Strategies for Shrinking Student Loan Debt

Agenda

1. The weight of student loan debt
2. How payments are applied
3. The impact of accrued interest and capitalization
4. Strategies to shrink the principal

The Weight of Student Loan Debt
The long-term cost of college continues to be a major challenge for millennials, even after they have established themselves in the workforce...

Source: Citizens Financial Group, 2016

A Lifetime Debt Sentence

Average length of repayment period varies by level of education

21.1 years was the average length for all levels combined

Source: One Wisconsin Institute

A Lifetime Debt Sentence

Average Length of Student Loan Debt

Source: One Wisconsin Institute
Life Milestones Delayed

56% of younger students with loan debt delayed major life events because of their loan debt compared to 43% of older adults.

| POSTPONEMENTS | 55% Retirement | 28% Having Kids | 14% Marriage |

Life Milestones Delayed

- Almost 30% of graduates postpone buying a home because of their student loan debt.

Life Milestones Delayed

Individuals who have already paid off a student loan were more likely to purchase a new vehicle.

- New: 51.5%
- Used: 48.1%

Student loan paid off

- New: 36.5%
- Used: 63.5%

Currently repaying student loan
Careers on Hold

Taking jobs below education level to keep up with student loan payments

- 44% of college grads are overqualified for what they do
- 20% of college grads give up on their preferred line of work to get a better job to help pay off their debt

Source: Forbes

Regrets

- 57% They regret taking out as many student loan
- 36% They would not have gone to college if they had known how much it was going to cost them

Source: Citibank Financial Group, 2016
Dissecting a Student Loan Payment

**Regular Payment**
- Monthly payment amount owed: $100
- Amount paid: $100

**Standard Plan**
1. Late fees (if any)
2. Accrued interest
3. Unpaid balance

**Income-Driven Plan**
1. Accrued interest
2. Late fees (if any)
3. Unpaid balance

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**Multiple Loans**
- Two loans: $3,000 and $2,000
- Amount paid: $100
- After accrued interest and late fees are paid: $50 remains

- Divide $2,000 by $5,000 = 0.40
- Divide $3,000 by $5,000 = 0.60

- $50 x 0.40 = $20
- $50 x 0.60 = $30
- $20 applied to $2,000 loan
- $30 applied to $3,000 loan

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**Partial Payment**
- Monthly payment amount owed: $125
- Amount paid: $30
- Accrued interest: $60
- Entire payment is applied to interest and $30 of interest is still owed on next payment.
Dissecting a Student Loan Payment

Extra Payment Amount

<table>
<thead>
<tr>
<th>Monthly payment amount owed: $50</th>
</tr>
</thead>
<tbody>
<tr>
<td>Amount paid: $125</td>
</tr>
<tr>
<td>$50 applied as regular payment</td>
</tr>
<tr>
<td>$75 applied to unpaid balance</td>
</tr>
</tbody>
</table>

The Impact of Accrued Interest and Capitalization

How Interest is Calculated

- Interest accrues daily on student loans

Simple Daily Interest Formula

\[
\text{Outstanding principal balance} \times \text{Interest rate} \times \frac{\text{Number of days in a year}}{365} = \text{Daily interest rate}
\]
How Interest is Calculated

- Interest accrues daily on student loans

**Simple Daily Interest Formula**

<table>
<thead>
<tr>
<th>$20,000 principal</th>
<th>× 6%</th>
<th>365 days</th>
</tr>
</thead>
<tbody>
<tr>
<td>$3.29</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Interest Capitalization

- Capitalization occurs when the unpaid accrued interest is added to the principal balance of the loan

Janna borrowed a $10,000 unsubsidized loan her first year. She leaves school and enters repayment. With a 6% interest rate, $902 accrued after the first year and during the grace period. $902 is added to the principal balance. She now pays daily interest on the principal balance of $10,902.
When Does Capitalization Occur?

- At the beginning of repayment
- At the end of a deferment or forbearance
- When the loan defaults
- When the borrower ceases to have a partial financial hardship or leaves the IBR, PAYE, or REPAYE plans
- Annually for the ICR plan, if the loan negatively amortizes (cap of 10%)
Shrinking the Principal

In-school Strategies

Out-of-school Strategies

Limit Borrowing

- Only borrow what’s needed to pay for educational expenses
- Look for alternative ways to reduce their need for loans

Apply for Scholarships

- Offices/organizations
  - Financial aid office
  - Civic organizations
  - Employer
  - Community service
  - Local library

- Websites
  - scholarships.com
  - fastweb.com
  - college-scholarships.com
  - mycollegeguide.org
  - finaid.org/scholarships
  - bigfuture.collegeboard.org/pay-for-college
Reduce Living Expenses

- Eat most meals in the dining hall, at home, or bring brown bag to campus
- Live with parents
- Share their residence hall room or apartment
- Use student discount
- Buy only the things they really need
- Leave car at home

Academic Planning

- Accelerate or graduate on-time
  - Map out classes to get the degree in less time
  - Meet with academic advisors regularly
  - Refrain from switching majors and/or school hopping

Know the Cost of Borrowing

- Use the Repayment Estimator to determine
  - Amount owed
  - Monthly payment amounts with various repayment plans
  - Total amount paid
  - Repayment period
- [https://studentloans.gov/myDirectLoan/index.action](https://studentloans.gov/myDirectLoan/index.action)
  - Sign in using the FSA ID
Know the Cost of Borrowing

- Be familiar of how interest accumulates on unsubsidized loans

$10,000 @ 6% interest rate borrowed the first year of college = $599 accrued after first year

Once borrower enters repayment, they will pay daily interest on the interest that is capitalized

Make Payments While in School

Pay the interest while in school

Benefits

- Save money
- Develop good habits

Joanie borrowed a $5,000 unsubsidized loan for a one-year program

With a 3.9% interest rate, $301 accrued after the first year and during the grace period

Total Payment

$6,410

Her monthly payment under the 10-year standard plan is $53

Source: U.S. News and World Report, May 2014
In-school Strategies

If Joanie paid interest while in school

Total Payment

$6,046 + $292 = $6,339

Her monthly payment under the 10-year standard plan is $50/month over 18 months for a total of $292

$71 less than if interest accrued and capitalized

Choose the Right Repayment Plan

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Choose the Right Repayment Plan

• Be aware that:
  – Loan payments are automatically based on the 10-year standard option, unless borrower selects one during the grace period
  – Longer repayment periods means more interest

• Select an IDR plan only if:
  – Cannot afford monthly payment under standard option
  – Owe more than annual salary
  – Working in public service
  – Determine how much interest they will pay with the IDR plan, and if they will be able to receive loan forgiveness
Choose the Right Repayment Plan

### Annual Salary – $44,000
Loan Debt – $28,950

<table>
<thead>
<tr>
<th>Plan</th>
<th>Monthly Payment</th>
<th>Total Interest</th>
<th>Total Paid</th>
<th>Forgiveness</th>
<th>Term</th>
</tr>
</thead>
<tbody>
<tr>
<td>Standard</td>
<td>$292</td>
<td>$6,058</td>
<td>$35,008</td>
<td>$0</td>
<td>120</td>
</tr>
<tr>
<td>Graduated</td>
<td>$163–$489</td>
<td>$7,555</td>
<td>$38,505</td>
<td>$0</td>
<td>120</td>
</tr>
<tr>
<td>IBR</td>
<td>$220</td>
<td>$7,042</td>
<td>$35,992</td>
<td>$0</td>
<td>132</td>
</tr>
<tr>
<td>Pay As You</td>
<td>$220</td>
<td>$7,042</td>
<td>$35,992</td>
<td>$0</td>
<td>132</td>
</tr>
<tr>
<td>Earn/REPAYE</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>ICR</td>
<td>$227</td>
<td>$7,926</td>
<td>$36,876</td>
<td>$0</td>
<td>152</td>
</tr>
</tbody>
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3.9% interest rate unsubsidized loan

Explore Loan Forgiveness

- There are various programs what will forgive all or some of federal loan debt if employed in certain fields or for certain employers
  - Public Service Loan Forgiveness
  - Teacher Loan Forgiveness
  - AmeriCorps and Peace Corps
  - Federal Government Loan Forgiveness Program

Choose the Right Repayment Plan

### Annual Salary – $31,000
Loan Debt – $34,900

<table>
<thead>
<tr>
<th>Plan</th>
<th>Monthly Payment</th>
<th>Total Interest</th>
<th>Total Paid</th>
<th>Forgiveness</th>
<th>Term</th>
</tr>
</thead>
<tbody>
<tr>
<td>Standard</td>
<td>$352</td>
<td>$7,303</td>
<td>$42,203</td>
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<tr>
<td>Graduated</td>
<td>$197–$690</td>
<td>$9,108</td>
<td>$44,008</td>
<td>$0</td>
<td>120</td>
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<tr>
<td>Extended</td>
<td>$182</td>
<td>$19,788</td>
<td>$54,688</td>
<td>$0</td>
<td>300</td>
</tr>
<tr>
<td>IBR</td>
<td>$10</td>
<td>$26,950</td>
<td>$26,950</td>
<td>$35,172</td>
<td>240</td>
</tr>
<tr>
<td>Pay As You</td>
<td>$10</td>
<td>$26,950</td>
<td>$26,950</td>
<td>$35,172</td>
<td>240</td>
</tr>
<tr>
<td>Earn/REPAYE</td>
<td>$182</td>
<td>$12,893</td>
<td>$47,793</td>
<td>$0</td>
<td>192</td>
</tr>
</tbody>
</table>

3.9% interest rate unsubsidized loan
### Pay More

- Pay more than the scheduled monthly payment

<table>
<thead>
<tr>
<th>Loan debt</th>
<th>Monthly payment $282</th>
<th>Additional $100/mo</th>
</tr>
</thead>
<tbody>
<tr>
<td>$28,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>10-year standard payment</td>
<td>2/1/2018</td>
<td>2/1/2018</td>
</tr>
<tr>
<td>Amount paid each month</td>
<td>2/1/2028</td>
<td>2/1/2025</td>
</tr>
<tr>
<td>Total interest paid</td>
<td>$5,858</td>
<td>$4,031</td>
</tr>
</tbody>
</table>

Source: Bankrate.com; 3.9% interest rate

### Out-of-school Strategies

#### Pay More

- Make bi-weekly payments

<table>
<thead>
<tr>
<th>Loan debt</th>
<th>Monthly payment $282</th>
<th>Additional $282/mo</th>
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</thead>
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<tr>
<td>$28,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>10-year standard payment</td>
<td>2/1/2018</td>
<td>2/1/2018</td>
</tr>
<tr>
<td>Bi-weekly payment</td>
<td>2/1/2028</td>
<td>9/1/2022</td>
</tr>
<tr>
<td>Total interest paid</td>
<td>$5,858</td>
<td>$2,584</td>
</tr>
</tbody>
</table>

Source: Bankrate.com; 3.9% interest rate

### Pay More

- Make one extra yearly payment

<table>
<thead>
<tr>
<th>Loan debt</th>
<th>Monthly payment $282</th>
<th>Additional $282/yearly</th>
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</thead>
<tbody>
<tr>
<td>$28,000</td>
<td></td>
<td></td>
</tr>
<tr>
<td>10-year standard payment</td>
<td>2/1/2018</td>
<td>2/1/2018</td>
</tr>
<tr>
<td>One extra yearly payment</td>
<td>2/1/2028</td>
<td>3/1/2027</td>
</tr>
<tr>
<td>Total interest paid</td>
<td>$5,858</td>
<td>$5,346</td>
</tr>
</tbody>
</table>

Source: Bankrate.com; 3.9% interest rate
Pay More

• Make one-time lump sum payment

<table>
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<tbody>
<tr>
<td>10-year standard payment</td>
<td>$282</td>
</tr>
<tr>
<td>One lump sum payment</td>
<td>$2,000</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Monthly payment $282</th>
<th>Lump sum $2,000</th>
</tr>
</thead>
<tbody>
<tr>
<td>Payment start date: 2/1/2018</td>
<td>2/1/2019</td>
</tr>
<tr>
<td>Paid in full date: 5/1/2027</td>
<td>2/1/2028</td>
</tr>
<tr>
<td>Total interest paid</td>
<td>$5,858</td>
</tr>
</tbody>
</table>

Source: Bankrate.com; 3.9% interest rate

Additional Payments

• Additional payments will be applied to:
  – Interest and late payments first (depending on payment plan)

• If there are multiple loans:
  – Highest interest rate loan first – or –
  – Specify how extra funds are to be applied

Additional Payments

• If using automatic payments
  – Scheduled monthly payment will be paid

• If paid by mail
  – Payments are prepaid or paid ahead
Make Automatic Payments

- Make payments through automatic debit
  - Borrowers with Direct loans receive a .25% interest rate reduction
  - Can choose payment date
  - Ensures payments are made on-time

Make Sacrifices

- Create and stick to a budget
- Avoid impulse purchases
- Plan ahead
- Avoid postponing payments with a deferment or forbearance
  - Only request as a last resort

Conclusion

- Less debt = greater success in repayment
- Repay debt quicker = increased opportunities to enjoy life and give back to their alma mater
- Provide borrowers with information and resources so they can become aware of how to shrink the principal
Resources

- Mygreatlakes.org
- Studentloans.gov
- Bankrate.com

Thanks for Attending
Please tell us what you think by completing the online evaluation.