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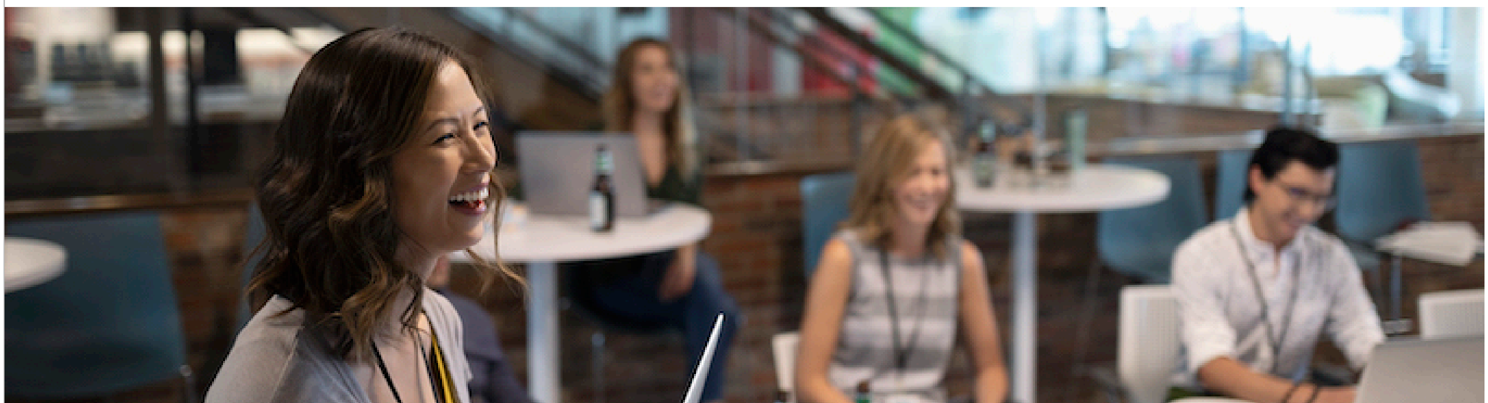
Strategies for student loan debt

How you take on—and pay off—student loans should be part of your financial plan.

Fidelity Viewpoints



Key takeaways

> It's important to understand the financial impact as well as the potential return on student loan debt.
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> Whether to pay extra on your student loans isn't always a simple answer—it should be part of a broader financial plan.

Students and parents admit that loans play a major role in financing higher education. In fact, 60% of high school students say they won't be able to afford college without the help of student loans.[1] It's debt that many people will carry for many years.

The purpose for the loans are to assist in paying for an education that will bring recurring benefits in the future, such as job security, increased wages, and career mobility. An important question to consider is: How do you calculate the return on your investment (ROI) ahead of time? Also, once you have the debt, how does it fit into a smart, overall financial plan?

To understand the long-term implications of student loan debt, it's important to look at the situation holistically, including the benefits and hidden costs. Here are some questions to help do the analysis on the potential financial return on taking out student loans, as well as how they fit into your broader life and financial decisions.

Feedback

Calculating the ROI on taking out loans

1. **Will there be a financial return on your education investment?** The 2023 Fidelity study on student loan awareness revealed that more than one-third (36%) of high school students don't know how long it will take to pay back their student loans.[1] Although it can be hard to project exactly how much you'll make over a lifetime, it's important to estimate what the financial return might be on paying for a degree—specifically, whether the gain in salary is likely to outstrip the cost of the degree, including the monthly student loan payments. For example, let's give a doctoral degree a hypothetical price tag of $150,000 and a master's degree a price tag of $65,000, which is based on the average for graduate tuition at a private college.[2] (This does not include living expenses.) You can ask yourself:
    - Will I be putting myself in a position to be more employable?
    - Is my earning power likely to increase by more than $150,000 or $65,000 (plus any accrued interest) over my working years? How long will it take?
    - How much is my salary likely to increase because of this degree? 1, 5, or 10 years after graduation?

- If I pay for my degree with student loans, will the increase in my salary be enough to cover the student loan payments? For example, if I have a student loan payment of $1,000 per month, then how much more does my salary need to increase to pay that comfortably?
- Will this degree have longevity (particularly knowing that women live longer and often retire at a later age)?
- Will I be likely to work in an industry or at a company that will offer student debt repayment assistance? Will I qualify for federal repayment assistance programs (often available to teachers, health care workers, and nonprofit careers)?

2. **Are there hidden costs to how you pay?** The cost of school generally isn't as simple as tuition plus living expenses. It's important to consider where the money is coming from and the potential lost opportunity costs, particularly if it's for graduate school. For example, many graduate students bypass or leave full-time corporate jobs to take teaching assistant (TA) jobs that include a tuition waiver plus a stipend. This is in hopes it will help reduce the burden of student loan debt. However, many TAs don't consider they are working for their tuition—just earning it through sweat equity. If we use the tuition hypothetical of $30,000/year and a TA stipend hypothetical value of $35,000/year, then a total hypothetical TA "salary" is $65,000, with the student "paying" $30,000 of their salary in tuition. Additionally, as a student employee, there will often be a reduction in the value of benefits (like a 401(k)/403(b) match and health care) or your own retirement contributions. Taking a TA position may likely help you avoid student loan debt and accrued interest. However, if you are in a field that doesn't require the teaching experience or networking, it's important to compare the salary, benefits, career growth of working elsewhere, and paying the tuition yourself or other options.

Tackling student loan debt

You get your diploma and just like that, you're an adult. You're starting a career. You're making plans. You might also be carrying some serious student loan debt. On this episode of Fidelity Investment's Money Unscripted, join host Ally Donnelly as she discovers how to get organized, prioritize payments, and still save for the future you want. View full transcript (PDF)

Calculating the ROI on paying down loans

Let's assume you've graduated and now you're paying the minimum on your student loans, saving for retirement, and have an emergency savings. You notice you have extra money each month. Do you use it to pay off your loans for a quicker pay off, or continue to pay the minimum? How do you weigh your options?

1. **Get organized and informed** The first thing to do is to get organized with all of your student loan information, which you can do through the federal government or through our student debt calculator. Write down all of your loans, the lenders, and the interest rates, and whether they are private or federal. This information will likely vary by semester, year, and school, and it impacts certain factors like your eligibility for repayment plans and federal legislation. Finally, make sure you know and understand the type of payment plan you're on (its terms and length of the repayment) as well as other potential options; these should be available on your lender's website.

2. **Consider the financial return of paying off your loans** Once you know the interest rate on your loan(s), you can compare that to how the money might perform if invested elsewhere. "If your interest rate is low (3%–4%), then you might want to consider investing extra money while you just keep paying the monthly minimum on your student loans—you can give your money the potential to grow beyond the rate of your student loan debt," says Sasha Heathman, CFP®. "However, if you have a higher interest rate (7%–8%) and/or your student loans are private (and therefore have less flexible repayment options), then you might want to consider putting extra money toward your loans." Look at the rest of your financial situation. Do you have other debt with a higher interest rate? Are you getting a tax deduction for your loans? Is your retirement on track? Do you have more pressing financial goals that you want to

save for? Before making a decision, you can use a tool like the student debt calculator or talk to a financial professional. Ultimately, how much to pay off should also be part of a larger financial plan.

3. **Consider your emotions** There is a reason that student loan debt is often called "crushing." It can be stressful, emotional, and feel like it's constantly hanging over your head. If that's something you don't think you can get past, then it might be worth paying it off even if the financial return might not be as high.

How to pay back student debt is a financial and emotional decision, and those are key factors in your strategy for taking out loans and paying them off. What's important is making informed decisions on paying for your education and debt and making sure it fits in with your long-term financial goals.

More to explore

Student debt calculator
See if there is a better way to pay off your student loans.

Women Talk Money live
Strategies for student loan debt

1. 2023 Fidelity College Savings and Student debt study

2. College Board's 2024 Trends in Higher Education Series

Keep in mind that investing involves risk. The value of your investment will fluctuate over time, and you may gain or lose money.

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