

A modest proposal for indentured servitude

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Where is Jonathan Swift when we really need him? Last week's *New York Times* opinion piece "The College Graduate as Collateral" really needs a rejoinder like Swift's "A Modest Proposal for Preventing the Children of Poor People from Being a Burthen to their Parents, or the Country, and for Making them Beneficial to the Publick."

The column by Luigi Zingales makes the case that the skyrocketing student loan debt problem threatens taxpayers and the credit markets—and even the "disadvantaged" themselves. The problem, he argues, arises from the lower classes of college students, those who attend but who actually can't afford to pay the bill.

Zingales, of the University of Chicago Booth School, is a rising star in free market economics and is keenly aware of Wall Street's growing fears about the "student loan bubble." No doubt, he also has his eye on the Quebec student fees protests and the general growth of social discontent throughout the US.

He expresses regret that needy students "cannot easily pledge their future income" and suggests that rather than incurring debt, they seek out the equivalent of "venture capitalists" to "invest" in their education. He explains, "In exchange for their capital, the investors would receive a fraction of a student's future income—or, even better, a fraction of the increase in the student's income that derives from college attendance."

This pledge, he envisions, would be piggybacked onto the tax system so that in years to come the Internal Revenue Service could collect the student loan "tax" directly on behalf of the banking industry. The state, with its full powers, would thus assume responsibility for student loan collection. In the US, late payment of taxes can be penalized up to 25 percent of the principal, with tax evasion a criminal offense punishable with prison. As a bonus, Zingales notes, this government

collection would be "at no cost to taxpayers"!

Trying to parry the obvious conclusions, the economist claims, "This is not a modern form of indentured servitude."

Well, there is actually truth to this statement. Indentured servitude promised a steady job and a debt-free status in three to seven years. By contrast, Obama's most recent student loan "reforms" provide some qualifying student loan debtors loan forgiveness after 20 years. Meanwhile, a large proportion of today's college grads are looking at a lifetime of peonage to the banks and/or federal government.

Depicting his scheme as a "voluntary form of taxation," Zingales states that it would "make only the beneficiaries of a college education—not all taxpayers—pay for the costs of it." His concern is that taxpayers might be picking up the tab for tuition costs for the undeserving, and according to recent media campaigns there really are *too many* college-educated young people.

This proposal, it turns out, is lifted entirely from arch-reactionary Milton Friedman [1], the architect of the concept of school vouchers, the proponent of the "denationalization" of education, and the advisor to the brutal Chilean dictatorship of August Pinochet. Friedman and his Chicago School played a central role in the policies of the Reagan and Thatcher government.

Recognizing the depth of the current economic crisis, Zingales has decided to resurrect Friedman's "equity contract" for university education. Perhaps leery of Friedman's notorious legacy, Zingales fails to acknowledge the true author. But entirely in his mentor's vein, Zingales explicitly opposes the concept of higher education for everyone, and foresees that selected "bright" students (though needy) can be picked up by venture capitalists, invested in and harnessed to lifetime payments.

Zingales is reacting to the growing nervousness of his

hedge fund and banking brethren about the financial implications of defaults on student loans. With a student loan securities industry literally betting on timely loan repayments, the dire statistics of nearly 50 percent unemployment among college graduates and parallel default rates are deeply troubling to these layers. They have a lot to worry about, as a brief survey of recent news for student loan securities shows.

*Hedge fund manager Daniel Ades recently told the *Wall Street Journal* that while he has consistently delivered strong returns on student loan debt trades over the past four years, he is not entering the market for the loans of recent graduates. “We can’t quantify the risk,” he stated.

*Chris Haid, a Barclays Capital director in asset-backed trading, expects a default rate at least 30 percent to 40 percent bundled into their bonds.

*Moody’s Investor Services last month downgraded 20 student loan revenue bonds, \$568 million in asset-based securities in Mississippi, and 24 classes of student loan revenue bonds issued by Michigan Finance Authority, previously known as Michigan Higher Education Student Loan Authority.

*In the arcane language of debt traders, McGraw Hill researchers noted that “a large number of US private-label student loan ABS ratings are currently on CreditWatch negative, reflecting the elevated level of the US unemployment rate.”

So who is Luigi Zingales and should we take his proposal seriously?

Zingales is not a fringe economist, but a faculty fellow at the prestigious University of Chicago Booth School of Business, a faculty research fellow for the National Bureau of Economic Research, a research fellow for the Center for Economic Policy Research, and a fellow of the European Governance Institute. His body of work includes “Saving Capitalism from the Capitalists” and “A Capitalism for the People: Recapturing the Lost Genius of American Prosperity,” works devoted to developing strategies for saving capitalism from growing popular anger.

His theories for saving “true capitalism” were most recently demonstrated in spades at General Motors. His analysis elaborated in 2008, “A Bankruptcy to Save GM,” was put into practice by the Obama administration. The auto giant, under the supervision of the federal government, used the bankruptcy courts as

an opportunity to shed tens of thousands of jobs, sharply cut health care and pensions, and cut in half the pay for new workers. This was used as the benchmark for an assault on the entire working class.

In his “modest” proposals for financing higher education, Zingales is only expressing, in a particularly crude form, the ongoing efforts by the American ruling class, now led by the Obama administration, to undermine and ultimately destroy the very concept of public education. The effect of such proposals as Zingales’s is to return higher education back to the days when it was the property of the wealthy elite.

Footnote:

[1] See: Friedman, Milton. “The Role of Government in Education” 1955.

The author recommends:

US Student Loan Debt: Where did it come from and who benefits?

[29 May 2012]

Milton Friedman 1912-2006: “Free market” architect of social reaction

[21 November 2006]



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