ECO 150, Fall 2022, Required Homework Assignment #1

Key

1. The basic proposal is for up to $10,000 of student loan debt to be forgiven for most holds, with a higher limit of $20,000 for those who received Pell Grants (a proxy for low income households). There is a $125,000 income limit for individuals and a $250,000 limit for married couples. In addition, the plan proposes capping student loan payments at 5% of disposable income.

The basic motivation is to provide relief for heavily indebted households and to reduce the de facto cost of college.

2. The primary winners are households holding student loan debt. According to the Wharton School's analysis, 65% of the benefits are likely to go to households in the 40th-90th percentile.

3. This plan essentially transforms student loan debt into public debt. The primary losers are thus households who do not own student loan debt but who will bear increased tax risk from higher public debt. The Wharton analysis suggests that these are concentrated in the top 10% of the income distribution and the bottom 40%

4. It can be argued that education is a positive externality where the private consumption of education benefits those not directly involved in the transaction. This may be because a more educated populace may exhibit more socially desirable behavior (less crime, more voting, etc.) If so, the policy may incentivize greater educational attainment by subsidizing education.

5. Moral hazard refers to cases where people may take on too much risk because they expect to be bailed out by someone else, often the government. In this example, student loan forgiveness may encourage households to take on too much student loan debt because they expect another governmental bailout.

6. Question #4 provides a theoretical benefit of the policy while #5 provides a theoretical cost. We do not, however, have evidence on the zise of these effects. This is a question for empirical economics. Good evidence that quantifies moral hazard and educational externalities would be helpful.

7. One source is the Board of Governors of the Federal Reserve.[1] This series reports the total level of outstanding student loan debt in the U.S. by quarter.

[1] Board of Governors of the Federal Reserve System (US), Student Loans Owned and Securitized [SLOAS], retrieved from FRED, Federal Reserve Bank of St. Louis; https://fred.stlouisfed.org/series/SLOAS, October 3, 2022.

8-9.

2019-01-01	1597.65409
2019-04-01	1603.29289
2019-07-01	1635.13196
2019-10-01	1637.88071
2020-01-01	1671.96878
2020-04-01	1672.50313
2020-07-01	1696.47462
2020-10-01	1693.86025
2021-01-01	1718.70655
2021-04-01	1719.06750
2021-07-01	1739.44383
2021-10-01	1733.41518
2022-01-01	1747.45551
2022-04-01	1748.25432
AVE	1160.074805
ST DEV	408.9095366

10. Real means that the data are adjusted for inflation. If inflation were 8% between 2021 and 2022, for example, we would want to increase the 2021 figure by 8% to get it in "2022 dollars." Per-capita mans per-person. We would want to divide our data by the population.