Ep40: America's Student Loan Crisis

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PATTI BRENNAN: Hi, everybody. Welcome back to "The Patti Brennan Show." Hey, whether you have $20 or $20 million, this show is for those of you who want to protect, grow, and use your assets to live your very best lives. Joining me today is Peter Sims. Peter is the president of PayForEd.

Today we're going to be talking about the student loan crisis, and how we as American parents can look at this question of putting our kids through college, and what is the most cost-effective way of financing that. Peter, welcome to the show.

PETER SIMS: Thank you for having me.

PATTI: Thank you so much for coming today. It seems like every other day I see a new headline about the student loan crisis. While we have boots on the ground and we see it every day, is this thing overblown?

PETER: Patti, I asked myself the same question when I entered into this field a couple of years ago, from being in the financial services for 30 years. Is it really a crisis? Not only is it a tremendous crisis right now, but it's growing. Currently it's $1.6 trillion. If I go back to 2005, we were a little over 500 billion.

PATTI: I was going to say. That is really fast. The last time I looked at it, it was $1.2. It's $1.6 now?

PETER: $1.6 trillion, and it's affecting nearly 50 million people. What the scary thing about it for me is, we've got 59 million people in secondary and educational schools. That's going to keep on growing.

PATTI: Oh brother. It's getting worse before it's getting better?

PETER: Correct.

PATTI: And you know, folks, this is a really important issue because here we are in an election year. As we all know the candidates are talking about it – it's really a popular topic. Rightfully so because it's affecting so many people. It's really good to have you here today, Peter, because I think that your company focuses on the solutions.

PETER: Correct, and Patti, you made a great point. There's over 137 different forms of legislation mentioning student loans, student loan repayment, sitting in the legislative bodies as we speak. As we're going through them, it could be added on, but it is a complex situation that we need to find a solution for.

I think that it's not only a solution for the current debt, but we've got to start preventing it. If you think about a medical situation, yes, you want to cure the current epidemic that's out there, but don't we want to prevent it?

PATTI: Yeah, absolutely.

PETER: That's where we come in.

PATTI: What I thought was interesting as I was doing the research today for the show, I was really fascinated at some of the statistics out there as it relates to graduation rates.

I have four kids Peter, and I know that you have...How many kids do you have?

PETER: I have four.

PATTI: We're eight between the two of us.

Wow. We are totally contributing to this crisis. I can tell you, when the Brennan household and the Sims household...what I thought was fascinating was that the graduation rates aren't what you read about in the glossy brochures or the dog and pony shows that they put parents through when you're taking the kids around at different schools.

PETER: It is absolutely mind-blowing at this point of time. If you look at the four-year schools, the graduation rates are less than 40 percent in four years. You're also talking about graduation rates of less than 60 percent in six years. Here's where it becomes extremely troubling for me. Transfer rates are around 35 percent.

PATTI: Now, why is that?

PETER: When people first go into a university or a college, and you saw that glossy brochure that you looked at, it is a wonderful choice. Think about it from a parent's standpoint, it's emotional.

You're so glad that your child is going but what you didn't really think about is how are you going to fund year two, three, and four? Financial situations end up being a large part of the transfer process.

Also, the way kids are looking at schools these days. Years and decades, and decades ago, we visited schools, then apply. Now, it's reverse. People apply and then go visit the schools that they've done a research on. Not knowing the school, not knowing the financial aspect, or the outcomes of your decision, leads to the transfer rates.

In addition, too, you'll also have people changing majors at a more rapid pace than ever before. I saw a recent statistic last week, that 50 percent of the students are changing majors at one point in their educational journey.

If you really look at the statistics — I was on a conference call last night – that applications are up, and admissions are down. That's one of the reasons why we see the tuitions increasing at the rate that they are. College tuition, believe it or not, is up 1,400 percent since 1978.

PATTI: Wow.

PETER: That's four times more than inflation.

PATTI: The graduation rate is really an important thing that we all have to keep in mind. I told my kids...My oldest took longer than four years to go through school.

The other three, I said, "OK, here's the scoop. We'll help you the first four years, after that you're on your own." You know what happened? All three graduated in four years.

Isn't that interesting? You know what? You also think about the universities, it's a business, right?

PETER: It is absolutely a business.

PATTI: Their job is to get students, put students in seats and keep them there.

PETER: Yes.

PATTI: They want to keep them there for that fifth and sixth year.

PETER: It's not hurting them at all for that person to come in, in particular, the people that are, say, full pays, or the people that are funding their education through loans. Getting a loan is quite easy to do in the federal system itself.

PATTI: Is that why you think the crisis is growing so quickly because it's so easy to get these loans?

PETER: I think that's absolutely one of the reasons. We talked about one, is that the tuitions are increasing very rapidly. We see people staying in school much longer. Now it's the access to capital through the federal government which makes it easier to pay for those additional years. It's adding on.

If you really look at it too, the way in which the loan structure is out there, it's complex, and people understand it. If you don't understand it, you just push it off to the side.

I always say that what we have to stop is the current strategy of hope. Hope has been the strategy [laughs] for many, many parents that are out there, "We'll figure it out later." Well, later is now because it's affecting yourself. It could be affecting the parents, the grandparents, and most importantly, the students.

PATTI: Absolutely. You think about the domino effect of kids graduating with $50,000, $100,000 of student loan debt. As we really think through this, and you and I both know, that has had an incredible economic effect on our country.

You think about the last 10 years and the slow growth of economy that we've experienced. You wonder, did one cause the other, or is one a contributing factor?

These kids are graduating with six-figure loans. They often then put off decisions that you and I might have made, getting married, buying their first home, having children. That has a trickle-down effect, doesn't it?

PETER: It absolutely does. If you are thinking about the direct economic impact, think about student loans. It's growing faster than credit card debt, mortgage debt, and most of the debt that's out there.

You mentioned some of the situations. You graduate with 30, 40, 50 thousand dollars' worth of loan. You're not able to put money away for a house so that affects the housing market. The housing market is cyclical in which people buy and sell houses. If you take buyers out of the marketplace, that affects it.

You talk about the situation where the entrepreneurship. If you've got $50,000 worth of loans, how are you going to start your own business? America was built on small business owners, so we're taking that out of the factor.

We also have the next scenario of retirement. What I mean by that is, say a parent is taking money out of their retirement plan to pay for education...

PATTI: A big no-no, folks.

PETER: Big, big no-no. All of a sudden, they've got to stay and work for an additional two, three, four years.

How does that affect the economy? It affects the economy in one way, directly is that the company now is going to have to pay healthcare benefits for an older person which is going to affect their bottom line, which is going to affect their staffing and the way in which they grow their business.

Little decisions are affecting the economy across the board. It is truly amazing how much of an impact that we're seeing now, and that more importantly, we're going to see in the next 10 years.

PATTI: When you really think about it, think about that older worker staying in that job, and we've got these kids that are graduating from college, and they're not getting promoted because guess what? The opportunities for growth within the organization aren't there because people are staying longer.

PETER: Very, very true. That means what? They job hop. The average person stays in the job less than three years now. It's probably close to 2.3, 2.4 years. How does the company invest in someone that's only going to be around so long? That affects the productivity of the company. Where are we going to be?

PATTI: Exactly. What about graduate school? I have a lot of friends who are physicians, attorneys, etc., and they're graduating with a debt of $200,000. Especially in the physician market, a lot of physicians aren't going into private practice anymore.

Their incomes are limited. They're being employed by hospitals. It's a wonderful opportunity and they're doing their life's vocation, but they've got this thing hanging over their head. It's a very different professional career path than it used to be.

PETER: Patti, that scares me the most. Three reasons, why. One, more and more companies are requiring a graduate school degree to move forward in their companies, which is in the business world, a growing situation. You think about medical school, doctors, teachers, education, in your master's degree at that point of time. That is only going to keep on increasing the debt.

However, you've mentioned numbers of 200,000. I had a conversation with someone in Philadelphia recently, that the average debt coming out of some medical schools is much more north of that, $300,000. Does that deter a qualified candidate becoming a doctor? Think about where we are as a nation if we lose our doctors and our teachers.

Two areas that need a graduate degree, it's becoming much more expensive. Even on the loan front, graduate school loans cost about 500 basis points or five percent, more than undergraduate loans.

PATTI: I didn't realize that. Wow.

PETER: As a strategy, some people say, "Well, we'll pay for undergraduate and graduate school is on you." You might want to rethink that strategy with your advisor, because it's much more expensive to borrow money later on.

PATTI: Very interesting. It's this whole thing. It's a web of complexity. You've got all the different loan programs, whether Parent Plus, Stafford, all of these different programs. I will tell you because I have your software, thank goodness, because your software helps us to really differentiate and optimize this whole question of how do we finance the education of our family?

You go into that and let's talk about the different types of loans. Let's break it down, Peter, between the federal loan programs and private loans. What's the difference between the two?

PETER: From a basic standpoint, the federal loans are issued by the government themselves, private loans or private sector loans that are there. There's three main differences that are out there. One would be the interest rate. Private loans, sometimes you qualify for a lower interest rate depending upon your creditworthiness.

The second factor is the amount of money that you can get on a private loan can be higher than a federal-government loan. The biggest difference is the flexibility. Flexibility of the federal loan is much better. If you T-charted it, it really depends upon your situation and that's one of the solution is.

Too many people talk about generalities, in regards their college planning, funding, and student-loan repayment. You have to take the approach of, it has to be customized towards yourself.

We'll go back to our other comment that you made, people going into different schools. If I'm in the same situation or my child's in the same situation as my neighbor, and they got into ABC school that's out there. My child's going to get in. No, it's much different depending upon your situation and what the school wants.

My biggest suggestion to everyone out there, is you need a customized solution to make the right educated decision.

PATTI: That's what real financial planning is all about, customized solutions that are geared towards the needs of the family. We're not necessarily looking at things, in this silo of college education. How does the college education decision affect other areas of a family's financial life? It really has to be holistic.

Here's a question for you. I'm going to tell you what a parent said to me recently. We were talking in the conference room, and he referred to college these days as adult daycare. It begs the question, is college still worth it?

PETER: Yes, it is. From a basic fact people make twice as much money. A recent study that came out, twice as much money of a lifetime having a college degree, than a high-school degree and more money as a graduate degree. What you do with that degree is another different story at this point of time.

Is education worth it? Absolutely. Is the daycare comment warranted? Yes. It's in association with five, six, seven, eight years of education. I know a good friend of mine took his decade-long educational route, but that could be qualified as daycare.

I personally believe that all parents should think about the fact of taking out a federal Stafford Loan, for the mere fact, that their skin in the game for the student themselves. If they have the assets to pay, put that into a plan. When they graduate in four years, pay off the loan.

If they have the knowledge that, that loan is on them, it might take away a little bit of that daycare scenario.

PATTI: Absolutely. It is an important point that you bring up, because when they do have skin in the game, they do understand they're involved in the process. We sit down with these families and the kids to talk about the different alternatives and give them real numbers and what it's going to mean for them, once they graduate.

If you go to this school, here's the financial ramification. If you go to school B, here's the ramification. One campus might be more beautiful than the other. Ultimately, what do you think you really want to do? Does the college provide a good depth and breadth of alternatives?

We don't necessarily want to encourage the kids to, as Peter Sims says, make your own major. I want to take a little bit of this, a little bit of that. At the same point, we also want to recognize that a lot of kids don't know what they really want to do.

I remember having a conversation with my daughter when she was a sophomore in college and I had, we call, the "deep and real." We're having a deep and real and to Carrie, I said, "You know, Carrie, communication, tell me what that means to you? What do you see yourself really doing with that? By the way, if money wasn't an object, what do you really want to do in your adult life?"

That was an amazing conversation. It opened up a wonderful thought process for her. She's up in Brooklyn, New York now acting. Who would have thought? It's very interesting because that degree in communication was focused on writing skills. She's written an entire movie, she's producing it, she's directing it, she's starring in it.

Talk about communication. You can't get much better than that, right?

PETER: Absolutely.

PATTI: It's a very interesting thing, in terms of, having that conversation with our kids. It's not only about the money, but what they see themselves doing and what their unique gifts are.

PETER: Patti, first of all, thank you for doing that with your clients. There's not many people across the country, who are advisors, that do that. They have to do that.

One of the most effective questions that I've ever seen an advisor ask, "Why? Why do you want to go to school?" That starts narrowing down the situation, not if you're going to go south, north, west. Why do you want to go to school?

I do believe advisors need to help families start getting a path of that university. The idea of trying to figure it out when you're in school, that might be OK, when school costs about $5,000. Now we're talking about quarter of a million, half a million, a million. That's a lot of money to try to figure something out.

Advisors need to be that third party in helping the families understand, what you said, financial outcome.

PATTI: It's OK also, not to go to that four-year college down south, or across the country. It's OK to go to a community college or, better yet, a trade school.

I will tell you Peter and folks in the audience. I will tell you with all of my kids, especially my daughters, I said "You know what you don't have to go to college. Yes, I want you to get a college degree eventually. There is nothing wrong with trade school, go be a plumber."

Can you imagine a young woman showing up at your front door to help you with your plumbing? They'd kill it.

PETER: Patti, my guys, I have four. I've got a 17, 15, 13, and 11-year old. When I think about the future of education, I also think about the society we've grown up in. I've got three boys and a girl. I came from a very large family of seven children. We were kicked out of the house, and we actually, believe it or not, rang a bell to come home for dinner at that point.

Today's society is so structured. Think about athletics. They're structured, there's not very many pickup games. The reason why I mentioned that is that they haven't been able to explore their own individuality. When you mentioned community college, that's the first step in adulthood without sending someone off at that point of time. I'm a big believer in the future of 2+2+2.

PATTI: I love that. You told me about this, Peter. I think it could go viral.

PETER: Two years of community college to make a better understanding of what you want to focus on, but not taking the financial repercussions of some other decision that you make. Two years to really focus upon what your major is going to be, and then the advanced degree in grad school.

I think if you take a mature approach in looking at what you really want to do, that's an excellent solution. I'm sure if my 17-year-old hears me say this, he might not be happy with me. That's the discussion that need to happen. I think that more people need to help families, advise them on the financial situation. You've gone through it. I'm going through it. Making that choice for college is emotional.

PATTI: So emotional.

PETER: I've heard you talk about, what's the problem with making an emotional decision with your investing?

PATTI: Yeah. It's a loser's game. It creates impulsive decisions that often people look back and say, "Why did I do that?" There's a lot of remorse with that. Unfortunately, with this, it follows these kids and these parents for years. 10 years, 15 years, this debt is hanging over their heads. I think it's even worse because a lot of kids are graduating and they're underemployed.

PETER: Yes.

PATTI: They're not even earning the income to be able to manage it.

PETER: No. It becomes very, very...not only financially it's a hardship, but it's also emotionally discouraging to them. That's a repercussion fact down there, at that point of time. Having a third party or second opinion come into the conversation is much more powerful.

Advisors need to understand educational planning like you do. It's just like retirement planning, if you come down to the basics, accumulation, and distribution, and then maybe legacy. It's the same thing with educational planning. There's accumulation, distribution, and maybe legacy, if there's a 529 moving on at that point of time.

However, one of the things that I'm asking people to think about when they're talking to their clients, is you need to break down that stigma that if you have debt you've failed. Hey, at this point, if you looked at a college cost analyzer...and I'll use just basic data. $2,500 goes into an account, you put $250 away a month, at an eight percent rate of return historically.

You might think as one child, you funded an education for your child. You might have funded maybe a third of it, or a quarter of it. It's not a matter of saying, "OK. Am I going to have to take debt?" It's, how do you want your financials to be structured? Start planning for it now.

PATTI: How does your company, how does PayForEd help people, help parents, or advisors, or even companies help their employees, for example, manage the debt that they might have accumulated? Tell us more about that.

PETER: In a simple way, we provide transparency and simplicity to a complex process. We give you the information and education that you need to make decisions. What does that mean? I always use a simple term. Think about TurboTax. TurboTax for education student loan planning.

You put your input in, but it's customized to you, and it gives you a strategy at the end on how to pay for it. We help people make these simple decisions that they might not have access to right now. It's very difficult to get the information you need because there's so many different parts that you're pulling on, and then it becomes overwhelming. What happens? You don't do anything.

PATTI: Isn't it true? I think you told me there are 128 ways to pay back a student loan.

PETER: If there's a married couple and both have student loans, and they're entering the workforce, there's 126 different options you can choose from.

PATTI: OK. OK, I overstated by two. Isn't it amazing?

PETER: Hey, listen, we could be at 130 by the time this legislation gets done.

PATTI: Yeah, yeah, yeah. Wow. It is amazing.

I will tell you, as the owner of your software, thank you so much. It does break it down and make it so easy for us to look at the options and optimize it for each individual family.

It's a great, great tool. Peter Sims, I could be here all day talking with you. You're so much fun with not so fun topic, by the way.

PETER: [laughs]

PATTI: I got good news for everybody listening, we're bringing him back. Stay tuned, because in the next episode Peter's going to join me again.

We're going to break down the tools available to get the real skinny on graduation rates. We're going to be looking at the different universities, public university versus private.

It’s not always what you see. It’s not always what’s on the piece of paper.

Peter’s going to walk us through the FAFSA form. What does that really mean? Who should be filling it out? Should you bother, etc.?

It’s going to be a great, great show. Please join us for the next episode.

In the meantime, Peter Sims, I can’t thank you enough for being with us today. Thank you for your input, your wisdom, everything that you’re doing.

I know you’re doing some work down in Washington. Oh boy, help us solve this crisis, Peter.

PETER: Thank you so much for having me. I look forward to coming back.

PATTI: Thank you. To all of you, thank you so much for joining us today.

If you have any questions, if you would like to learn more about the student loan crisis or how you can apply what you’ve learned today, and the tools that Peter and I are talking about, go to the website, put in a question or give us a call.

We’re here to help you. Until next time, I’m Patti Brennan. I hope you have a wonderful day.