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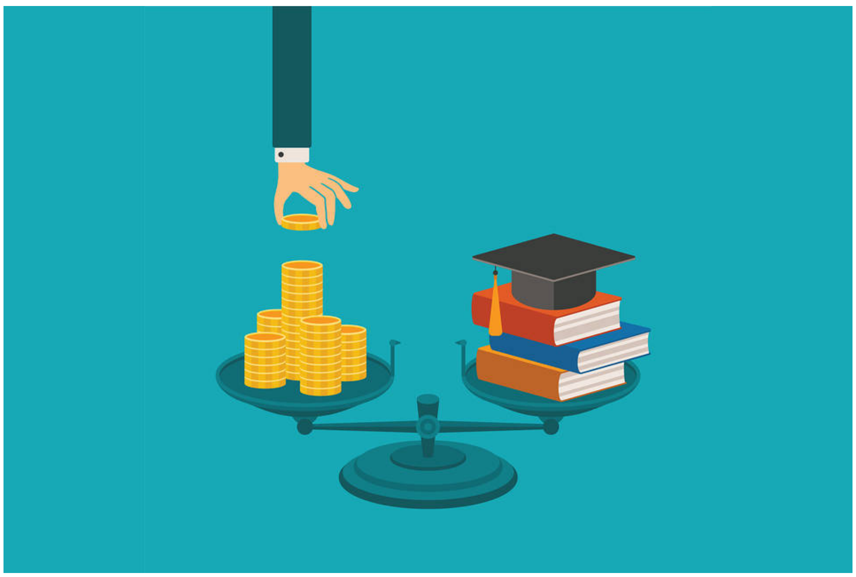
OPINION | COMMENTARY

Bigger Loans for STEM Students

Science majors are more likely to find jobs and repay debt.



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By **S.P. KOTHARI** and **KOROK RAY**
Aug. 14, 2016 5:41 p.m. ET

Outstanding student debt has ballooned to $1.3 trillion and is now, aside from mortgages, most American households' largest liability, according to the Federal Reserve. Last year alone student debt increased by almost $83.2 billion, or 6.7%. The price of tuition has risen an average 3.4% each year for a decade, markedly outpacing inflation.

Meanwhile, the U.S. faces a daunting skills gap in science, technology, engineering and math. Each year there are 1.3 million new openings in STEM fields but fewer than 600,000 new graduates. Is there a way to solve both these problems at once?

Yes: Restructure the Federal Direct Loan Program to target loans based on field of study. Students' interests would be better served and taxpayers' dollars would be more productively invested if the Education Department were to extend loans depending on the employability and long-term economic productivity of different fields of study.

Since 2010, when the Obama administration's Direct Loan Program was launched, all federal student loans have run through the Education Department. At the end of last year they totaled $840.7 billion of debt to 29.9 million students. In 2015 the default rate on direct loans was on average 2.1% per quarter or 8.4% for the entire year.

When the government is in the business of offering credit, as it is now with student loans, it should think hard about credit risk. One of the chief lessons of the 2008 financial crisis was that mispricing credit risk can have catastrophic consequences.

Yet the government's Direct Loan Program mostly ignores the credit risk of students, treating them largely as identical in their long-term employment outcomes. Just as a mortgage provider now requires higher down payments from risky borrowers with lower FICO scores, federal lenders should tailor the loan amount based on the long-term economic opportunities of the borrower.

Our proposal is to target the loan amount for each student based on field of study. First, we restrict attention to the loan amount rather than the interest rate since a partial loan (rather than higher rate) is better at ensuring that students have "skin in the game."

Second, the field of study category need not be determined by government alone but can rely on market data. The Boston-based company Burning Glass Technologies collects data on earnings and collegiate educational choices to quantify the value of different majors in college. Relying on such an index would allow government officials to peg the loan size to market data rather than by government fiat alone.

Some may feel that it is unfair to offer a greater subsidy to a computer science major than a history major. But treating these majors as financially equivalent imposes undue risk on the ultimate creditors behind student loans: taxpayers.

If the nation is serious about staying competitive in the global race for STEM talent, then targeting student loans is one solution that can and should earn bipartisan support.

Mr. Kothari is a professor of accounting and finance at the MIT Sloan School of Management. Mr. Ray is an associate professor of accounting at the Texas A&M University Mays School of Business and served as a senior economist on the Council of Economic Advisers from 2007-08.

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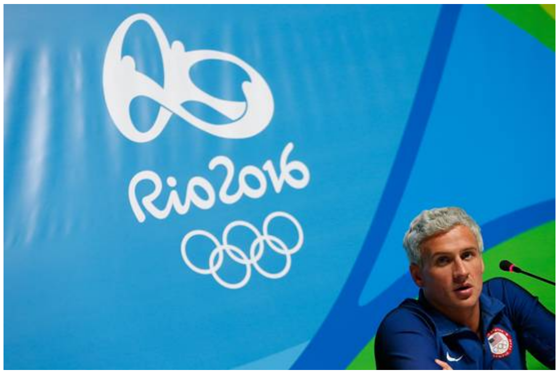

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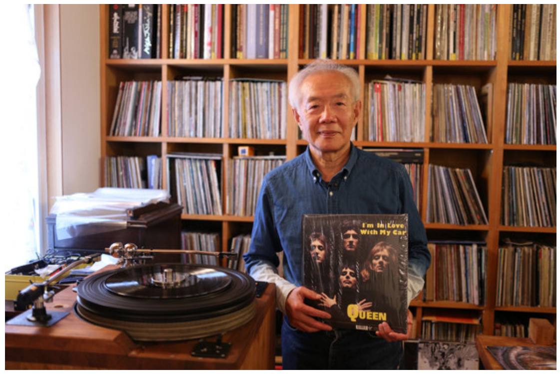

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