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Cut Waste or Invest? Try Both

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Washington

President Obama wants to be sure that the United States keeps making the investments that help the economy grow. Congressional Republicans want the government to stop wasting so much money.

Education — particularly higher education — offers a great opportunity for a compromise that would let both sides claim victory and, even more important, help the economy.

Why? Education is the [single best investment](#) a society can make. High school became universal in the United States in the early 20th century, when other countries viewed universal schooling as wasteful, which goes a long way toward [explaining our economy's](#) 20th-century success. Likewise, the slowing increase in the number of new college graduates in the 1980s and '90s helped contribute to the slow economic growth of the last decade. So protecting higher education from across-the-board budget cuts, as Mr. Obama is urging, makes sense.

But the status quo is not worth protecting. Both the federal government and the states spend money on higher education in terribly wasteful ways. They don't offer incentives for success, and they demand little accountability from colleges. Colleges that do a masterful job of graduating students receive no reward, and those that do a subpar job — [of which there are many](#) — go unpunished, giving them little

reason to improve.

“Colleges are very much like high schools,” as [Arne Duncan](#), the education secretary, says. “Some do a phenomenal job in building college-completion cultures and helping first-generation, low-income and minority students graduate, and some do a horrendous job.” When I asked Mr. Duncan last year whether the Obama administration would consider changing federal financial aid to encourage success, he said, “Yes, stay tuned.”

It has not happened yet, though, which makes it a good opportunity for the White House and Congress to work together now.

The basic problem is that colleges receive government money based largely on how many students they enroll. Perversely, colleges can even help their budgets by having a lot of dropouts. A college with a high dropout rate will have many more freshmen and sophomores than upperclassmen, and freshmen and sophomores are cheaper to have on campus, because they take big lecture classes.

Without any financial incentive to turn students into graduates, most colleges have paid far too little attention to their graduation rates. Nationwide, [only about half](#) of teenagers who enroll in college end up graduating.

The economic consequences have been severe. You often hear that income has stagnated in recent years, but it hasn't stagnated for four-year college graduates. They have received [a 19 percent raise](#) since 1979, on top of inflation. People who went to college without getting a four-year degree — a combination of dropouts and two-year graduates — suffered a 7 percent pay cut.

Fortunately, a few states have started to respond. Most intriguingly, West Virginia's biggest merit scholarship requires students to remain on track to graduate in four years. The policy has lifted the four-year graduation rate of recipients by almost 7 percentage points, according to [research by](#) Judith Scott-Clayton of [Columbia University](#).

Indiana, meanwhile, has [tweaked its formula](#) for financing public colleges, to give more money to those

with higher graduation rates. The formula also takes into account students' economic backgrounds, in an effort to recognize that some colleges have an inherently tougher job turning freshmen into graduates. But even in Indiana, the amount of public money that depends on results is small, less than 10 percent of the total. And virtually no federal funding is tied to results.

In the [federal budget](#), the obvious candidates for cutbacks come from a grab bag of programs that cost about \$12 billion a year and make up about one-fourth of federal spending on colleges. (An additional \$32 billion goes to Pell grants, scholarships for low- and middle-income families, which do appear to lift graduation rates by helping students stay enrolled.)

Most of the \$12 billion subsidizes [student loans](#) so that interest doesn't accrue while students are still in college. That may be a nice little benefit, but it does not help students stay in school. For one thing, it is too complicated to persuade people worried about tuition costs to enroll in college anyway. Even without the subsidy, their loan repayment would not begin until later; the subsidy merely reduces future payments.

The remainder of the \$12 billion is no better. Many of these dollars are matching funds for financial aid awarded by colleges, which means much of the money ends up going to wealthy private colleges. [Sandy Baum](#), a [George Washington University](#) economist who led a recent [financial aid commission](#), calls the allocation of this money "inequitable and inefficient."

It isn't hard to think of more productive ways to use the \$12 billion. Some of it could pay for promising state programs like West Virginia's or Indiana's. Other money could turn into additional aid for Pell recipients who remain on track to graduate in four years. Yet other money could reward colleges that succeed in graduating large numbers of low-income students — an idea the White House is considering, officials say.

The fairest objection to policies focused on graduation rates is that they could cause some colleges to graduate undeserving students. And it's true — they could. But such cases would probably be the rare

exception.

Kevin Carey of Education Sector, a Washington research group, points out that most dropouts today are not students unable to keep up with college work. Instead, they generally attend colleges that, **research shows**, are neither very rigorous nor very engaged in students' lives. Many of these colleges devote little energy to thinking about — let alone improving — their graduation rate. Changing the funding rules could help change that mind-set.

The historical returns to education have been so high that I would rather see Washington both increase higher education spending *and* make it less wasteful. If anything, the federal government's role is more important now, when many states are cutting education spending.

But even if Congress won't increase spending, it can still do a lot to improve spending. The same is true of states, which together spend much more on colleges than Washington. A dollar that's well spent on education today will more than pay for itself tomorrow, through faster economic growth. For that reason, a tougher approach to college funding is actually a form of deficit reduction as well.

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