US student loan interest rate doubles

Zac Corrigan
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The interest rate on subsidized Stafford loans doubled on Monday, rising from 3.4 percent to 6.8 percent. Stafford loans are federal loans available to US college students who can't pay out of pocket for higher education.

Under the present system, Congress sets the interest rate on these loans annually. Last summer, during the presidential campaign, Democrats and Republicans agreed to keep the 3.4 percent rate in place for one year. Secretary of Education Arne Duncan called this an "election-year fluke." Congress then set rates to double automatically for 2013 unless they intervened before the deadline, which didn't happen.

Subsidized Stafford loans, which account for one third of government aid to college students, do not begin to accrue interest until the borrower leaves school. They are aimed at students most in need of financial assistance. If rates remain at 6.8 percent, it is estimated that a typical borrower will pay $1,000 more over the duration of his or her loans.

With more than 7 million students projected to take out subsidized Stafford loans for the upcoming school year, this would immediately result in an extra $7 billion paid out by the neediest student borrowers.

Congress can still intervene to retroactively change the rate before the beginning of the school year when it returns to session on July 10, after its Independence Day recess. The media has characterized their inaction thus far as an inability to compromise and overcome "congressional gridlock," but in reality both parties are moving to say goodbye to the current rate.

Various plans have already been floated by both Democrats and Republicans to switch federal student loan interest from a fixed rate to a variable rate. These plans would tie the interest rate on subsidized Stafford loans to the interest rate on 10-year treasury bonds plus about 3 percent. This would destabilize student borrowers by putting them at the mercy of the market. The amount they must eventually pay could vary significantly from one year to the next.

Any increase in interest rates on student loans will add to the already devastating burden imposed on working class and middle class people, predominantly youth, seeking higher education. Student loan default rates are already on the rise, exceeding 13 percent of student borrowers nationwide. 30 percent of borrowers are "delinquent," having missed payments for at least 90 days.

US college students are in ever-increasing need of financial assistance. Since the financial collapse of 2008, state governments have cut funding to public universities by 28 percent, and tuition has risen 27 percent nationwide. Over the same period, median household income has dropped 8 percent.

Average student loan debt among 25-year-olds in the US now exceeds $20,000—more than double what it was a decade ago. 43 percent of 25-year-olds have student debt, up from just 25 percent over the same period. Total US student loan debt now exceeds the $1 trillion mark and is rising, according to the Consumer Financial Protection Bureau (CFPB), making it the largest non-mortgage debt source, more than auto loans or credit card debt.

A recent Federal Reserve Bank of New York (FRBNY) report showed that since the onset of the slump in 2009, 25-year-olds burdened by student debt are increasingly unlikely to own their own homes or purchase vehicles, and have worse credit scores than those without student debt. These figures all represent a dramatic reversal of historical trends. Before the crisis those borrowing money to pay for higher education were instead better off than those without loans in all three categories. Presently, 47 percent of employers conduct credit checks before hiring.

A lousy job market ever more dominated by low-income and part-time work ensures that a growing section of the population, particularly working class and middle class youth, face decades of indentured servitude and a declining standard of living as they are crushed under debt. Half of recent college graduates are either unemployed or underemployed, and average yearly incomes for 25- to 34-year-olds with a degree is down about $10,000 since 2000.

With the aid of the Obama administration, Wall Street has been able to make huge profits out of this situation. As the administration pumps $85 billion per month into the financial sector, a market frenzy for student loans has emerged. In March Sallie Mae (SLM), the former government entity that has turned into a student loan originator, collection agent and debt seller, announced that it had sold $1.1 billion worth of new student loan debt securities. SLM itself made $514 million in profits in the fourth quarter of 2012.

As students are forced to borrow and repay more and more money, a growing student loan bubble could also threaten to destabilize the economy in the same way the housing and dot-com bubbles did in the first decade of the 21st century. Securities called SLABS (Student Loans Asset-Backed Securities), first created in 1992 by Sallie Mae, now account for between a quarter and a third of the $1 trillion total of student loan debt, and are on the rise. As with the subprime loan racket, SLABS are often bundled with other kinds of loans for trading purposes.