 2013 to spring 2016, according to the National Student Clearinghouse, compared to 3% overall enrollment growth for four-year public universities and 5% growth for private universities over that period.

Growing participation in income-based repayment programs will continue to lower default rates in the future as borrowers are presented with more affordable repayment plans to meet their economic circumstances (see Exhibit 3). Increased use of these federal repayment plans helps to limit the potential future financial burden of student loan debt and will contribute to overall stabilization of average debt per student.

Exhibit 3

Federal Income-Based Repayment Plans Continue to Grow

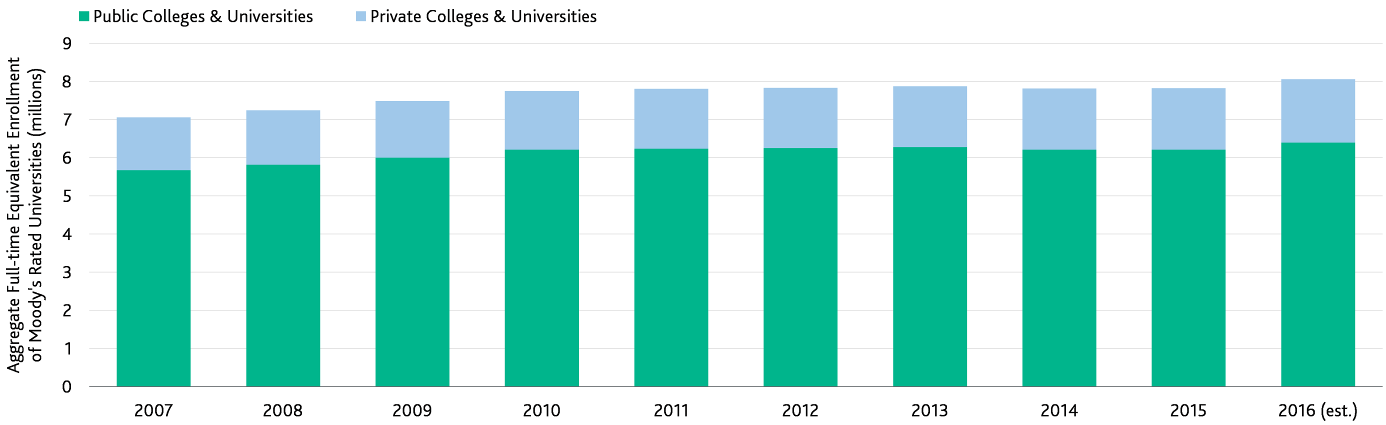


Sources: National Student Loan Data System (NSLDS), Moody's Investors Service

Student loans are not deterring demand at Moody's-rated universities given strong return on investment for education

The high return on investment for higher education over a student's lifetime fuels stable enrollment for public and private universities that we rate (Exhibit 4). The majority of these institutions have strong brand recognition, and above average graduation and retention rates that substantiate the perceived value of their education. We expect stable demand to continue.

Exhibit 4
Moody's-rated Public and Private Universities Maintain Relatively Stable Enrollment



Enrollment numbers are for fall of the calendar year.
Sources: Moody's Investors Service, Moody's Estimate

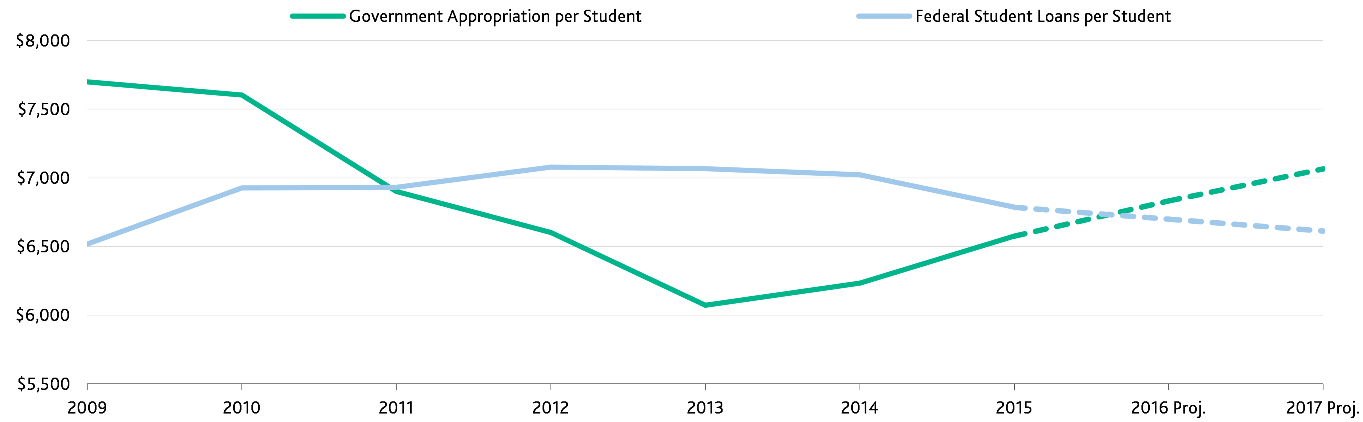
While the growing student debt burden has resulted in heightened public scrutiny of the value of a higher education degree, there is substantial evidence that income and employment rates are strongly correlated to degree attainment. In 2016, college graduates earned approximately 40% more than high school graduates after about five years in the work force; an even greater disparity exists between those with high school and professional degrees.[3] Students who have completed degrees are also more likely to remain employed, with just a 2.8% unemployment rate for Bachelor Degree holders, compared to a 5.4% for high school graduates in February 2016. [4]

Growth in public university student debt burden will slow with stabilized state operating support and limited tuition increases

State appropriation changes directly affect public university student debt burden. The student loan burden rose for public universities that raised tuition to offset state funding cuts during the recession (see Exhibit 5). Median state operating support per student declined by 23% from fiscal 2008 to 2013, and public universities correspondingly increased tuition, driving a record 40% growth of net tuition per student over that period. This rapid price increase caused more borrowing among public university students. However, the student loan burden will moderate in the near-term future with resumed slow growth of state funding and lower tuition rate increases at public universities. Experiences will differ by state, and dramatic reductions in state operating support would change the trajectory of student loan burden for public university students in affected states.

Exhibit 5

Student Loan Burden for Students Attending Moody's-rated Public Universities Will Moderate



Calculated average of undergraduate federal student loans per student for Moody's-rated public colleges and universities. Federal student loans are classified as any monies that must be repaid to the lending institution for which the student is the designated borrower. Includes all Title IV subsidized and unsubsidized loans. Does not include PLUS and other loans made directly to parents.

Sources: IPEDS Data Center, Moody's Investors Service

Public university net tuition per student growth has slowed considerably since 2014 and we expect that trend to continue through FYs 2016 and 2017 as public universities and state legislatures remain focused on access and affordability. With only 2-3% median net tuition per student growth expected for FY 2016, and 2% projected for FY 2017, the rate of public university student loan borrowing will continue to subside.

Public university students still have slightly lower per-student debt burden than private students due to lower cost per student, but the gap is narrowing due to the longer-term state disinvestment of public higher education. A student graduating with a four-year degree from a Moody's-rated public university in May 2014 would have an average student debt burden of $27,056 compared to $27,806 from a Moody's-rated private university, according to the latest National Student Loan Data Survey.

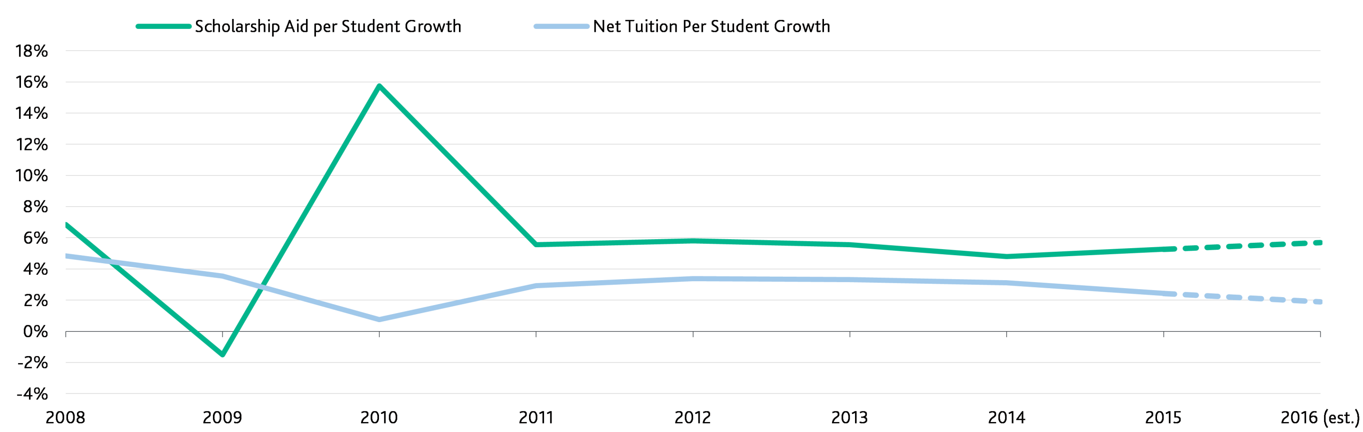
Average level of debt per student for students at Moody's-rated private universities is declining

For private universities, the affordability burden has shifted primarily to universities as families have remained highly price sensitive since the recession, creating continued pressure on smaller universities with limited financial resources. Growth in net tuition per student has hovered at little more than inflationary rates for the last several years. We project net tuition per student to grow 2-3% in fiscal years 2016 and 2017 (see Exhibit 6).

Exhibit 6

Private Universities Are Holding Costs Down Through Financial Aid

Scholarship aid growth outpaces net tuition per student growth



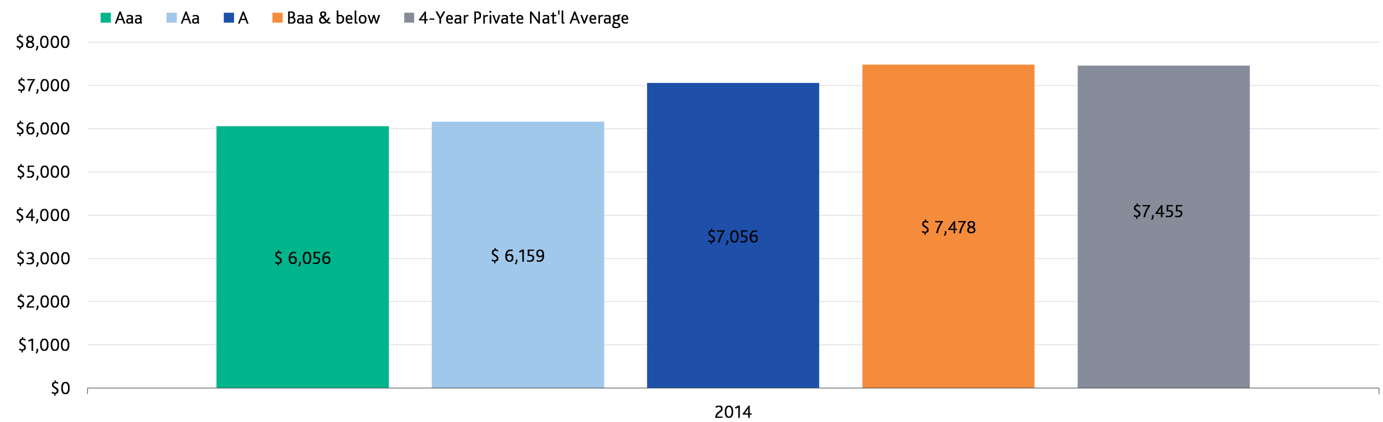
Source: Moody's Investors Service, Moody's Estimate

Rather than pass tuition increases on to families, many private universities continue to increase their tuition discounting, with median first-year discounting nearing 50% and continuing to rise annually. As a result, scholarship aid per student continues to grow at a faster pace than net tuition per student. We expect this weak net tuition revenue growth for universities to translate to low growth of debt burden per student for Moody's-rated private universities overall, but with students attending smaller private universities with weaker credit quality experiencing more rapid growth of average debt burden (Exhibit 7).

Exhibit 7

Students at Wealthy Private Universities Carry Lower Average Debt Burden

Average annual federal loans per student by rating category, FY 2014



Sources: IPEDS Data Center, Moody's Investors Service

A college's overall wealth and the amount of its endowment dedicated to financial aid are key factors driving the average student debt burden at private colleges. Moody's-rated private universities, particularly those rated in the Aaa and Aa categories, have lower debt per student than the national average because they have greater financial resources to support financial aid for lower income students. Many highly selective, elite private universities are committed to need-blind admissions programs with a financial aid packages that have dedicated scholarships to meet the full need of their students. A number have "no loan" or limited loan policies for students.

The student loan burden at less wealthy universities that we rate is in line with the national average. However, their financial aid programs are typically not funded by gifts and endowments but rather from true discounts on tuition, resulting in a heavier budgetary burden. These factors contribute to lower student debt burden among wealthy universities, whereas universities that are discounting tuition typically do not have sufficient resources to meet the full financial needs of its students, nor to support a "no loan" policy. Therefore, although the cost of attendance is not rising substantially, students with financial need must take out more federal student loans to attend and have higher student debt burdens than students attending wealthier institutions.

Moody's Related Research

- » Universities Face Another Year of Low Net Tuition Revenue Growth, Survey Shows, November 2016
- » US Private Universities Maintain Stability but Pockets of Stress Remain, July 2016
- » US Public Universities Largely Stable but with Considerable Sector Variability, July 2016
- » AMC Universities Maintain Stability Through Strong Brands, Large Size and Diverse Operations, July 2016
- » State Budgets Offer Mixed Results for Public Universities, July 2016
- » Higher Education - US: 2016 Outlook - Moderate Revenue Growth Supports Sector Stability, December 2015

To access any of these reports, click on the entry above. Note that these references are current as of the date of publication of this report and that more recent reports may be available. All research may not be available to all clients.

Endnotes

1 Throughout this report, Moody's-rated universities refers to the 225 public and 262 private not-for-profit universities we rate in the United States as of December 1, 2016.

2 Federal Student Aid, US Department of Education. Cohort list as of September 28, 2016

3 Bureau of Labor Statistics

4 Bureau of Labor Statistics, Labor Force Statistics from the Current Population Survey

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