Credit and Insurance for Human Capital Investments

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Abstract:

Student loan debt in the US stands at roughly $1 trillion, exceeding credit card debt. In recent years, private lending for undergraduates has skyrocketed to account for roughly 20% of all student loan dollars disbursed. At the same time, youth from low-income families are significantly less likely to attend college relative to their higher-income counterparts. This paper examines the nature of credit for education in the presence of uncertainty and problems of limited commitment by borrowers, moral hazard, and adverse selection. Efficient lending contracts, combined with insurance against adverse labor market outcomes, are considered in a variety of economic environments. We examine the importance of different incentive problems in US data to aid in the design of improved credit and insurance for human capital investment.