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OPINION

Government creates the next bubble in higher education

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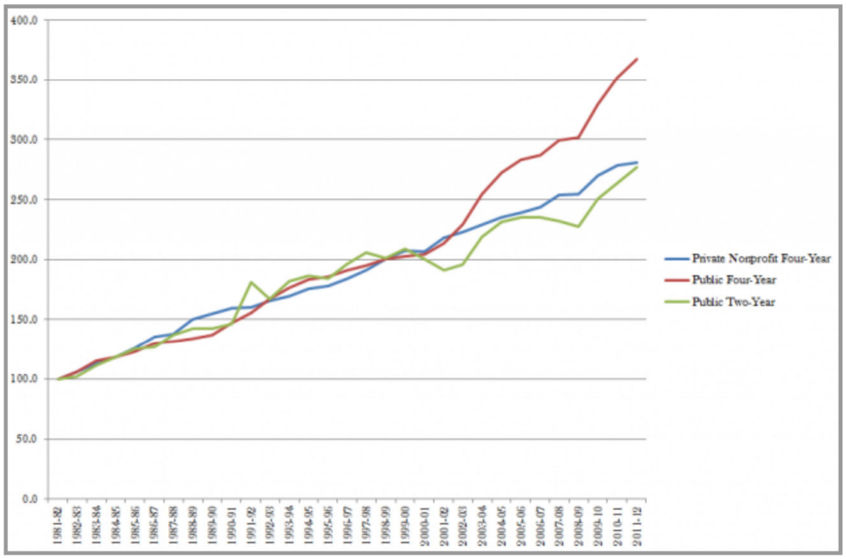

College grade inflation: Inflation-adjusted growth in college tuition and fees since the base year of 1981 (set at 100 percent). Public four-year institutions, which were cheaper to begin with, have led the way with tuition increases approaching 270 percent. Private four-year institutions and public two-year colleges have both raised prices by about 180 percent in the same period. Source: The College Board Advocacy and Policy Center.

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A phoenix has risen from the ashes of the Occupy movement. As anger over the housing crisis wanes, protesters have returned home from their camps to find student loan bills -- one trillion dollars' worth. Ironically, it is now they who are looking for government bailouts -- and from a hole that government essentially put them in.

The impending student loan crisis, like the recent housing crisis, is born of government meddling, and promises to have similar results. But with the students, the coming bankruptcies will be much worse.

The anatomy of the housing crisis is simple. Years ago, the U.S. government decided that the path to prosperity was homeownership. When the free market did not provide what the government considered "enough" housing, the government used both carrots and sticks to force markets to lend more money for mortgages.

When private banks shied away from high-risk borrowers, the government instructed its enterprises, Fannie Mae and Freddie Mac, to direct more than 40 percent of their lending toward low-income borrowers. These two

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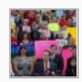
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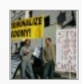
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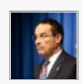
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government-sponsored enterprises took lending risk away from private banks and placed it on the backs of taxpayers instead.

The government also offered tax incentives for people to take on more mortgage debt, and the Federal Reserve made mortgages cheaper by holding interest rates at historically low levels. Predictably, people rushed to secure cheap mortgages, fueling a boom in homebuying and causing home prices to soar over 400 percent from 1976 to 2010. When the rush tapered off, households realized they could not afford to pay their mortgages and declared bankruptcy in droves.

The anatomy of the student loan crisis is similar. Having decided that the path to prosperity is a college education, and that the free market was not providing "enough" college education, the federal government created Sallie Mae (and later, used the Department of Education) to take lending risk away from banks and place it on the backs of taxpayers. The tax code provided modest tax incentives for students to take on more loans, and lately, the Federal Reserve has continued to make borrowing cheap by holding interest rates low. Sound familiar?

As with housing, the price of college education has skyrocketed over the last 30 years (see charticle). Just as homebuyers borrowed to speculate on houses they could not afford, students now borrow to speculate on educations that many will not complete, and which others may find to be of little value.

The impending burst of the education bubble will be far more damaging than the housing bubble. When homeowners got behind on their mortgages, they can declare bankruptcy to free themselves of crippling debt. Either they or their bank can offset some of what they owed by selling the collateral -- the house. Students cannot rely on either of these things. Bankruptcy does not wipe out student loans, and an education cannot serve as collateral.

In both housing and higher education, government failed to seek out the reasons why there was not "enough" lending going on. Many people were in no position to afford the loans, and the banks couldn't afford the risk. With unbounded hubris and dogged myopia, politicians decided to "fix" the market by forcing people and banks to do what each had determined was imprudent.

Just as the government sought to engineer an increase in homeownership, it now seeks to engineer an increase in higher education. This is the stuff of which bubbles are made.

The solution is economic freedom: Let private banks determine lending without government interference. Allow people to decide for themselves whether one level of debt or another is prudent. This latest bubble will burst, as they all do. The government, unfortunately, will be there to create another.

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