

EconoFact Chats: How Much Does Going to College Cost?

Phillip Levine, Wellesley College

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Michael Klein:

I'm Michael Klein, Executive Editor of EconoFact, a nonpartisan web-based publication of the Fletcher School at Tufts University. At EconoFact we bring key facts and incisive analysis to the national debate on economic and social policies, publishing work from leading economists across the country. You can learn more about us and see our work at www.econofact.org.

Michael Klein:

In the preface to his book on the cost of college, 'A Problem of Fit,' Philip Levine describes how his parents struggled with figuring out how they were going to pay for his college education and their difficulties in filling out financial aid forms. Something that many of us have experienced. Phil ended up attending Cornell University, parts of which are funded by the State of New York; before getting his doctorate at Princeton and becoming a professor at Wellesley College. That experience shaped some of Phil's research, as did his work on behalf of Wellesley for their board of admissions. In fact, it prompted him to develop an internet-based tool, MyinTuition, that helps families better understand how much it would cost to attend college.

Michael Klein:

College costs are far from straightforward. For the vast majority of those attending four-year private colleges, it is not the sticker price. Rather, colleges offer a range of different types of financial aid, but it's hard for families to figure out beforehand how much financial aid they're likely to receive. What are the problems that arise from the opacity of college costs for families, and for colleges and universities? What are some reasonable plans to make college more affordable? To answer these and other questions about college affordability, I'm very happy to welcome Phil Levine to EconoFact Chats. Phil, thanks for joining me today.

Phil Levine:

Thanks for having me here.

Michael Klein:

Phil, let's start out by asking the question of whether or not college is actually a good investment from a purely economic perspective?

Phil Levine:

Sure. I think before I get started, I should mention that the remarks that I'm going to make today are largely focused on students who are dependents, traditional age, and enrolled at four-year residential colleges and universities. So the ones that "charge," I'll come back to that later, potentially \$30,000 at a public institution or \$80,000 at an elite private institution. That said, the returns to a college education these days are very large, on the order of hundreds of thousands of dollars over a student's lifetime. Far in excess of what a college education today. Certainly at full price, but most students receive financial aid. If you are paying some fraction of the total price, because you're receiving financial aid, this is certainly an investment, and any discussion that maybe college isn't worth it, I would argue is misguided.

Michael Klein:

So in A problem With Fit, you mentioned that you describe and analyze college pricing in your Principles of Economics course or ECON 101 course. How do you explain it in this course?

Phil Levine:

So if you think about it, in a traditional ECON 101 course there's supply and demand and consumers and producers and markets. And that's not really a lot different than what's going on here. That there's the supply is what firms provide, are the colleges. And there's demand, which is what the students are demanding. Those are the consumers. They meet in a marketplace and prices are set in markets. So I think it's perfectly natural to think about college pricing as something that you can incorporate into an ECON 101 class.

Michael Klein:

So what are some of the facts about college pricing? How many students receive financial aid at private colleges and at universities, and how many at public ones? And what forms does this financial aid take?

Phil Levine:

So this is this issue about sticker price. That \$80,000 and \$30,000 number I mentioned before, those are the numbers that people know. The thing is that there's very few people who have actually pay those numbers. Almost the large majority of students in the country receive some form of financial aid. The financial aid could come in the form of grants, could come in the form of loans, or it could come in the form of work-study funding. No matter how you look at it, though, most students receive financial aid. At private institutions perhaps 90% of students get financial aid, at four-year public institutions 85% of students get financial aid. Those sticker price numbers are just not relevant for most people.

Michael Klein:

So the sticker price doesn't stick?

Phil Levine:

Not for very many people. And the ones for whom it does are very high income.

Michael Klein:

So even with this financial aid, are private colleges and universities, pretty much the enclave of the upper-middle class and the rich? And if this is true, what are the implications for social mobility?

Phil Levine:

Yeah, it certainly is true that college enrollment is skewed by socioeconomic status, particularly at private colleges and universities. The issue is why? And certainly, pricing is an important issue here, but there's other issues as well. So for instance, the K-12 education system isn't exactly a level playing field. That also contributes to the problem. But regardless of the reason, it's something that we need to fix. Because if we want to expand social mobility, if we want to provide economic opportunity for every student, we need to be able to provide ways for everybody to go to college. And for them to go to college that's a good fit for them.

Michael Klein:

You use the word fit. And that of course is in the title of your book, A Problem of Fit. What do you mean by fit exactly?

Phil Levine:

So I think the right way to think about it is there in some dimensions there's a good fit school for everybody, regardless of who you are and your qualification. There's a school that's right for you. Harvard might be it. You might be the perfect fit student for Harvard. That is true for a very small number of people. But for those, for whom it is, that's where you should go. Other people are good fit students at a place like Ohio State, other students at community college. Some students might be a good fit, not at college at all, a trade school might be the right solution for them. The issue that we face is finding ways for everybody to get to the school that is the good fit school for them. If they're not, that's creating something of an inefficiency. And what we need to think about, are there elements in the financial aid system that are preventing that from happening?

Michael Klein:

So in particular, I think the problem would be that low-income students who might be a good fit at expensive private colleges and universities don't attend. There's what you call an undermatch, right?

Phil Levine:

Yeah. So undermatching is an example of where high-quality, highly capable students from lower-income backgrounds don't find out about their options for attending elite private institutions. That's sort of just a specific example, but it really goes all the way through the spectrum. At public institutions, they lose students who choose to enroll at community colleges because they don't feel like they can afford the residential expenses of the four-year institutions. There's students who may be good fits at community colleges who decide not to go to college at all, because they feel like they can't afford it. To the extent that the pricing system is preventing students from attending the institutions where they're a good fit, that's a problem, and something that we need to fix.

Michael Klein:

So we're talking about a problem of fit for students and how it affects students, but in your book, you also write about a problem of fit for colleges and universities, and they're harmed by not having the right students there as well.

Phil Levine:

Yeah. I mean, the people that I talk to at colleges and universities also are sort of looking for more. So what are they looking for? At the higher-end institutions, they're looking for more socioeconomic diversity, they feel like they're not able to attract the lower-income students that they'd like to be able to get. This is the issue of undermatching. For everybody else, the issues are about enrollment. That especially as we head into a period in which cohort sizes are going to be declining, the ability to attract enough students is going to be an issue for ... It's an issue now, and it's going to be a bigger issue for them in the future. How do you get enough students to come? And so if there's this chain reaction of public four-year institutions, losing students to community colleges, who lose students not going to college all. If we can fix this pricing system to get everybody to go where they're supposed to go, where they're a good fit that will increase enrollments everywhere.

Michael Klein:

So there's a demographic challenge facing colleges and universities too. Nathan Grawe who's at Carleton College has written about this for EconoFact and I've also interviewed him about it. Phil, let's talk a little bit about how financial aid works. And you described your father using some choice words that I can't repeat in this podcast, while he sat at the kitchen table, trying to fill out financial aid forms. Has applying for financial aid gotten any easier since the early 1980s?

Phil Levine:

You know, really it hasn't. At the end of the day, you're going to put a form in front of someone and ask them a whole bunch of complicated questions that requires knowledge of the tax system, detailed knowledge of their assets and liabilities. And you're going to ask them to complete all of this within some relatively short period of time. I mean forgetting about the assets and liabilities, just the taxes, people don't like taxes. They certainly don't like doing their taxes. Most people don't do their own taxes. They either use TurboTax or some such thing or hire it out. And then you ask them to do stuff themselves that requires tax knowledge. Well, they don't like that and they have difficulty doing that. And so it's no simpler now than it was then.

Michael Klein:

Has the Federal Government taken some steps to try to make this easier for people?

Phil Levine:

There's definitely been some recognition that this is a problem. There was a law passed in 2008 that went into effect in 2011, that required institutions to have net price calculators on their websites. These are tools that are designed to help students try to figure out how much college is going to cost them. They often have similar problems of requiring tax information that scares people off. There was in 2020, FAFSA Simplification Law was passed. It's still too early to tell exactly how effective that is going to be. That doesn't go into effect until 2024. But from where we are right now, we certainly have a problem of complexity that makes it very difficult for people to figure out how much college is going to cost them, and for them to make the right decision about what college to attend.

Michael Klein:

Phil, is the problem of college pricing, different across public and private colleges? And is it also different between private colleges that have big endowments and those that have smaller endowments?

Phil Levine:

If anything, the institutions that are able to do the best job in pricing are the high-priced institutions with large endowments. The reason is because their high prices are only paid by higher-income students. Those additional revenues that they get from them can be used to subsidize lower-income students. Their large endowments can be used also to help subsidize them. Those are the institutions at which lower-income students actually pay affordable prices.

Michael Klein:

How well known is that? Harvard had this program where tuition was going to be free if your family's income was lower a certain amount. And that got a lot of publicity, but maybe only among a limited group of people.

Phil Levine:

What's interesting about that is finding ways to communicate those messages and keep it in the public's eye is really difficult. You get one big shot where you make your initial announcement, but then how do you keep the lens on that? Especially given the fact that there's constant media attention telling people that college is very expensive and Harvard charges, \$80,000 a year. They do, if you're high income. The fact that they charge virtually nothing, if you're low income, that tends not to make it into the newspapers.

Michael Klein:

So Harvard is able to do this because they have a huge endowment, but I imagine that other private universities with smaller endowments just can't do that. And so maybe they can't lower the sticker price that much, is that correct?

Phil Levine:

It is. And the issue that other private institutions face is they have to compete with public institutions. Public institutions are forced by law to limit their sticker prices, to the number, like \$30,000. So for those institutions that reduces their revenue, which makes it difficult for them to provide sufficient financial aid. It also means that for other private institutions they have to compete that if they're not at the level of Harvard, they are competing with public institutions. They can't charge that much more than the \$30,000. That limits their revenue and makes it difficult for them to provide sufficient funding for lower-income students too. And at those institutions, at least at public institutions, they have resources available and direct state funding. The private institutions, the tuition dependent private institutions don't have that. And they don't have endowments or anything to speak of because they have no additional sources of funding to help make the system more affordable for lower-income students.

Michael Klein:

So you've used the word compete a few times just now. Economists often think that competition can help solve problems. What's the scope for competition for students among colleges and universities to solve the problem of college affordability?

Phil Levine:

I think it's almost a knee-jerk reaction among economists to think that competition is the answer to everything. It does very good things in most circumstances. It has the ability to maintain lowest possible prices, most efficient production. And for a whole range of issues, competition is a good thing. It's just not obvious in this case, that it is. The reason is because I think we value the financial aid system. We value the fact that higher-income students pay more than lower-income students. In economic language that's called price discrimination. To be able to price discriminate, it has to be the case that firms have market power, it can't be perfectly competitive. The more market power you have, the greater ability you have to price discriminate. If anything, a perfectly competitive system would satisfy the law of one price, everybody pays one price. There's no financial aid in that system. That would be great if you were high income, but terrible if you were low income.

Michael Klein:

Also, price discrimination works really well for colleges and universities because they have all this information about what you can afford. It's kind of like if you went to the supermarket and brought your tax forms along, then they would charge you differently, if you were rich than if you were poor for the same dozen eggs.

Phil Levine:

Definitely. There's conditions that need to be met for a firm to be able to price discriminate. And distinguishing across customer types is one of them. That's exactly what the FAFSA, the financial aid forms do, is enable schools to distinguish across customers. The other interesting difference is that these are all institutions that we're talking about in this context are nonprofit. For-profit firms, if like you're describing, if you were for-profit that could price discriminate, you would make a lot of money. There'd be excessive profit in those contexts. These institutions that we're talking about here, colleges and universities are not-for-profit. The revenues that they get in excess of their costs for the high-income students, which would be profits in the private sector, can't just get held. They have to be transferred to the lower-income students, and that's why the whole system works.

Michael Klein:

So there's been a lot of talk about free college. Is that a viable policy option?

Phil Levine:

Is it a viable ... Before we talk about free college, I'd prefer to talk about my preferred solution, which is doubling the Pell Grant. So the affordability gaps that we see among lower-income students are on the order of \$5 or \$6,000 a year. Like that's sort of what colleges charge them, that they can't really afford. The current maximum Pell Grant is \$6,500. Doubling the Pell Grant pretty much fills in the gap in affordability. It does so for exactly the right students, for the lower-income house students, lower-income families who have the greatest difficulty in affording a college education. And it's the right solution to addressing a problem exactly targeted to the people who face it the most. Free college has some different problems associated with it. Some proposals don't have income caps. I'm not a fan of providing subsidies to high-income students to go to college.

Phil Levine:

You can impose an income cap. Sometimes people propose \$125,000 as a cap. Again that's better, but not really exactly where the problem is in the market. It's really the lower-income students that face the greatest problems. And then there's issues about fact that free college is only for public institutions. From the story that I just told about the struggles that private institutions face, tuition-dependent institutions...not private institutions. They would be devastated by a free college policy. I'm not sure if that's something that we care about as a society, but it seems like having more choice is better.

Michael Klein:

Well as a professor at a private college, I'd care about whether my institution is devastated. We've been talking about pricing as a barrier to higher education, but there are lots of other barriers to higher education, especially for those who come from economically disadvantaged backgrounds, or those who would be the first in their families to get a college degree. Right?

Phil Levine:

Yeah. Going to college is a process. There are several hurdles that stand in your way, from thinking about should I go to college or not, at whatever ninth grade or eighth grade. Or whenever these discussions start, or if these thoughts start occurring, to enrolling, four or five years later. You have a lot of hurdles to get over. There's hurdles of, well, first you got to get through the K-12 education system. And that is not exactly a level playing field. There's the process of learning how college works, and how do you choose a college? Which is better or works better, if say your parents went, because they went through the process and they can help you with it. But if your parents didn't go or you're first generation or whatever, it's going to be a lot more difficult. There's the problems of filling out forms, applications, financial aid applications, there's test-taking, just any number of hurdles.

Michael Klein:

And yet pricing is a critical hurdle, right?

Phil Levine:

Yeah. I mean, and in essence, that's the focus of the book, is the price hurdle. And the reason why I focus on that in the book is because if anything the price hurdle is the first hurdle. If you can't get over the hurdle that college is affordable for you, or that you think that college is affordable for you, both of those two things have to be met. Before you can get over it, unless you get over that hurdle, the rest of the hurdles don't matter. What difference does it make, how hard it is to fill out a college application if you

don't think you can go. You have to be able to get people over the first hurdle of feeling like they can afford college and having it be affordable for them before we can deal with all the rest of those issues, which all need to be addressed too.

Michael Klein:

And as you said, people start to make these decisions in eighth or ninth grade. And if you think that college is unaffordable, you might make decisions that early on that makes it so that you don't go to college. So it's not only the affordability, but the perception of affordability as well.

Phil Levine:

Sure. At some point, it can become a self-fulfilling prophecy that you don't think you can go to college, so you can't go to college. And that's something that certainly we would like to try to avoid.

Michael Klein:

Well, Phil, thanks very much for joining me today and speaking about this very important issue, that's linked to so many other important topics like income inequality, and the possibility for people to improve their economic situations. And also thanks for your book, *A Problem of Fit*, which I think is going to be a really important contribution to public discussion on this issue.

Phil Levine:

Oh, thanks for giving me the opportunity to talk about it.

Michael Klein:

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