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FINANCING HIGHER EDUCATION IN LESOTHO: A REVIEW OF STUDENT LOAN PROGRAM IN THE LIGHT OF INTERNATIONAL EXPERIENCE

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REPORT SUBMITTED IN PARTIAL FULFILMENT OF THE MASTER OF ARTS IN EDUCATIONAL PLANNING AND ECONOMICS OF EDUCATION REQUIREMENTS OF THE UNIVERSITY OF LONDON, INSTITUTE OF EDUCATION

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ABSTRACT

Lesotho, like most developing countries is facing increasing pressure for more and better education as a result of population growth and excess demand for places at all levels of education. On the other hand the government is faced with financial constraints compounded by the ever increasing costs of education and training and pressure from other sectors of the economy for more funds.

The source of funds and the way funds are allocated within the education system becomes a cause for concern. In Lesotho there is an imbalance in public expenditure between different levels compounded by private contribution at primary and secondary whilst higher education is almost free. Hence, a prima facie case exists to change and modify the existing system in the interest of equity and efficiency.

The introduction of student loans and fees at higher education could be used to restore balance and improve the existing system in terms of efficiency and equity. The introduction of student loans and fees may also reduce the burden on both public expenditure and on the taxpayer, enabling the system to expand without imposing a greater burden on public funds, at the same time improving access and opportunities, especially to the low income group. The internal efficiency of the education system may also increase as a result of the new system of funding.

The paper will use efficiency and equity arguments to justify the introduction of loans and fees in Lesotho. It will further make use of international experience with student loans programs to see what lessons can be learned. Having considered the evidence the paper presents a student loan model which should satisfy efficiency and equity considerations and increase the flow of funds into education in Lesotho.

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CHAPTER ONE

1.0 INTRODUCTION

Lesotho like most developing countries (LDC'S) is facing an increasing pressure for more and better education. There is mounting pressure due to high population pressure and excess demand for places at all levels of education in Lesotho. There is an annual population growth of 2.6% and estimates predict that the population will double in 25 years.(Education Sector development plan;1992:2) About 40.1% of the population constitutes children under the age of 15 while adults over the age of 60 make up 8.1% of the population and women of child-bearing age (14-49 years old) make up 45.6% of female population. This age structure shows that there is a high dependency ratio which would have significant effect on ability, availability and resource allocation in the economy.

This is compounded by the fact that for primary education the coverage is still not satisfactory, the 1991 estimates give a gross enrolment ratio of 114.4% and a net ratio of 75.2% the latter indicating that only three quarters of the required primary school age population was enroled whilst the former may lead to a conclusion that the country has attained universal primary education but this ratio is misleading because it covers over and under age students an effect of late entry and repetition rates.(Fifth Five-Year Development Plan;1992:11) Whereas higher education can only absorb 38% of applicants due to insufficient places.(University Annual Report;1991:11) As a result greater supply of finance is required to produce more and improve quality.

The government's main priority in an attempt to foster development in view of the limitation on natural resources endowments[1] has been given to manpower development as the key to attain economic growth hence sustain development. In order to achieve this challenging objective the government has to provide basic education opportunities for all and to every citizen of the country.

Despite the pressing obligation the government is faced with a tight budget constraint due to ever increasing share of education budget to total public expenditure. The education budget shows an increasing trend of 18.1% to 25.3% from 1982/83 to 1991/92. In terms of the efficiency criteria, the level attained may not be regarded as the optimum or maxima achievable, although it is evident that education has been accorded the largest share and public budget may not increase any further.

This is compounded by increasing pressure from other sectors of the growing economy for an equal or even larger share of the budget. Since resources are limited some opportunities need to be sacrificed when decisions are finally made, and justification for an investment must be that it will make the greatest possible contribution to society's objective.(Psacharopolous and Woodhall;1991:128)

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[1]Lesotho has water and labour as its significant natural resources.

The source of financing education in this context becomes an important issue. In Lesotho the government finances 42% of total expenditure while the private (parents and society) finance 33% the rest being financed by the foreign community. In addition 320 000 primary pupils share 40% of the education budget whereas another 20% is spent to educate just over 1 000 university[2] students.

The high private contribution to total public budget is made up of financial cost borne by parents and society for both primary and secondary levels excluding higher education. This contribution is in the form of tuition fees, examination fees, boarding and textbooks. On the contrary university education is 'free' since government finances tuition, student accommodation, food, books and pocket money through public subsidy in the form of loans.

The existing system of financing education in Lesotho is on both equity and efficiency grounds, a cause for concern for the government, hence the need to change, and financing of education systems prevailing in many countries has been challenged on the same ground. Generally public subsidies are positively related to the level of education, that is they tend to be greater the higher the education level and by contrast inversely related to enrolment numbers.(TABLE 1.1)

The university student population is 0.60% of total student population whilst per pupil expenditure is 70-75 times more at university than at primary level. Moreover the education pyramid continues to be narrow at the top and very broad at the bottom

[2] There is one university in the country, the National University of Lesotho (N.U.L.)

indicating that majority of children do not proceed to the higher levels.(Appendix 1) Equity is aggravated when more is given to those who are already in a privileged position, moreover there are high rates of return (private and social) at primary than at higher education in most developing countries. (Psacharopoulos;1985:586)(refer to Appendix 2.)

TABLE 1.1

MOE Sectoral Allocations and Recurrent Cost Per Pupil, 1991/92*

Sector	Expenditure	Percentage	No. of Pupils	Per Pupil Expenditure
Primary	75,022,748	52.0	361,144	208
Secondary	42,908,391	30.0	46,572	921
University	21,260,080	15.0	1,415	15,024
NTTC	3,733,590	2.4	630	5,926
LP	2,388,990	0.6	680	3,513

* EXCLUDES PARENTAL CONTRIBUTIONS.

Note: NTTC: National training teacher college, LP: Lerotholi Polytechnic, MOE: Ministry of Education.

Cost per pupil is expressed in local currency Maloti which is at Par with the South African Rand.

Source: Education Sector development Plan;1992:36&37

There may be need to improve efficiency and equity by implementing a cost recovery policy through student loan system and fees and reduce the level of public subsidy. It is assumed cost recovery as a measure may lead to cuts in public expenditure, allow higher education to expand without more public funds, release extra funds to be used at lower levels, improve both internal and external efficiency and the relevance and quality of higher education and narrow the gap between costs and benefits of higher education.

If the equity principle is accepted: He or She who benefits must pay, students who benefit from higher education should at least apportion a share of their future incomes because of the evidence that students subsequently benefit financially from their increased higher education. The idea of student loans is not new in Lesotho but the problem is with the management and administration of the loan system hence the focus of the study.

THE AIMS OF THE REPORT

The study will use an economic framework to analyse the present system of financing higher education in Lesotho. The need to change, modify or improve the existing financial arrangements in higher education stems from the government financial constraints and on equity and efficiency criteria.

The report will make use of international experience with a discussion of its strength and weaknesses to examine the possibilities for introducing a cost recovery policy for financing higher education in Lesotho. Such a policy would imply reducing public

subsidy to students and increasing the private cost of education.

To establish the necessary conceptual background chapter two will introduce the concepts of equity and efficiency in financing higher education. In chapter three there will be a critical review of international experience (both in developed and developing countries) with student loans and emphasis will be on administration and cost recovery mechanism. It is worthless to participate in a big scheme that involve both public and private funds without beneficial results. Finally chapter four will suggest a possible model for Lesotho. The writer is aware that no 'ideal model' exists anywhere in the world for the simple reason that the choice between alternatives depends on the conditions in a particular country. However it is suggested that more focus should be on practical choices, objectives and priorities in the country. This may prove useful in designing and managing a workable student loan program. (Woodhall;1987:2)

CHAPTER TWO

2.0 HIGHER EDUCATION FINANCE: AN ECONOMIC ANALYSIS OF CONCEPTUAL ISSUES ON EFFICIENCY AND EQUITY AND THEIR APPLICATIONS.

2.1 INTRODUCTION:

Higher education is a major tool by which governments/policy-makers attempt to achieve their economic, political, social, or educational objectives. Justification for government intervention is based on equity and efficiency.

This chapter will discuss the concepts of efficiency and equity when applied to higher education and the reasons for government intervention. This discussion will lead directly into the consideration of some alternative method of financing higher education that have been proposed i.e. student loans. This analysis provides the necessary background to justify reduction of public subsidies and introduction of student loans in higher education in Lesotho.

2.2 EFFICIENCY AND EQUITY: CONCEPTS AND THEIR APPLICATION

EFFICIENCY:

Efficiency has become the major concern in financing higher education because in education, as elsewhere in the economy, resources are limited therefore it is desirable

that they should be used in such a way as to maximise the educational output(s) possible from their use.(Mace;1992:4).

Efficiency is defined as either achieving the greatest amount of output from a given set of inputs or achieving a specified amount of output utilizing minimum quantity of inputs. (Windham;1986:17) Efficiency is concerned with the relationship between inputs and outputs of a process. In education this relationship can be analyzed from several perspectives therefore efficiency can be defined in several ways. The different meanings relate to internal and external efficiency.

INTERNAL EFFICIENCY

Internal efficiency is related to the inner workings of the system, referring to the relationship between a system's output learning achievements and the corresponding input that went into creating them.(Coombs and Hallak; 1987:9).

EXTERNAL EFFICIENCY

The external efficiency refers to the relationship between education and the economy outside of education and it may be judged by two criteria: The extent to which the education system provides the necessary skills for the smooth running of the economy, and extent to which school leavers or graduates are absorbed into the labour market, and the balance between the costs of investments in education and the economic benefits as measured by the higher productivity of educated workers that is, by the social rate of return. (Mace;1992:4)

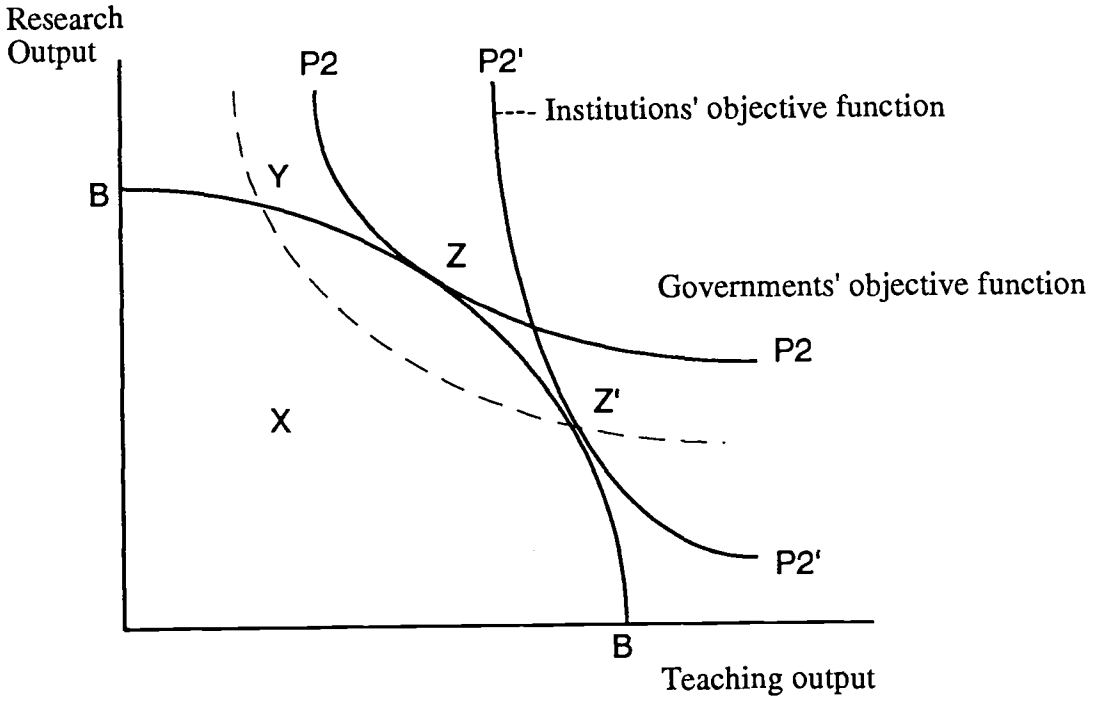
TECHNICAL AND ECONOMIC EFFICIENCY

There are two aspects of production efficiency:**Technical and Economic efficiency.** Technical efficiency is achieved when inputs in educational processes are combined in a way to **maximise output** at a given level of technology. Economic efficiency is achieved when a desired level of output is attained at **least cost.** Technical efficiency deals with physical terms whilst economic efficiency with cost. Planners strive to achieve production efficiency because educational resources are scarce and costly.

Education being a multi- product industry is concerned with a number of outputs or to satisfy more than one demand. Where a range of output combinations is possible to ensure efficiency in production it is necessary to maximise the production of this desired combination at least cost. When this is achieved it is called allocative efficiency.(Mace;1990:3)

If the concern is to satisfy society's objective we have a special case of allocative called exchange efficiency which refers to the efficiency with which appropriate educational outcomes are matched with society's demand. Exchange efficiency implies production but the converse does not hold. It also depends on whose preference is given priority between governments and institutions thus we can achieve production efficiency at two different exchange efficiencies. With the help of a diagram that can be illustrated.

DIAGRAM 2.1



Source: Mace, 1993: 9

Assuming that institutions produce two educational outputs research and teaching, curve BB represents the production possibility curve for research and teaching. A move from X to Y achieves an increase in production efficiency and a move from Y to Z achieves allocative efficiency. P_2P_2 and P^1_2 P^1_2 represents different social indifference curves or objective functions (optimum combination of research and teaching). P_2P_2 and P^1_2 P^1_2 both depict the government and institution objective functions respectively.

Both Z and Z^1 illustrate production efficiency, but Z and Z^1 represents exchange efficiency according to the government's preference and institution's preference respectively. Thus, exchange efficiency depends on whose preference is given priority

between governments and institutions and economic efficiency in education depends just as much on whose educational objective we are maximising as on the technical relationship in education between inputs and outputs.

EQUITY

Equity is concerned with the distribution of resources or opportunities and refers to equal access to educational opportunity and income distribution. The concept of equity is subjective,normative and value laden, a consequence of judgement. Economist use three different concepts of equity:**HORIZONTAL EQUITY**, referring to equal treatment of equals;**VERTICAL EQUITY,** referring to unequal treatment of unequals; and **INTERGENERATIONAL EQUITY** which lies between the other types and concerned with ensuring that inequalities in one generation are not perpetuated. (Psacharopolous et.al;1991:252, Macmahon;1982:18).

2.3 THE RATIONALE FOR GOVERNMENT INTERVENTION IN THE FINANCING OF HIGHER EDUCATION.

If it is accepted that higher education benefits society as a whole, it may be efficient for the government to finance higher education or bear part of the costs. On the other hand a degree may also confer private benefits to students at higher education (higher pay, greater job satisfaction) therefore it may be both efficient and equitable for students to pay part of the costs themselves. (Barr and Barnes;1988:25) This section will examine the rationale for government intervention.

In many countries, including Lesotho, governments subsidise higher education on the basis of equity and efficiency arguments which have its roots in welfare economics. (Blaug;1970:102). According to economists (James;1988, Geske & Cohn;1990, Jiminez;1985, Psacharopoulos et. al;1991) justification for government subsidy has to do with externalities that is to say, since marginal social benefits exceed marginal private benefits governments need to subsidize education to prevent underinvestment or sub-optimal investment.

Secondly, it is believed economies of scale exist in higher education and that it is efficient to finance and provide education publicly. (Cohn;1979:263, Verry and Davies;1976:112,) Although there is evidence of economies of scale differences in unit costs of education do not seem to be clearly related to its financial sources. (Psacharopoulos et.al;1991:138)

Thirdly, proponents of public subsidy argue that there is consumer ignorance. Although it may exist in primary education, it seems improbable for the age group about to undertake higher education to fail to make an assessment of probable benefits. There is evidence in Pakistan, U.K. and U.S.A. that 16-18 year olds are well informed about the effect of schooling on labour market. (Mace;1990:24)

Lastly, due to capital and insurance market failure, only those who could afford to pay tuition fees could enrol. In addition it may not be possible to launch a student loan scheme on a scale large enough to pool risks and reduce the borrowing and premium risk hence the need for government subsidy to higher education in order to improve

equity and equality of opportunity.

The four arguments above support government subsidies on grounds of both efficiency and equity, but do not suggest whether all or even most of the costs of education must be publicly financed. What is at issue is not whether education should be subsidized, but to what extent. (Psacharopoulos; et.al;1991:138). In Lesotho this question becomes more relevant where all other levels except higher education are not subsidised instead the society pay heavy fees.

In addition to efficiency there are social,political and equity arguments all of which involve value judgements. This include how higher education institutions should be funded and how students in higher education are and should be financed. The two issues will be considered hereunder:

2.4 INSTITUTIONAL FUNDING

> **"The way in which higher education is financed affects the scale and type of provision, the composition of the student body, the style of governance of educational institutions,the range, level and type of curricula offered and, to some extent, the quality of teaching and research".(Mace;1990:31).**

In other words whatever educational objectives decision makers are pursuing ,the way institutions are funded will have implications for their attainment and on the efficiency with which objectives will be achieved. Let us examine the different ways of financing higher education.

There are three different models namely: "bureaucratic", "collegial",and the "market model".(Clark 1982). Under the bureaucratic model, financial decisions are taken at the highest political level usually the central authority, which decides both the resources available to the higher education sector and the rules according to which these resources are distributed between institution and within institutions. This model currently prevails for higher education in Lesotho.

The collegial model contrasts sharply with the bureaucratic model in that institutions are financially independent perhaps from past endowments, and are free to manage their own affairs at own will. In this model decision making is dependent on consensus.

Under the market model power is diffuse and indirect, generally the consumers (students) exercise more discretion on availability of funds for the institutions. The university's income is generated by selling its services (teaching, research and consultancy) to whoever wishes to buy. In this model power is shifted to consumer and to the units that produce and sell the services. This model will be relevant to higher education in Lesotho because about 33% of total expenditure is financed through fees by parents for primary and secondary education (as indicated in chapter one,) therefore the system in existence is akin to the market model.

In analyzing the implication of any method of financing higher education we need to ask whether it is consistent with the achievement of both production and exchange efficiency.(Blaug et.al;1983:17). This may depend on the measure of control on the

funds exercised by the governments. Implications may arise by allowing virement (that is institution are able to divert funds from one activity to the other) when awarding grants to institutions and awarding moneys to institutions in the form of fee income.

If under the collegial model institutions are allowed to exercise virement when awarded grants, there may be implications for both production and exchange efficiency. The university staff may not be prepared to maximise educational output at least cost. They may not be well informed about the costs and benefits of their decisions and there might not be a consensus among staff as to the nature and importance of these costs and benefits.

Exchange efficiency may not be achieved. Institutions may not be concerned with matching educational outputs with society's demand or government's objective when free to vary spending and change outputs (teaching,research,consultancy) in accordance with their individual interests. The quinquennial system of funding university education was abandoned in the mid 1970's in Britain owing to this tendency. That is how Adam Smith saw the universities of Oxford and Cambridge in the eighteenth century. (Mace;1986:15).

In the absence of virement, the bureaucratic system may result in a top-heavy, cumbersome, slow and inflexible system which may not make it possible to achieve either production or exchange efficiency; even though educational financing may be arranged in accordance with society's demands.

Blaug and Mace (1983) write that:

"Perhaps the answer to this dilemma lies in taking the decision-making out of the hands of both university staff and the government bureaucracy and putting it in the hands of the consumer. In other words, there may be a case for a 'market model' (my emphasis) p.23

The market model brings in the issue of fees. In this case universities are compelled to act like businesses in attracting customers. The likely result, unless there is a shortage of university places is that competition will develop between universities with the aim to attract as many customers as possible. It is very unlikely in such a situation that the amount of research will fall. Whether the amount and quality of teaching rises concomitantly is debatable.

On the other hand such a fee policy may encourage universities to become more responsive to student's needs and improve their quality of output, that is move towards their production frontiers and thus towards greater production efficiency, at least with respect to teaching.

There might be a move towards greater or less exchange efficiency. This is because the behaviour of individual student which will determine educational output may not coincide with the educational output that is thought to be most appropriate by the state for the society.

From the foregoing analysis, it may be possible to combine the market-type with central funding. The advantages of the 'hybrid model' will be to reduce the possible

undesirable effect of student power thus moving towards exchange efficiency perhaps by rewarding teachers and institutions via special pay increments, promotions and so on. In addition uncertainties of finance for higher education may be minimised by ensuring at least a consistent flow of funds. Lastly governments may be able to ensure that activities of higher education are consistent with both production and exchange efficiency and thus achieve economic efficiency.

This model may be desirable to Lesotho, the effect of consumer power might not be harmful as everyone (the society) seeks a place, instead the university may be encouraged to achieve production efficiency and at the same time be compelled to improve their quality of output. It would be desirable for the National university of Lesotho (NUL) being a small growing university to secure consistent funds.

According to economists the "market model" is akin to a student loan system thus it is relevant and applicable. Mace (1987:17) writes that the bureaucratic and collegial model of financing tuition expenses works smoothly with a student grants, whereas a market model of tuition funding combines more easily with a system of loans system. Thus a brief discussion of student loans model of funding is worth examining.

2.5 STUDENT LOANS IN HIGHER EDUCATION

The issue of student loans is one of the most widely debated in the field of educational finance about the future of higher education. There are two forms of arguments in this debates: Firstly arguments for or against loans in principle; and secondly proposals for or against changes in existing level or type of subsidy. The latter case is more

relevant to Lesotho where it is argued for a reduction in the level of subsidy with introduction of loans and fees. Both opponents and advocates base their arguments on efficiency and equity criteria to support their cases. Economic analysis may help clarify the arguments and help planners to reach a decision about the merit and demerit of student loans.

EFFICIENCY ARGUMENTS

According to proponents, student loans scheme if properly designed and managed are a potential source of education finance which may reduce the burden on government expenditure. This argument is related to the costs of administering the loan scheme.

If administering costs are exorbitant as compared to the benefits, the introduction of loans cannot be justified on the grounds that it reduces public spending. A situation prevailing in Lesotho as will be shown later. This argument is based on one of the canons of taxation developed by Adam Smith which states that no government should introduce a tax whose collection will cost more than the revenue it raises.

Opponents of loans are also sceptical about its feasibility because of high defaulting in repayment and inadequacies in the banking system in many developing countries. Proponents acknowledge existence of many practical problems that may hinder a smooth administration of loans, but they are optimistic that a solution to minimise the problems should be provided rather than abandoning the loan system.

In most developing countries like Lesotho it may be possible to minimise the default

since majority of graduates work in the formal sector and loan repayment could be arranged through the treasury utilising the existing tax system. Although the success rate of this method relies on good record keeping, one deficiency prevalent in developing countries. There is a pressing need for Lesotho to improve its administrative capacity, according to a three day forum held in Kenya, Lesotho raised high rate of default as one major problem in the administration of loans.(Woodhall;1991:59)

Critics of loans argue that international migration of graduates may render the loan repayments a formidable task, this is a major problem to Lesotho where there is high brain drain to South Africa for better paying jobs and prospects. Proponents argue that it might be possible to minimise the problem by tightening international migration procedures or alternatively make recipient of loans pay the cost of their education before migration either by working in their own country for a significant period or by payment of a lump sum. Personally I believe this problem may be minimised if respective governments take appropriate initiative to secure and allocate jobs efficiently to graduates within reasonable time after graduation.

It is argued that reducing public subsidies and charging fees or introducing loans would give students a higher incentive to choose responsibly among alternative education options. The students would be inclined to opt for quality, relevance and efficiency in production of their education since they will be paying for their education. This argument is relevant to Lesotho to improve internal efficiency by reducing repetition rate and drop out an existing problem currently especially at early stages of

courses.

The argument goes further that universities may be able to expand and improve without imposing an extra burden on public expenditure. For Lesotho expansion is inevitable due to growing student numbers and unmet social demand at higher education but at the same time there is need to expand and improve lower levels hence the need to mobilise funds from within the university by introducing loans and fees. Opponents argue that reduction in subsidies and introduction of loans may result in lower enrolments since students from modest low income groups would be debarred from enroling in higher education.

Psacharopoulos and Mingat (1985) write that:

"Some reduction in enrolments could be expected though it is known that aggregate demand is not very sensitive to increases in the cost of studies, especially when the private rate of return is already high." p14.

This argument is more relevant in Lesotho and other developing countries where there is excess demand and high private rate of return in higher education (refer to Appendix 2). Advocates argue that there could be more improvement in internal efficiency of higher education i.e. minimise wastage by maximising retention rate and minimising drop out rate since students of low academic ability are less likely to enrol.

In terms of external efficiency it is suggested that increasing the cost of studies would encourage students to pay more attention to labour market signals and make them

behave more like investors rather than consumers thus improve the linkage between education and the labour market.(Psacharopoulos et. al;1986:20)

As I indicated in the previous section a loan scheme would compel universities to respond to the student's choice and this would lead to exchange efficiency in terms of output they produce[3] and production efficiency in so far as they would attempt to minimise their cost per student in order to attract more.

Opponents argue that there would be an insignificant saving of public funds. They contend that high cost of administration, large default and the need to provide guarantees for those unable to repay their loans due to unemployment may counter balance all potential savings. It is argued that financial problems arising from repayments of loans may result in high wastage alternatively a grant system would encourage the students to spend their time efficiently because less time can be spent pondering over financial problems.

EQUITY ARGUMENTS

Proponents of loans systems base their arguments on the equity principle: He or she who benefits for higher education must pay. They argue that since people with higher education generally enter higher income and higher status jobs than others, why should the average low-income taxpayer pay for the advantages education bestows

[3] Exchange efficiency may be achieved only if consumers have the same objectives as the "society".

on graduates? To do so is to violate both horizontal and vertical equity hence it is reasonable to request them pay part of the cost of their education from their future higher earnings.

Opponents argue that the reasoning is over simplistic, in the first place it ignores the fact that higher education gives rise to social benefits enjoyed by the community at large rather than being an exclusive benefit to the individual. Secondly higher earnings of graduates it is argued may stem from other factors rather than education, for example as a result of their innate ability. If this is true it would be a mistake to ascribe the higher earnings of graduates to their education.

On the other hand it is argued that whether or not graduates earn more than non graduates because of their higher education the fact remains that they enjoy the consumption benefits of three or four years of education at the expense of the general taxpayer. They maintain that if we accept the principle of he or she who benefits must pay, there is a strong case for shifting at least part of the costs to the student. A student loan scheme is a simple device for bringing this about. (Blaug et. al;1983:33)

In Lesotho this argument is relevant because about 0.6% of student population benefit at the expense of unmet social demand. Secondly it is only at university level where there is no private contribution, in addition the opportunity cost for students is lower than at lower levels lastly in Lesotho qualifications have more bearing than experience for promotions and securing better paying jobs.

2.6 CONCLUSION

After an exploration of efficiency and equity from the foregoing analysis there appears to be a case for loans. Moreover economists who believe in the concept of competition in promoting economic efficiency, could link the 'market' model with the introduction of loans and fees and a reduction in public subsidy so that universities could compete to reduce costs, improve quality and relevance, attract students, move towards their production frontiers and attempt to achieve exchange efficiency thus seek more efficient use of resources. The next chapter will explore and examine international experience with student loan programs.

CHAPTER THREE

3.0 INTERNATIONAL EXPERIENCE WITH STUDENT LOANS: EFFICIENCY AND EQUITY CONSIDERATIONS IN THE ADMINISTRATION AND MANAGEMENT OF LOANS.

3.1 INTRODUCTION

Generally higher education is heavily subsidised to cover both living and tuition costs in the form of grants, scholarships, bursaries, low or non existent tuition fees, low or no interest and low cost board and lodging. The heavy subsidization and the reasons for the subsidy vary from country to country. In developing countries there are historical reasons in addition to economic and social justification for government involvement. The provision of scholarships and tuition -free higher education in the 60's and 70's was seen as a leeway to an increase in the supply of graduates to replace expatriates. The argument for shortage of qualified nationals is much weaker today than it was one or two decades ago. (Mingat, Tan, Hoque;1985:6).

The poor macroeconomic conditions prevailing since late 80's has led to changes in the pattern of government subsidization. Economist advocate for increased private contribution through introduction of student loans and fees. Students could pay for their education at the time of enrolment. But this arrangement may limit access to those able to pay at the time of enrolment at the expense of qualified students from poor families hence inefficient and inequitable. An alternative arrangement is a student loan system, by which students could defer payments for the costs of attending higher

education until they are earning incomes.

The application of this policy is focused on higher education on both efficiency and equity grounds as discussed in the previous chapter. Extensive literature has been optimistic about the efficiency and equity of student loans (Woodhall;1983,1987, 1990, Johnstone;1987, Mingat, Tan and Hoque;1985, Psacharopoulos et.al;1985). Fewer studies have actually examined student loans' financial impact on government and student budgets particularly in developing countries. In this respect the implementation and management of loans is a major problem that contributes to the sluggish performance in these countries hence my focus on Lesotho.

This chapter will discuss types and coverage of student loans, eligibility,loan recovery ratio, loan in relation to university costs and default and evasion with existing loans scheme internationally with a view to present a possible model for Lesotho with student loan scheme. In most developing countries including Lesotho loan programs to date have been more expensive than continuing with a policy of outright grants.

The first part will review the existing student loan schemes in both developed and developing countries. The second part will draw lessons for Lesotho from international experience with student loans.

3.2 EQUITY CONSIDERATIONS

METHODS OF REPAYMENT

The method of repayment may have both efficiency and equity implications. Currently loan programs exist in over fifty developing and developed countries most commonly introduced to assist student to pay their living expenses and in fewer cases to support direct payment of instructional costs. (Albrecht and Ziderman;1991:3) Table 3.1 provides a summary information on these programs.

With most existing loan scheme there are basically two methods: the first is the **"mortgage loan"** by which interest rates and the maximum length of repayment are used to calculate fixed periodic payments usually on monthly basis.(the minimum may be three or four years like in Hong kong to twenty years maximum like in Sweden) With fixed payments the burden is greater in the early years of employment when income is low and declines as annual income rises. This method may have distributional effects thus inequitable, since payments are fixed graduates earning higher incomes will be favoured at the expense of low earners. In contrast to equal nominal payments graduates pay equal real amounts in most universities in Chile.

With the second type the **income contingent loan**, repayments are made as a proportion of a graduate's income each year.The repayment is expected to be more favourable to low income students. Mace;(1986:27) shows that under a fixed repayment scheme, it is also probable that potential students with low- income

TABLE 3.1

Existing Student Loan Programs

Country (Loan Organization)	Repayment Mechanism	Administering Institution	Purpose of Support	Average Loan Value	Year Begun	Percent of students with loans	Data year
LATIN AMERICA AND CARIBBEAN							
Argentina (INCE)	Mortgage Loan	Autonomous Body	Living				
Barbados (SRLF)	Mortgage Loan	Autonomous Body	Tuition and Living	$11,000	1976	12%	1989
Bolivia (CIDEP)	Mortgage Loan		Living				
Brazil (CEP)	Mortgage Loan	Commercial Banks	Tuition	$400	1974	25%	1989
Chile	Graduated	Universities	Tuition		1981		1988
Colombia (ICETEX)	Mortgage Loan	Autonomous Body	Tuition and Living	$280	1953	6%	1985
Costa Rica (CONAPE)	Mortgage Loan	Commercial Banks	Tuition and Living		1977		1983
Dominican Republic (FCE)	Mortgage Loan	Autonomous Body	Living				
Ecuador (IECE)	Mortgage Loan	Autonomous Body	Living			3%	
El Salvador (Educredito)	Mortgage Loan	Autonomous Body					
Honduras (Educredito)	Mortgage Loan	Autonomous Body	Tuition and Living	$2,700	1976	1%	1991
Jamaica (SLB)	Mortgage Loan	Autonomous Body	Tuition and Living	$405	1970	20%	1985
Mexico	Mortgage Loan	Commercial Banks					
Nicaragua (Educredito)	Mortgage Loan	Autonomous Body					
Panama (IFARHU)	Mortgage Loan	Autonomous Body			1966	6%	
Peru (INABEC)	Mortgage Loan	Autonomous Body					
Trinidad (SRLF)	Mortgage Loan	Autonomous Body	Tuition and Living		1972		
Venezuela (Educredito)	Mortgage Loan	Other	Tuition and Living	$400	1967	1%	1991
(FGMA)	Mortgage Loan	Universities	Tuition and Living	$2,200	1975	1%	1991
(BANAP)	Mortgage Loan	Commercial Banks	Tuition and Living	$700		1%	1991
ASIA							
China	Mortgage Loan	Universities	Tuition and Living		1987	30%	1989
India	Mortgage Loan	Other	Tuition and Living	$85	1963	1%	1989
Indonesia *	Mortgage Loan	Universities and Commercial Banks	Tuition and Living	$550	1982	3%	1986
Korea	Mortgage Loan	Commercial Banks	Tuition and Living		1975		
Malaysia	Mortgage Loan	Commercial Banks	Living	$1,300	1985		
Philippines	Mortgage Loan		Tuition		1976	1%	
Pakistan	Mortgage Loan	Commercial Banks	Tuition and Living		1974		
Sri Lanka	Mortgage Loan	Commercial Banks			1964		
MIDDLE EAST, NORTH AFRICA							
Egypt	Mortgage Loan	Autonomous Body				5%	1980
		Commercial Banks				2%	1980
Israel*	Mortgage Loan	Commercial Banks	Tuition and Living			12%	1983
Jordan	Mortgage Loan						
Morocco	Mortgage Loan	Commercial Banks	Tuition			<1%	1990
SUB-SAHARAN AFRICA							
Ghana	Income Contingent	Government Dept.	Living	$200	1989	68%	1990
Kenya	Mortgage Loan	Commercial Bank	Living	$845	1973	100%	1990
Nigeria*	Mortgage Loan	Autonomous Body	Tuition				
Rwanda							
Burundi*							
Malawi	Mortgage Loan		Living	$80	1988	50%	1989
Tanzania*	Mortgage Loan		Living				
INDUSTRIAL COUNTRIES							
Australia	Income Contingent	Government Dept.	Tuition	$1,750	1989	81%	1990
Canada (Quebec)	Mortgage Loan	Commercial Banks	Tuition and Living	$2,800	1963	59%	1990
Denmark	Mortgage Loan	Commercial Banks	Living	$3,700	1975		1985
Finland	Mortgage Loan		Living	$2,200	1986		1987
France	Mortgage Loan	Government Dept.	Living			1%	
Germany	Mortgage Loan		Living	$1,500	1974	30%	1987
Hong Kong	Mortgage Loan	Government Dept.	Tuition and Living	$1,050	1969	26%	1989
Netherlands	Mortgage Loan		Living	$200			1989
Norway	Mortgage Loan	Autonomous Body	Living	$4,000		80%	1986
Japan	Mortgage Loan	Autonomous Body	Tuition and Living	$2,500		19%	1987
Singapore	Mortgage Loan	Government Dept. Commercial Banks	Tuition and Living			39%	1990
Sweden	Income Contingent	Autonomous Body	Living	$5,828			
United Kingdom	Mortgage Loan	Autonomous Body	Living	$750	1990	7%	1990
USA	Mortgage Loan	Commercial Banks	Tuition and Living	$2,176	1964	28%	1987

Banks imply information was not available.
Programs in Indonesia, Israel, Nigeria, Tanzania and Burundi have been abandoned.

SOURCE: Ibid;1991:5

expectations or strong positive time preferences will be discouraged from entering universities. Borrowing may be risky and greatest for the poor because their future job and earnings opportunities are less favourable and the future value of the degree is not immediately apparent. Consequently, the poor tend to be more risk averse than the well to do. (Barr;1991:160, Reuterberg and Svennson;1990:34). Mortgage loans may deter access among the very groups that loans are intended to serve.

Income contingent loans constitute a mechanism for achieving a balance between effective recovery costs and minimum risk to the borrower. Therefore economists conclude that on equity and efficiency grounds, an income related scheme is preferred to a fixed repayment scheme. As indicated in TABLE 3.1, there are only three income contingent loans programs in Sweden, Australia and Ghana. In Sweden students are required to pay 4% of their yearly income to the loan fund until their debt is repaid. The schemes in Ghana and Australia, use social security contributions and income taxation for loan repayment respectively.

Finally there is a graduate tax type that has not yet been implemented anywhere. The rational behind graduate tax is that by subsidizing higher education the government assumes a share in financing creation of human capital, this produces a future stream of benefits in the form of increased earnings of the graduates. By the same analogy the government appropriates an equity share in the human capital created thus is entitled to a dividend from the ensuing income benefits. This dividend can take form of a percentage tax on graduate's income over their working lives. Percentage tax rates vary with income level while graduates from low income may be exempted from

the tax. Most economists advocate for this equity finance approach first suggested by Milton Friedman.(Friedman;1962:103,Blaug;1970:303,Barnes and Barr;1988:30)

ELIGIBILITY

It is essential to decide whether a student loan program should be available to all those who wish to borrow or be selective and based on need or ability. Those concerned with efficiency criterion will favour loan recipients chosen on academic ability as they are likely to succeed and repay their loans whereas the equity criterion will take into account the financial needs of borrowers. This is important to consider because there is a link between eligibility for loans and the cost to government. If the loans are subsidized, open access can be expensive to governments. The primary advantage of open access to loan support is that no one will be missed, but the disadvantage is that usually fewer funds are available to needier students and limited available support may benefit those who can afford to pay.

A selective loan system may be preferred on grounds of cost effectiveness, although the choice between alternative eligibility does involve a conflict between efficiency and equity objectives. Without effective targeting, less than full loan recovery and growing students numbers may result in increasing, unsustainable pressures on limited loan funds. Given that loans funds are subsidized and most probably may continue to be so, targeting may limit the extent of loan subsidization and reduce the burden on public expenditure. As indicated by table 3.1, in many countries there is a relatively low percentage of students receiving loans therefore the need for targeting becomes more eminent in terms of efficiency and equity.

It is a common shared view that an effective and acceptable targeting criteria (especially under increasing pressure on public funds) should be dependent on financial need and to ability. (Woodhall;1987:40,Albrecht et.al.1990:24) The following criteria are used:

Means testing:

Access to loans under means testing is limited to those students whose family or personal income falls below a threshold value. Means test can take a variety of forms: In the U.S.A. a strict means test is now applied since 1982 to determine eligibility for subsidized loans. During 1970's the means test was changed as a result of the Middle Income Student Assistance (MISSA) which made the Guaranteed Student Loan Program (GSLP) available to all students regardless parental income, and resulted in a large increase of borrowers from 1 million to about 3.5 million between 1978 and 1981 with costs increasing from US$670 million to $2,425 within the same period. (Woodhall;1983,1987) Critics of loans argued that there is need for government to control public expenditure and to avoid what Gladieux describes as "the real danger that federal benefits will drift increasingly toward the relatively well off at the expense of the poor and neediest. (Gladieux;1989:2) The American experience illustrates the danger of making a loan program 'open ended' without attempting to make eligibility selective.

In Sweden, Norway and Netherlands parental income is disregarded and students over 19 years are treated as financially independent of their family. Almost all students are

eligible for support. The Swedish experience has indicated that there is no unwillingness to borrow, even by the poorest students, as critics have suggested. (Woodhall;1983:17) It is also believed the criterion has been significant in ensuring access for women. For developing countries it is argued that this requirement has favoured students from wealthier families to benefit more from loan support because students at the age of nineteen (19) are unlikely to have their own source of income.

In developing countries mean testing can be difficult to implement due to lack of accurate data on family income for income tax, where there is a large subsistence sector and where the extended family is important. Experiences in Colombia and Brazil indicate that progress could be better if stronger restrictions on income ceilings were imposed. In Colombia funds were allocated to students whose families fell below an income threshold. But the threshold used was relatively high. In Brazil, need is prioritized by ranking students. The government disburses all the funds it has in a given year according to the ranking and does not try to conserve funds.(Vahl;1990)

Ability criteria:

Access to support may be based on student performance. Ability restrictions have the advantage of rewarding those who are most likely to benefit from higher education and to give students a strong performance incentive. In addition to improve the internal efficiency by avoiding subsidising students who are likely to repeat or drop out. In Indonesia, students were eligible for loans after successfully completing about 75% of their course and proven their academic ability. In Venezuela and Honduras a

student failing to meet expected grades forfeits the loan and is expected to resume payments forthwith. In Colombia, access to loans is determined partially by results on the national secondary school examination. However, the use of ability criteria may result in the selection of wealthier students with access to better educational facilities. Hence involves a conflict between efficiency and equity criteria.

Duration:

The period for which student support is available can affect student flows, and thus efficiency of institutions. In many higher education institutions repetition may be fostered by open ended availability of support, restricting loans to a given length of a course may improve student performance and also save funds. This consideration has been incorporated in program reforms in Australia, Brazil and the Netherlands, where support is limited to official duration of study. This restriction may penalise part time students who are likely to take longer to complete their courses most probably low-income group hence efficiency may be achieved at the expense of equity.

3.4 EFFICIENCY CONSIDERATIONS

PAYMENTS FORMAT

A number of loan programs incorporate incentives for students. This is an attempt by government to improve efficiency by motivating students to complete their studies in minimum time or take up desired professions. Given the large number of variables in a student loan programme it is clear that loans are potentially a very flexible

instrument. (Woodhall;1987:64) A planner has to choose between a wide range of alternatives in providing repayment terms for different categories of students depending on the objectives of the student aid system.

In Germany the government gives 30% off loan forgiveness incentive to students completing their studies in minimum time since many students study part time or break off in the middle of their degree to work; or 20% of student loan converted into a grant for completing their course successfully or achieving high grades in Barbados. In Sweden students from low incomes are given automatic postponement of their loans.

In the U.S.A. loan forgiveness or cancellation has been used to encourage students to enter the student teaching profession. Experience from the first loan established in the late 1950's for the same purpose indicated that incentives had little effect on student career choices. Instead, those who already decided to be teachers were willing to take a larger loan because part of the loan would be cancelled.

Several countries offer bonded scholarships (Botswana,Swaziland) similar to loan forgiveness. Graduates are expected to repay on failing to enter or remain in a particular occupation trained for. Enforcement of this, may be difficult as in repayment of a loan. The advantage of the incentives is that governments may be able to meet manpower shortages. The main disadvantage is that a system of incentives introduced in times of labour shortages may respectively give rise to labour surplus. Secondly students can be disillusioned if after training they are not provided with guaranteed employment. In Egypt the guaranteed employment introduced in 1973 is blamed for

excess demand for higher education and inefficiencies in the labour market.(Woodhall;1987:64)

LOAN RECOVERY RATIO

Loan schemes are meant to enable students to share the financial burdens for tuition and/or maintenance expenses with governments through payments from future earned income. The financial efficacy of any loan scheme may depend on the "loan recovery ratio"- the extent to which the loan is repaid in full. What the government lends out to students and what is returned may be used as an indicator of loan efficiency. An inefficient program will refer to a situation where government continues to bear the cost burden of higher education and/or student maintenance expenses by recovering little compared to what it lends out.

The second indicator of efficiency may be the "cost recovery ratio"- the average loan repayment in relation to unit costs. That is what costs are recovered. Experience has shown that most loan programs may reduce government burden on maintenance expenses and not address the problem of diversifying the resource base of higher education by making students contribute towards tuition fees. Institutional recovery cannot be high unless tuition fees are high and loans are used to support students paying tuition.

Jallade; (1974) points out:"loans cannot be considered as a source of finance for public universities because .....little was done to increase the role of fees". It is stressed that cost recovery impact of loans would be significant only if they are

accompanied by fees.It would be meaningless to discuss their performance outside the context of a fee policy. (Mingat;Tan;Hoque;1985:37)

According to Mingat and Tan;(1986:287) the extent of cost recovery under a loan scheme may be assessed from the ratio of graduate's income to the public spending per student in higher education. TABLE 3.2 illustrates the data for four major world regions. In Asia the relatively high ratio 4.44 may suggest that students could afford to repay their education.In contrast, the ratio in Anglophone is low,1.09 indicating that students may encounter difficulty to repay all the subsidies they receive from government.

TABLE 3.2

Public spending per Public spending per student in higher education and graduates salaries in major regions of the world 1984

Country/Region	Unit cost of higher education (1)	Graduates, salaries (2)	Salary-Cost ratio (3) (2)/(1)
Anglophone Africa	9.2	10.0	1.09
Francophone Africa	8.0	19.4	2.43
Latin America	1.2	3.4	2.83
Asia	0.9	4.0	4.44

Footnote: The data in column (1) and (2) are measured in terms of per capita GNP.

Source: Mingat et. al;1986:287

Economists contend that loan recovery may depend on three major issues: the amount of hidden interest subsidies on loans, repayment losses due to default and administration costs. Table 3.3 gives information on these indicators for twenty different countries.

TABLE 3.3

Hidden Subsidies and Government Losses on Selected Student Loan Programs

Country	Nominal Interest rate	Real Interest rate	Maximum or Projected Repayment Period	Hidden Grant to students per cent of loan	Government loss with default	Government loss with default and administr-	Year	Estimates
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	
MORTGAGE LOANS								
Colombia I	11.0% a	-10.6%	8	73%	76% c	87%	1978	Administrative 2%
Colombia II	24.0%	3.0% b	5	29%	38% c	47%	1985	Administrative 2%
Sweden	4.3%	-3.0%	20	61%	62%	70%	1988	Administrative 1%
Indonesia	6.0%	-2.3% b	10	57%	61%	71%	1985	Default 10%, Adm 2%
USA (GSL)	8.0% a	3.8% b	10	29%	41%	53%	1986	Administrative 2%
Hong Kong	0.0%	-6.3% b	5	43%	43%	47%	1985	Administrative 2%
UK	6.0%	0.0%	7	26%	30%	41%	1989	Default 5%, Adm 1%
Norway	11.5% a	5.6%	20	33%	33%	48%	1986	Administrative 1%
Denmark	8.0% a	1.6%	10	52%	56%	62%	1986	Administrative 1%
Finland	6.5% a	-0.6%	10	45%	46%	52%	1986	Default 2%, Adm 1%
Brazil I	15.0%	-35.0% b	5	91%	94%	98%	1983	Default 30%, Adm 2%
Brazil II	318.0%	-14.9%	8	62%	65%	71%	1989	Default 10%, Adm 2%
Jamaica I	6.0%	-10.7%	9	74%	84% c	92%	1987	Administrative 2%
Jamaica II	12.0%	-5.6%	9	56%	62% c	70%	1988	Default 20%, Adm 2%
Barbados	8.0%	4.1%	12	13%	18%	33%	1988	Default 5%, Adm 2%
Kenya	2.0%	-6.9%	10	70%	94% c	103%	1989	Administrative 2%
Quebec	10.0% a	5.2%	10	31%	31%	37%	1989	Administrative 1%
Chile	varies	1.0% b	10	48%	69% c	82%	1989	Administrative 2%
Japan	0.0%	-1.4%	20	50%	51%	60%	1987	Administrative 1%
Venezuela	4.0%	-23%	20	93%	98%	108%	1991	Administrative 3%
Honduras	12.0%	3%	8	51%	53%	73%	1991	Administrative 5%
INCOME CONTINGENT LOANS								
Australia	varies	0.0%	17	48%	52%	57%	1990	Evasion 3%, adm 0.5%
Sweden	varies	1.0%	10	28%	30%	33%	1990	Evasion 3%, adm 0.5%

General notes:

All subsidy calculations use a real opportunity cost of capital according to the government rate of borrowing or estimates used by the World Bank. Loans are assumed to be paid in equal installments over a four year period, adjusted in size each year to keep up with inflation. Given the availability of relevant data, Swedish income contingent calculation is based on Australia's age earning profile information;

(1) Countries with I and II refer to situations where the loan program underwent reform.

(2) Nominal interest rate refers only to the rate during repayment. 'a' refer to loans that use a different rate during the disbursement and grace period. 'b' denotes those programs with interest rates which are indexed.

(3) Real interest rates use Purchasing Power Parity formula, where inflation is based on the average of the 1980-1988 period as reported in the World Development Report, except in instances noted where a 5 year average of inflation was calculated from the data date.

(4) The repayment length is the maximum prescribed in the loan, except for the two income contingent loans where it is the repayment length that is implied by the average income profile of a graduate. This does not include grace periods.

(5) The hidden grant percentage is calculated as a discounted cash flow of the student's account, and therefore excludes default and administrative costs.

(6) The government loss due to default subtracts the % of default from each year of the repayment stream. 'c' denotes where these figures have been estimated.
For Colombia, Jamaica, Chile and Kenya the figure used is loans in arrears.

(7) The loss with default and administrative costs subtracts an annual administrative cost related to outstanding debt each year.

(8) Year is date from which loan information was collected, and from which inflation calculations were made.

SOURCE: Ibid;1991:15

HIDDEN INTEREST SUBSIDIES

Student loans have a "hidden grant" if they charge an interest rate that is less than market rates for borrowing. The factors influencing the size of the hidden subsidy are interest rate charged and length of repayment. Because interest rate charged is below market rates the real loan value recovered even if all students repaid on time would still be low. Table 3.3 indicates that all loans programs are subsidized ranging from 13% in Barbados to 93% in Venezuela. Even in Sweden and Barbados when real interest are positive the loans are still subsidized because interest charged is below market rates.

Equally important to minimise the hidden grant is ensuring a limited repayment length, although longer repayment periods are effective against default and less burdensome to student it leads to larger hidden subsidies.

EVASION AND DEFAULT

Critics of student loans argue that it will be difficult especially in developing countries to secure repayments of loans and prevent default. Mingat and Tan;(1986:290) show that this problem depends on the effectiveness of arrangements in debt collection. For example it may be insignificant under an arrangement where employers make loan repayment deduction prior to paying out borrower's salaries. Good record keeping of borrowers is essential to reduce default rate since defaulters can easily evade payments.

In most countries inadequate collection procedures constitute a major weakness of loans programmes. For example in Sri Lanka loan repayments represented only 15% of the total value of loans awarded between 1964 and 1980. Main reasons for this low performance is usually attributed to inadequate attention by banks to loan recoveries and student evading repayment even after obtaining employment. (Hemachandra; 1982:4) TABLE 3.4 indicates default and evasion in several countries. Kenya shows a non repayment of 81% in other countries like Sweden,Hong Kong and Canada default is less of a problem. Although experience indicates that default and evasion constitute a more severe problem than subsidies measuring default is difficult. Some countries measure arrears rather than default. West;(1988:) shows that if what is used is the value of the outstanding unrepaid debt in relation to the total outstanding loan instead of a percentage of a number of unpaid loans, default rates would be higher therefore losses may be underestimated.

TABLE 3.4

Non Repayment of student loans as percentage of total loans in selected countries

country	Non repayment as percentage of loans	year	Country Definition
Jamaica	38.8	1985	Arrears
Sweden	1.0	1988	Default
Ontario, Canada	0.5	1988	Default
Colombia	12.0	1985	Arrears
Chile	40.0	1989	Arrears
USA	17.0	1987	Default
Denmark	10.0	1987	Default
Israel	2.0	1980	Default
Japan	2.3	1985	Default
Kenya	81.0	1987	Arrears
Hong Kong	1.0	1988	Default

Note: Each country has different definition of non-repayment. Default means that countries have written off loan, while some countries list payments as in arrears,when in reality students have defaulted.

Source: Ibid.1991:17

ADMINISTRATIVE COSTS:

Administrative costs including processing, maintenance and collection costs need to be considered to establish the true cost of a deferred cost recovery program and improve efficiency. For developing countries administrative costs may be higher, for example in Kenya it has been difficult and costly to track mobile students. In addition small average loans used in developing countries makes them proportionately more costly to administer.

Sweden, Hong kong and Canada as illustrated in table 3.4 have the most efficiently run operations with costs ranging from 0.5% to 1% of outstanding debt each year. In Latin America overall administrative costs are between 12% to 23% of the value of the loan which suggests that institution investing in cost recovery spend even more. Programs that rely on commercial banks or taxation have lower administrative costs. In Brazil operating costs for commercial banks are approximately 10% of the total loan value. Administrative costs for taxation collection may even be lower due to large economies of scale.

LOAN IN RELATION TO UNIVERSITY COSTS

One of the central and practical rationale for loan programs especially in developing countries is to diversify and broaden sources of funding for higher education. Experience shows that most loans are used to reduce government burden for student maintenance and few are used to reduce institutional funding.(Albrecht et. al;1991:20)

Table 3.5 compares contributions to higher education instructional funds from students paying direct fees from their own funds and those paying with government loans. Experience with seven countries constituting some of the highest public sector cost recovery in the world, shows that governments recover between 4% (Columbia) and 14% (Quebec) of instructional costs from loan recipients (as indicated by column three which shows the proportion of teaching expenditure that governments recover from loaned students).

Except in Australia all countries have the average size of the loan greater than tuition costs, and governments spend large amounts of money on student support in addition to institutional subsidies,hence, actual cost recovery is low. The reason for for low cost recovery is compounded by the fact that loan programs often require further government expenditure to recover the loans i.e. collection and administrative costs.

TABLE 3.5

Effective cost recovery from loan recipients at Public Universities as a fraction of unit instructional costs*

Country	(1) Unit Instructional Costs	(2) Average Tuition From Non-Loan Students	(3) Implied Cost Recovery Ratio for Loan Recipients	(4) Average Loan size in relation to fees
Chile	100	35	5	Greater
Colombia	100	4	4	Greater
Indonesia	100	25	7	Greater
Australia	100	18*	9	Equal
Canada	100	22	14	Greater
Japan	100	9	4	Greater
USA	100	24	11	Greater

* Fees in Australia are nominally set at 21% of recurrent costs, but students receive a 15% discount on fees if they pay them up-front.

Source: Ibid.1991:20

3.4 LESSONS FOR LESOTHO FROM INTERNATIONAL EXPERIENCE WITH STUDENT LOANS

Experience indicates that there is often conflict between efficiency and equity criteria with student loans therefore depending on the loans main objective individual countries may follow a populist view or an elitist view (meritocratic). The former would distribute education opportunities equally among members of society, whereas the latter would base the distribution of higher education on ability and promote vertical equity, those who believe that the poorest and disadvantaged groups should be given priority, their definition of equity might conflict with that suggested by a meritocratic definition.(Psacharopoulos et al;1985:252).

Loans scheme can be made to work successfully. Experience from Sweden shows that students (even the poorest) are not unwilling to borrow, and the loan scheme is operating effectively with an insignificant administrative costs and default rate.

To minimise the borrowing risk to low income students, most governments subsidize loans. But large subsidies undermine the purpose of having the loan in the first place. Governments may minimise more effectively the problem of risk aversion by limiting the repayment burden in any given year: by linking payments to income, imposing payments ceilings, or providing exemptions if income falls. Such measures can minimise the risk to low income students and encourage them to borrow to finance

their studies. Experience indicates that an income contingent loan may meet the above measures.

A deferred payment program requires the availability of a fully fledged credible collection institution, preferably a taxation department or a social security agency depending on the method of collection used, this proposition does not rule out use of banking systems.

The current evasion rate among graduate on taxes, the number of graduates that work in the public and private sectors, and the current rate of unemployment are relevant variables to be considered.

There must be a willingness to charge interest rates equal or above inflation in order to minimise the hidden subsidy. With tax or income contingent collection the rate should be assessed to ensure significant cash flows. This needs careful financial calculations particularly on the size of annual disbursements and growth of higher education to account for the impact of inflation.

In order to minimise excess burden on graduates and ensure payments it is necessary to examine the relationship between repayments and the likely income of graduates. The income range according to profession and sector may be equally important in addition to average income profiles of graduates.

It is essential to develop a means of targeting support to the needy and academically

able students to achieve a program's efficiency. The larger the expected participation rate, the greater is need for tight repayments and strict collection in order to maintain a revolving fund. For developing countries there may be need to consider institutions closer to students such as universities which may be able to make rational academic judgement.

3.5 CONCLUSION

Experience with student loans has shown that there are differences in various schemes hence models and mechanisms may not be transferable from one country to the other. Historical, political, ideological, social and economic conditions shape each country's policies and idiosyncratic patterns. However cross- national comparisons can help enlighten and influence the student loan system in Lesotho notwithstanding the limitations of transferability. (Johnstone;1986:13) The next chapter will suggest a possible model for Lesotho.

CHAPTER FOUR

4.0 THE MODEL OF A STUDENT LOAN SCHEME FOR HIGHER EDUCATION IN LESOTHO.

4.1 INTRODUCTION

The idea of loans to students is not new in Lesotho, it originated in May 1952, when the then Paramount Chief Lerotholi ordered the establishment of a Basotho Higher Education Fund. (Woodhall;1991:56) There was a combination of loans bursaries and grants and most of the loan bursaries were free whilst in some cases loans were repaid without interest by recipients upon completion.

It was until 1978 when the idea of free bursaries was abandoned the major reason was that government could no longer afford to bear the cost of the bursaries alone. There was need to apportion the cost between the government and the consumer. Thus, the Loan Bursary Fund was established in 1978 by Legal Notice No.20 (Appendix 3) by which students had to repay a portion of the cost upon employment (commencing as from the end of the first month of employment for a period of five years) and the major objective (which still holds to date) was to provide a revolving fund from which assistance could be given to Basotho students to further their education on a repayment or partial repayment basis. (p.211)

The reasons for change to loan bursary was: the increasing cost of education and training, the increasing social demand and the limited funds and resources available for education and training. This is compounded by increasing competition from other sectors of the economy for scarce resources. On the other hand it was hoped that when the fund was fully operational, it will provide a revolving fund from which more and more capable Basotho students could be assisted, provide savings for government in the long-run and reduce financial burden (be self financing) on government for education and training and improve efficiency because such a scheme would make students behave more like investors than consumers, thus, consider their work more seriously and repetition rate might be reduced.

However, since the inception of the loan bursary scheme the results are benign. After ten years in operation the fund was still financed by government and the objective that it be a revolving fund was not realized.(Woodhall;1991:58) It is largely owing to the inefficient administration of the loan program which results in high rate of default and evasion hence the need for improvement and change.

Once it is accepted that a loan scheme can be used as a means of financing higher education, and that it can be more advantageous than a grant system in terms of cost-recovery, efficiency and equity, whether or not a student loan can be made to work successfully will depend, to a great extent, on efficient administration.
As mentioned in the previous chapter loan schemes are now in operation in over fifty developing and industrialised countries and experience from them can provide useful lessons to other countries for administering loan programs.

However there is no 'ideal model' of a loan scheme because of the diversity in political, economic and educational policies in individual countries. For any loan scheme to be viable, it must be designed according to the reality of the situation in a country. This chapter will concentrate on practical issues that would affect the design and management of a loan scheme in Lesotho.

In order to suggest a possible model of a student loan program for higher education in Lesotho, there is need to give an economic background and the government source of finances as a background in justifying the need to change the present system of financing higher education.

4.2 ECONOMIC BACKGROUND IN LESOTHO

The government of Lesotho (GOL) is increasingly recognizing that, as the country's natural resource endowments are severely limited Lesotho must emphasize human resource development as the key to its future economic growth. As a means but not necessarily as a sufficient condition the government policy is to provide basic education opportunities for all and to every citizen of the country.

Lesotho as a small country completely surrounded by the Republic of South Africa (RSA) has only two significant natural resources i.e. **WATER AND LABOUR.** (Fifth Five-Year Development Plan;1992:3) It has limited agricultural land and low potential for mineral exploitation. Because of the large area covered by mountains the arable land is about 13% of the total area. During the 80's the share of agriculture to GDP fluctuated between 20% - 26% and reached a low of 13.9% by 1991 whilst the

manufacturing sector contributed only 14.2% in 1991.

Lesotho is currently involved with RSA under a big scheme, the Lesotho Highland Water Project (LHWP) worth $2.5 billion, in an attempt to utilize the abundant water resources. The LHWP consists of two components, that is export of water to RSA and generation of hydroelectric power in Lesotho. On completion the LHWP is expected to provide significant benefits to the country including employments effects and infrastructural investments. Although the prospects of the project are promising it is a highly sensitive venture depending on political harmony and co-operation between the two countries hence its future is unpredictable.

The country's Five Year Development Plans have emphasised the need to improve access, quality and relevance of education in Lesotho. The development of human resources appear high on the agenda as an essential ingredient for the country's development.(Education Sector Development Plan,1992:4). In order for the GOL to achieve its challenging obligation there is need for an equitable and efficient use of scarce funds within an effective management of the education system.

As illustrated by TABLE 1.1 (chapter 1) the imbalances between different education levels are exacerbated when per pupil expenditure are examined. Although wide variation in per pupil costs across different levels is common in Sub-Saharan Africa, the situation is accentuated in Lesotho because of the high parental contributions at the primary and secondary level. In contrast, almost all costs at the university are borne by the government. Nevertheless, the discrepancies in per pupil outlays at

different levels are cause for serious concern hence my proposal for introducing and improving cost recovery for higher education as the prevailing system is both inefficient and inequitable.

4.3 SOURCES OF GOVERNMENT FINANCES

One of the important features of the government revenue is that it must be stable and reliable in order to facilitate the planning process. In most developing countries this is not the case and Lesotho is not an exemption. It is necessary for the government to have direct control and power over its revenue so that the money could be spent in areas of first priority, that are crucial and deterministic towards attaining a self sustained growth which may lead to development.

In the case of Lesotho one can identify three main sources of government revenue namely, Customs Union Revenue under the present South African Customs Union Agreement (S.A.C.U.A.), Foreign Aid and Tax Revenue. While accepting the importance of the first two, for any government particularly in a developing country like Lesotho, the long term stable source of government revenue is taxation. This is so, because the other two sources are temporary and short lived and cannot be relied upon as sources of government revenue for long term investment purposes like manpower development for an example.

According to the Lesotho government estimates of Donor aid from 1975-80 there has been a declining trend from 22% to 13% of total donor aid. The instability of this

source is justified because the question of withdrawal does not purely depend on economic matters only but depends also on political matters which might affect the economy adversely.

> **"In the past, receipts from customs union were the principal source of government revenue ... However, the importance of customs revenue both as a proportion of GNP and in nominal terms is expected to fall ...This requires an increased reliance on the domestic economy as a source of taxable income ...Government will aim at diversifying and increasing non-custom revenues ... This will entail an improvement in the enforcement of existing taxes". (Fifth Five Year Development Plan,1992:44)**

Whilst it is apparent that taxation is an important and reliable source of government revenue in Lesotho the present tax system may not be adequate and efficient in that more effort is needed to improve the administrative capacity and widen the scope for taxable capacity. In addition the tax structure in Lesotho ranks amongst the highest in Africa especially income tax rates. (Ambrose, Johnson & Campbell;1983) An indication that the burden is heavy on the taxpayer hence my argument that taxable resources be explored, the taxable capacity should be widened and tax effort be improved.

Introducing cost recovery measures through student loans and fees for higher education may shift the burden from the taxpayer by allowing students benefitting from university education to have a share in financing their education from future earnings and to reduce burden on public expenditure and free funds to where returns are higher thus the system will become more equitable and efficient.

4.4 ADMINISTRATION OF STUDENT LOANS

According to Woodhall (1987:32) there are four administrative functions to consider in order to improve efficiency and equity in administration of loans. There should be a body responsible for; selection of recipients, distributing loans to students, deciding on who has to guarantee loans and who has to secure repayment of loans. These are not straight forward functions to address nor provide optimal solutions. The choice of an administrative model may depend partly on the existing banking, tax and educational structures in a given country.

Experience with some loan programs is to divide responsibility for the different administrative functions between different agencies. For example universities may be responsible for selection whilst commercial banks may provide the loans and collect repayments. The justification for this, is that commercial banks may have expertise in the management and collection of loans whilst universities may make rationale academic judgements.

In developing countries which do not have the vast network of private banking and financial institutions special agencies may have to be established or state owned banks be given responsibility. Whilst banks may manage the disbursement and collection of loans, they lack knowledge of how to select deserving students therefore many countries rely on university staff (Chinese, Chilean and Indonesian universities) and other institutions to process loans applications and select recipients. The model suggested for Lesotho is to divide the responsibilities between the university, the state

owned bank and the tax department whilst the overall coordinator should be the existing National Manpower Development Secretariat (government office responsible for manpower development).

It is suggested that loan application and selection be a responsibility of the university in consultation with the national manpower office (coordinator) for the following: The university is responsible for selecting students for admission, the loan and admission selection may be done concurrently by the staff already employed. This may alleviate the problem whereby students will get admission from the university but have to wait for the award of a loan bursary. This would be cost effective and improve efficiency in that there would not be a time lag which is currently a problem for the university to know in time how many students will be admitted for a given academic year.

In addition an effective and acceptable selection criteria should be based on need and ability and the university staff might be in a better position to make rational decisions. Students could be interviewed with their parents or guardian about family income and documents like financial statements be requested if deemed necessary. The suggested selection criteria could improve efficiency in that it could instil a sense of obligation to students and make them regard their work more seriously at the same time make parents (society) aware of the importance of loans hence the need to avail to the rest of the society.

The Lesotho Bank (government owned) is presently responsible for distribution of loans and it is suggested that the collection be a responsibility of the tax department.

This would minimise default in that most graduates are in the formal sector moreover the university would be supplying an exhaustive list of loan recipients to the government department responsible for securing and allocating jobs to graduates[4] which would in turn forward the lists to the tax department. Presently the government guarantees student loans in Lesotho and borrowers are compelled to provide a personal guarantee (parent or guardian) in cases of default.

4.5 TYPE AND REPAYMENT OF LOANS

As discussed in chapter three there are basically three types of loans, the 'mortgage', 'income contingent' and 'graduate tax'. One has learned from international experience that the graduate tax is advocated on equity grounds but this type has not been implemented anywhere. However this type would be preferred in Lesotho if the tax department would be responsible for collection since it would be cost effective and efficient.

Without experience with graduate tax, it is suggested that an income contingent loan should replace the mortgage loan type presently in place (refer to Appendix 3 page 212) on both equity and efficiency grounds because the former constitute a mechanism for achieving a balance between effective recovery of costs and minimum risk to borrowers. This can be illustrated with the aid of a diagram below showing the advantages of income related over the straight repayment scheme.

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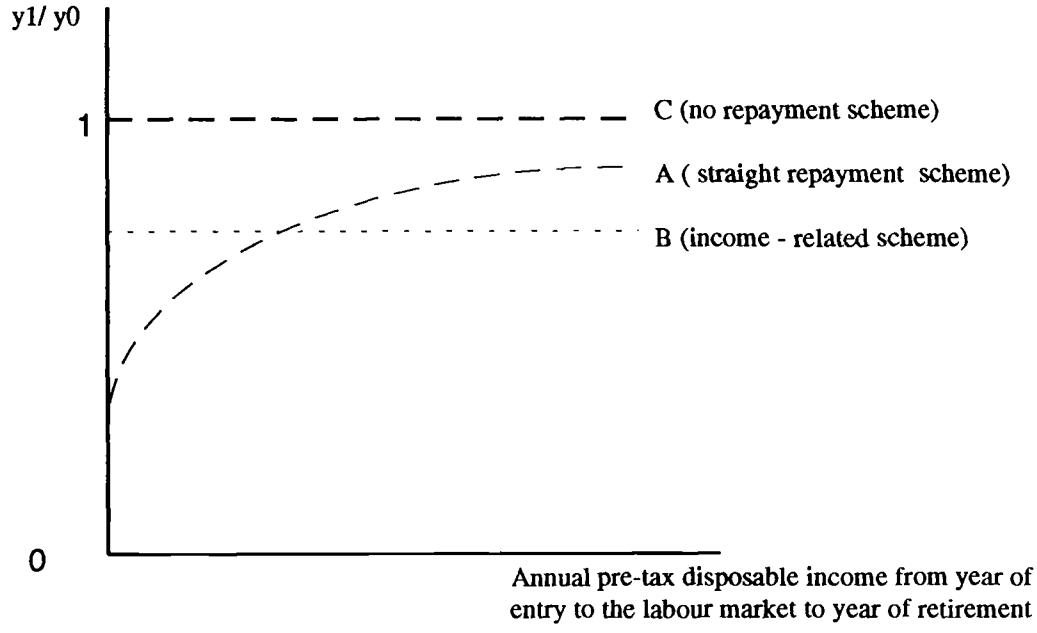
[4]This department presently does not exist in Lesotho but this will be discussed under recommendations.

DIAGRAM 4.1



Sources : Mace, 1987 :27

The two methods of payment shows how annual disposable pre-tax income will be affected through working life. In diagram 4.1 the horizontal axis shows annual disposable income from year of entry to the year of exit from the labour market. The vertical axis shows the ratio of annual income after the policy change, Y_1, to annual income before the policy change, Y_0 . We can observe the way the ratio Y_1 / Y_0 is affected by income-related and fixed-repayment schemes. With a straight repayment scheme, the burden of repayments is greater in the early years of employment when income is low. As annual income rises with work-experience, the burden declines and ceases abruptly when the loan is paid off (see line A). As described by horizontal line B, the income related scheme requires a fixed proportion of income, the borrower pays less when the salary is low or zero if earnings are zero. Line C represents a position where no repayments are required, so that $Y_1 = Y_0$ and $Y_1 / Y_0 = 1$.

A straight-repayments scheme may be inequitable, in that it will have adverse distributional effects since every graduate has the same amount to repay. These repayments will amount to a higher proportion of the annual incomes of low earners than of high earners. Under a straight-repayments it is probable that potential students with low-income expectations will be discouraged from entering universities and this result would be inequitable by discriminating against access of certain groups of potential students. This would make the loans repayment scheme equivalent to a regressive tax (that treats unequals equally) that is, a tax that takes proportionately more from low-income than from high-income.

Barr (1991) supports this when he writes:

> **"Mortgage loans - type are risky from the individual student's viewpoint and so are likely to deter applicants particularly from disadvantaged backgrounds. This is inefficient because it wastes talent and inequitable because it reduces intergenerational mobility.(p.160)"**

An income-related scheme is redistributive in that by taking more from high earners than from low-earners, it reduces the inequality of income that would exist without a loans scheme and under a straight-repayments scheme. An income-related scheme is efficient, in that default and evasion by borrowers may be minimised since the burden of repayment would be proportional to income level and the size of the hidden subsidy could be reduced since the repayment amount is not a uniform proportion of income. Graduates with larger income would be paying more than with smaller incomes. Hence this method is recommended for Lesotho in the interest of both equity and efficiency.

4.6 HIDDEN INTEREST SUBSIDIES

With a loan scheme, full cost recovery is theoretically attainable. In reality, however, the outcome may be limited since it depends on the practical feasibility of implementing repayment policies, especially with regard to interest rate charged for recovery and the length of repayment period for borrowers. There might be conflicts between equity and efficiency criteria.

Firstly, to minimise the hidden grant government need to ensure a limited repayment period but longer periods are effective against default and less burdensome to students. Secondly, to minimise borrowing risk to low income students governments need to subsidize loans hence charge low interest rates less than market rate or no interest at all. But large subsidies undermine the purpose of having the loan in the first place and result in a low recovery ratio, leading to an inefficient program where government will continue to bear the cost of higher education (tuition and maintenance costs) by recovering little compared to what it lends out.

According to Woodhall;(1987:24,42) it will be impossible to monitor the effectiveness, equity and efficiency of loans unless the objectives of the program are stated clearly and explicitly. This is the dilemma facing student loans in developing countries, although in Lesotho the main objective is to increase cost recovery and make the scheme a revolving fund and possibly release funds to lower levels or generate extra resources for higher education, it is also the governments' concern to increase opportunities and access to all able Basotho students especially the low-income group

by providing subsidies.

It is suggested that the repayment period for Lesotho be extended from the current five years say to ten years. Since the repayment of loans has been envisaged as an income-related method the repayment period can be longer than a fixed-repayment method and a moderate interest rate of 5% - 8% could be charged. Although such an interest rate may imply a hidden grant for the loan repayment being lower than the market interest rate for loans, and the function of the loan as a cost recovery may be weakened. According to loan bursary fund regulations (Legal notice no. 20 of 1978:213) the recipients of loans are free to accelerate their loan repayments, the interest rate can be decreased or written off if a student is prepared to repay the loan within a shorter period of time. Since the extent of subsidization is closely related to the duration of repayment: The shorter the duration of repayment the less subsidization by government.

4.7 INCENTIVES FOR LOAN PROGRAMS

Experience from student loan programs in the previous chapter has indicated that they can incorporate flexibility in their design, for example, in providing variable repayment terms and different interest rates for different categories of students, and loan forgiveness for students who meet certain conditions or to encourage student to enter certain professions. However one has learned that incentives may jeorpadise the objectives of a loan scheme, for example, incentives had little effect on student career choices in the USA.

In Lesotho student loan scheme provide generous incentive and flexibility. This is so because one of objective of the loan scheme is to provide skilled manpower for the economy, particularly the public sector (the largest absorber of graduates). This is reflected in the loan repayment terms (Appendix 4). If the borrower works for the government for a minimum of five years after graduation, then 50% of the loan is transformed into a bursary; if the graduate joins the private sector, 65% of the loan must be repaid and those who chose to work outside the country must pay 100% of the loan forthwith.

Attempts to incorporate flexibility in this way may raise a number of questions and create a number of complications. For instance as mentioned earlier Lesotho suffers from brain drain of graduates for better paying jobs into RSA and it is impossible to trace them, but it is this borrowers working abroad who are expected to pay 100% of their loan. Secondly without an effective machinery to monitor borrowers' future career by securing and allocating jobs for graduates within reasonable time after graduation enforcing different rates of payment would result in an inefficient and inequitable system. Moreover it is easier to trace graduates in the public than in the private sector yet borrowers in the latter must repay an amount higher than the former. The discrepancy may discourage borrowers to join the public sector after all. A scheme which incorporates many variables may be more difficult and costly to administer than a simpler program.

There may not be an immediate answer to a policy choice in deciding on flexibility in repayment on loans. However experience suggests that there may be advantages in

introducing a fairly simple system initially and introducing administrative complexity and flexibility in the light of experience.

In Lesotho a flexible repayment method may be recommended on condition the government adopts the system prevailing in Botswana. Whereby there is 'good' record keeping of students' place of study and year of expected completion by a department specifically assigned that. Whilst, another department, the Directorate of Public Service Management (DPSM) is responsible for allocating graduates to different departments, private and parastatal sectors and allocation is based on student preferences which is submitted to DPSM by completers at the end of their final academic year. This proposition does not rule out the uniform repayment criteria as it may be less easy to administer and less costly.

4.8 RECOMMENDATIONS AND IMPLICATIONS

1. An office/department be established and be responsible for: keeping up to date records of students' program of study and expected year of graduation and for securing and allocating jobs for graduates soon after completion. The government may minimise the high rate of default and evasion at the same time reduce brain drain of graduates.

This may also improve efficiency in that the government may be able to monitor and perhaps regulate overproduction, underproduction and imbalances of different profession in the economy thus achieve exchange efficiency. This might introduce additional costs to the administration of loans, however, it is believed the government

might realise savings in the long run.

2.In order to reduce the existing imbalance in the financing of education, by improving equity and efficiency the present level of public subsidy should be reduced by introducing fees and loans. Fees be introduced to constitute part of tuition whilst loan bursaries should cover tuition, accommodation and books. Pocket money and food should be a responsibility of the individual students. The aim is to reduce the high imbalances between sectors.

One may also argue that the prevailing system enables high income groups to enter university since there is no free compulsory education at lower level those who afford to pay benefit from the publicly financed education by the same analogy he or she who benefits must pay. However cost recovery in education and elsewhere involves changing costs and this change is associated with a policy change.

The changes can be met with an effective barrier for implementation on economic and political grounds. It is a challenge to policy makers to discover ways to effectively block reform. In Lesotho, it is hoped that if the parents (society) are well informed of the need and importance of such changes resistance could probably be short lived as the issue of paying fees is not new in the education system. Publicity campaigning is essential for implementation of a new policy for it to gain favourable popularity.

Another important aspect is for the government to be able to use the generated income efficiently and equitably within the education system. The ultimate disposition

of funds depends upon those who are given control over them. It may be preferable that funds raised through user fees be controlled by authorities directly involved in the education system to avoid their allocation outside the education sector. There is need to research on information on the costs of collecting fees and to evaluate the appropriate level of fees to charge if fees are meant to reduce the costs of financing higher education in terms of institutional funding and not only student maintenance.

3.Closely related to the above discussion is the dilemma facing financing of education in Lesotho. It has been argued that with the existing imbalances within different levels there is need to shift resources from higher education to primary education in the interest of equity and efficiency. In reality, both higher education and primary education have a legitimate claim to higher funds.

With regard to higher education as indicated earlier, there is an unmet social demand therefore expansion is inevitable. In addition N.U.L. being a small growing university suffers from diseconomies of scale, acquiring more funds would help the university to produce towards its production frontier (optimal point) to achieve production efficiency (refer to chapter 2 diagram 2.1) and realise economies of scale. Moreover manpower development has been given top priority by the government as the key to attain economic growth hence sustain development.

For primary education, the goal of universal primary education has not been achieved about 75.2% of required primary school age population are enroled. According to the Education Sector Plan (1992:4) the existing system suffers from decline in quality, lack

of relevance to occupational and social realities, high drop out and repetition rates and very poor facilities and staffing.

Introducing cost recovery through loans and fees might help towards solving the dilemma, in that extra funds could be released by reducing the burden on government expenditure hopefully achieving a self financing revolving fund and the recovered funds be used within higher education.

4.There is need to revise the existing legal framework established by Legal Notice No. 20 of 1978. The method of repayment as stipulated in page 212 should change from a fixed monthly payment to income - related payment on equity and efficiency grounds as indicated earlier. Secondly under "repayment of bursaries" on the same page, it is recommended that a uniform method of payment be used unless as argued earlier recommendation 1 is met. Generally all other changes may follow from this two major ones, for example extending payment period from five to ten years.

5. Presently, the university statistics indicate that about 80% of the student population are financed through loans. It has been impossible to get information about the amount of funds the government disburses yearly, and the amount it recovers. Despite the shortcoming one can conclude that performance has been poor on two counts: according to a statement made earlier that after "ten years of the inception the loan fund has failed to meet the objective of a revolving fund".

Secondly the Lesotho delegation at the 1991 symposium held in Nairobi indicated high

rates of default and evasion with student loans, an indication of low cost recovery ratio hence the government is paying more and recovering less. In addition to improvements in management and design there is need to implement the selection criteria based on need and ability as recommended earlier hence the neediest should benefit from the loan bursary. This is emphasised in view of the imbalances existing in the financing of different sectors which will have efficiency and social implications.

4.9 CONCLUSION

This report used an economic framework to analyze the present system of financing higher education in Lesotho and argued that the existing system needs to be modified and changed. The need to modify and change stems from the following: the government financial constraints, (as indicated in chapter 1 page 2, and under 4.3 sources of government finances) pressure on government for more and better quality as a result of high population growth (chapter 1 page 1) and on equity and efficiency criteria.

Due to eminent imbalances in government expenditure (table 1.1 page 4) between different levels exacerbated by the fact that private contribution is confined to secondary and primary and is almost non existent at higher education there is a case for introducing a student loan scheme and fees as a means of cost recovery and to reduce public subsidy at higher education.

A switch to loans and fees could be beneficial to Lesotho on both equity and efficiency grounds in these ways:

If it is accepted that higher education benefits society as a whole, there is a case on equity and efficiency grounds for government to pay part of the costs. However, a degree confers private benefits on students (higher pay, greater job satisfaction) so it is both efficient and equitable if the students also bears part of the costs themselves.

Secondly, if capital markets were perfect (if all students could borrow against their future earnings) the private market could supply loans itself. Since many students especially the low-income group are unable to obtain long-term private loans government intervention is necessary. Therefore the government needs to guarantee and perhaps also provide loans. This may improve equality of opportunity and efficiency in that capable and able students could now enrol.

Thirdly loans may reduce the public costs of higher education, making it possible to expand the system to a more efficient size i.e. to realise economies of scale. Fourthly loans may make it possible to shift the burden from the already over burdened parents and taxpayers (refer to sources of government finances 4.3) It is rationale to allow students deferred payments through loans and pay from their future earnings.

From the analysis presented it appears that the introduction of loans and fees at higher education is justified on both equity and efficiency grounds and is therefore desirable and beneficial to Lesotho. The report further purported to argue that the 'market' model of financing may be appropriate in financing education in Lesotho. As indicated in chapter two a market model may combine more easily with a system of loans hence the need to introduce loans at higher education.

This model would have the advantages of securing consistent funds for higher education, encourage universities to achieve production efficiency and probably an insignificant effect on exchange efficiency. In addition internal efficiency would be achieved as repetition and drop out might be reduced. Efficiency and equity criteria

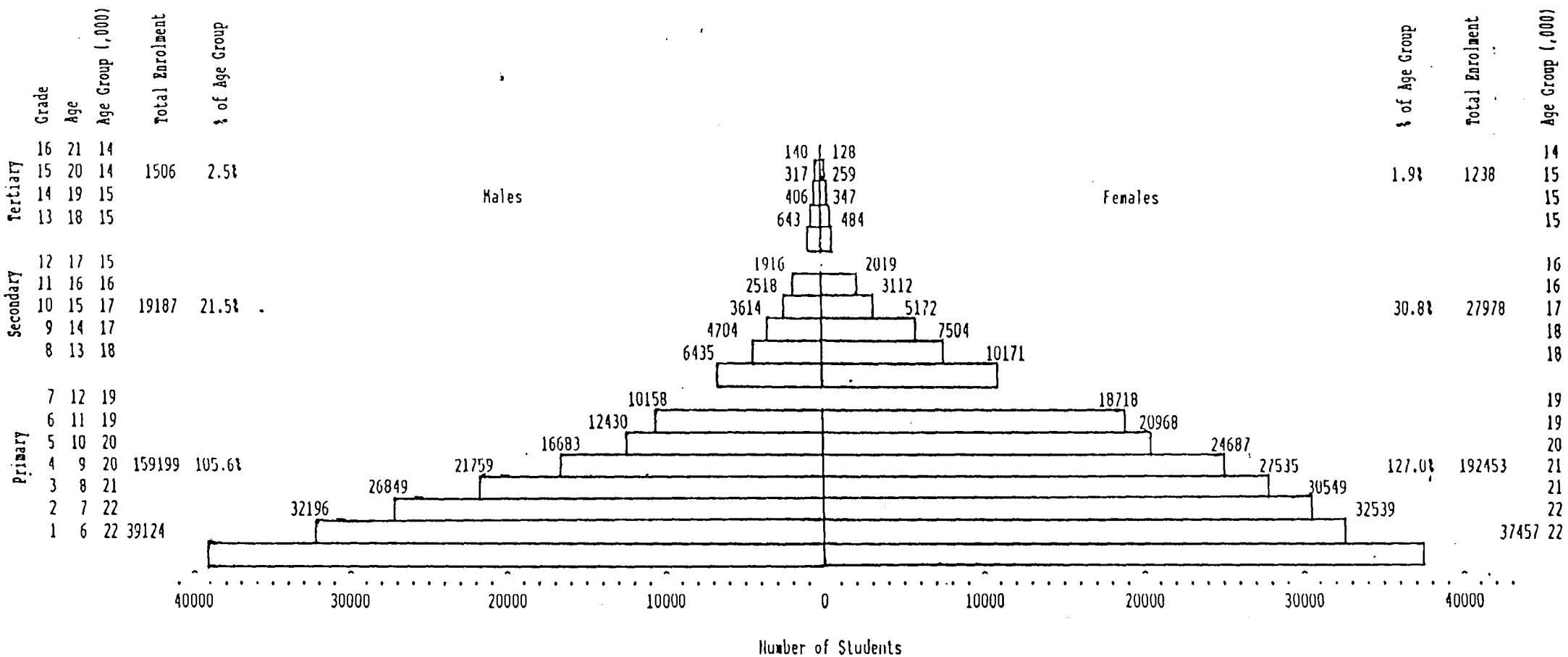
might be improved as the selection would be based on need and ability.

Moreover a cost recovery measure would not only improve economic efficiency but may also have an impact on social equity, allocation of resources, redistribution of income, bridge the gap between costs and benefits of higher education and improve manpower development.

This paper attempted to provide an insight into the nature of the problems by identifying and suggesting what could be done to minimise them. Hopefully the government may improve the present situation by adopting them.

APPENDIX 1

Figure 2 Lesotho Education Pyramid, 1990



Notes: (a) Figures for school-age population are estimates based upon the census of 1976.
(b) Grades 1 to 7 are Standards 1 to 7.
(c) Grades 8 through 13 include enrolments in general secondary courses, teacher training courses, and vocational/technical courses.
(d) Enrolments for all grades include over-age students.
(e) Students studying abroad at a tertiary level are not included.

SOURCE: EDUCATION STATISTICS;1990:2

APPENDIX 2

AVERAGE RETURNS TO EDUCATION BY COUNTRY TYPE AND LEVEL

(PERCENT)

Region	Social			Private		
Country Type	Primary	Secondary	Higher	Primary	Secondary	Higher
Africa	26	17	13	45	26	32
Asia	27	15	13	31	15	18
Latin America	26	18	16	32	23	23
Intermediate	13	10	8	17	13	13
Advanced	NA	11	9	NA	12	12

NOTE: NA= not available because of lack of a control group of illeterates.

SOURCE: Psacharopoulos;1985:587

LEGAL NOTICE NO. 20 OF 1978

Loan Bursary Fund Regulations

In exercise of the powers conferred by section 16 of the Finance Act 1973, I,

Evaristus Retšelisitsoe Sekhonyana

Minister of Finance, make the following regulations —

Citation

1. These regulations may be cited as the Loan Bursary Fund Regulations.

Interpretation

2. In these regulations—

"bursary" means payment of university, college, institution, hostel or other fees or allowances to or on behalf of a student undergoing an educational course and any other disbursements and expenditure for or on behalf of the student for the purpose of, or in connection with, the course funded out of the Loan Bursary Fund or by other bodies than Government, but, in the latter case, only where the bursary is awarded by or through the Council;

"Council" means the National Manpower Development Council;

"Director" means the Director of the National Manpower Development Secretariat;

"Minister" means the Minister of Education.

The Fund

3. (1) There is established a special fund entitled the Loan Bursary Fund.

(2) The Fund shall be administered by the Director.

4. The purpose of the fund is to provide a revolving fund from which assistance can be given to Basotho to further their education on a repayment or partial repayment basis.

Receipts into Fund

5. There shall be paid into the fund —

(a) any sums appropriated to the fund;

(b) repayments of bursaries awarded to students;

(c) donations or grants made for the purpose of the fund;

(d) other receipts connected with the purpose of the fund.

Disbursement from Fund

6. (1) Moneys shall be paid from the fund for —

(a) bursaries to citizens of Lesotho;

(b) such related expenditure as may be approved by the Minister after consultation with the Minister of Finance.

(2) Where a bursary is funded by a body other than Government, the sums awarded to a student by that body shall, whether

or not they have been paid into the fund, be deemed to have been paid out of the fund.

Approval of bursaries

7. (1) At each meeting of the Council, the Director shall present a statement showing the balance of the fund available for bursaries, allowance being made for known commitments.

(2) Bursaries awarded by the Council, if awarded directly from the fund, shall not in any one year exceed the amount shown as available therefor in the approved estimates of the fund for that year.

(3) Awards of bursaries shall be subject to the execution of a loan bursary agreement between the Government and the student.

Repayment of bursaries

8. (1) On completion of a student's educational course a report on his progress shall be made to the Council who shall decide whether or not the student has recorded an outstanding performance and take note of the employment he is entering.

(2) A student completing an educational course outside Lesotho who fails to return to Lesotho, upon completion of the course or within such time thereafter as may be allowed by the Council shall repay the full cost of his bursary.

(3) A student who does not serve Lesotho upon completion of his course for a minimum of five years shall repay the full cost of his bursary.

(4) A student who, after completion of his course, works in the private sector or for a parastatal organisation which is not defined as a statutory body under the Audit (Statutory Bodies) Act 1973 shall repay 65% of the notional cost of his bursary.

(5) A student who after completion of his course works for Government or for a statutory body as defined in the Audit (Statutory Bodies) Act 1973, shall repay 50% of the notional cost of his bursary.

(6) A student who changes his occupation during the five year service required of him under sub-regulation (3) shall have the amount of his repayment under sub-regulations (4) and (5) adjusted accordingly.

(7) Subject to his serving Lesotho for five years a student who has recorded an outstanding performance as decided under sub-regulation (1) shall receive a remission of 10% of the notional cost of his bursary.

Method of Repayment

9. (1) Loan Bursary fund agreements shall provide for the repayment of bursaries by equal monthly instalments over a

period of five years commencing as from the end of the first month of employment subsequent to completion of the course.

(2) Recipients of bursaries are free to accelerate their loan repayments.

(3) Notwithstanding sub-regulation (1) the Council may, for good cause, the reasons for which shall be communicated to the Minister, and with the approval of the latter, vary the terms of repayment so as to —

(a) Provide for repayment by instalments at intervals other than monthly;

(b) extend the period of repayment;

(c) remit all or part of the repayment during periods of unemployment or illness or in circumstances where repayments would cause undue hardship.

Termination of bursaries and consequences

10. (1) Where a student —

(a) commits a criminal offence;

(b) uses habit-forming drugs;

(c) drinks excessively;

(d) is the subject of adverse reports as to his general conduct;

the Council may terminate his loan bursary fund agreement, and in this event, the student shall repay the full cost of the bursary as at the date of termination.

(2) Where a student changes his course of study without the written consent of the Council or where his performance at the course is deemed to be unsatisfactory, the Council may terminate his loan bursary fund agreement and require repayment of all or part of the cost of the bursary as at date of termination.

(3) For the purposes of sub-regulation (2) "unsatisfactory" means —

(a) wilful failure to comply with the attendance requirement necessary to complete the course, including attendance at examinations;

(b) unsuccessful completion of a year of study.

(4) Where the unsuccessful completion of a year of study is attributable to no other reason than lack of ability, repayment of the bursary may be waived.

Amount of repayment

11. (1) The Director shall keep a record of each student to whom a bursary has been granted.

(2) Once during each academic year, the Council, on the advice of the Director, shall establish the average cost of a bursary at the National University of Lesotho.

(3) The Director shall, each year, enter the amount of the average cost referred to in sub-regulation (2) on each student's record and the amount shall be deemed to be the notional cost of the student's educational course for that year.

(4) Upon completion of the student's educational course the notional cost for each year shall be totalled and the total shall form the basis of repayment under regulation 8 (4), (5) and (7)

Estimates

12. (1) The Council shall cause estimates to be prepared each year for consideration by the Minister.

(2) The estimates shall be submitted to the Minister of Finance for approval.

Accounts
A.11 of 1973

13. (1) Pursuant to section 16(2) of the Finance Act 1973 the Accountant-General shall maintain a separate account entitled the Loan Bursary Fund in which he shall record the receipts and disbursements referred to in these regulations.

(2) The Director shall maintain accounts in such a manner as the Accountant-General shall direct in which shall be recorded all receipts into, and all disbursements from, the fund.

(3) The Director shall observe the Financial Regulations and other laws and regulations governing the receipt, control and disbursement of public funds.

Annual Accounts

14. (1) As soon as possible after the close of the financial year, but not later than three months thereafter, the Director, shall submit to the Account-General accounts of the fund including —

(a) a statement of receipts and payments for the period of the financial year;
(b) a balance sheet showing the assets and liabilities of the fund at the close of the financial year; and
(c) a detailed statement of repayments in arrears.

(2) A copy of the annual accounts shall be included as a supplementary statement to the annual account submitted by the Accountant-General to the Auditor-General, in accordance with section 27 of the Finance Act 1973.

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Loan Bursary Agreement of the Government of Lesotho

WHEREAS the Borrower has requested the Government to assist in financing the entire training of the Borrower by granting a loan to him in the amount specified hereunder:

AND WHEREAS the course of training of the Borrower in justified from the standpoint of the priorities reflected in the national development plans of Lesotho.

AND WHEREAS the Government has agreed, on the basis, interalia, of the foregoing, to grant a loan to the Borrower in the amount of .....

NOW THEREFORE, the two parties hereby do agree as follows:

1. The Borrower undertakes:—
   (a) to serve the country after the completion of his course of study for a minimum of 5 years;
   (b) where studies are undertaken abroad, to return to Lesotho immediately on completion of the authorised course of training or to pay 100% of the loan forthwith;
   (c) not to change his course of study without the written consent of the National Manpower Development Council on behalf of the Government. Any application to change the course of study shall only be considered by the said Council subject to a written recommendation of the Tutor or Head of Department of the institution concerned;
   (d) to attend, during the course of his training, all lectures, tutorials, field work, practical work and all other training required for his course and to successfully complete each study year. A student will be excused from this condition only on production of medical certificate stating that the disease was the cause of failure;
   (e) not to commit a criminal offence;
   (f) not to use habit-forming drugs whatsoever;
   (g) not to be found drunk.
2. The Government undertakes:—
   (a) to pay the travelling expenses of the Borrower to and from the location of training if such training is undertaken outside Lesotho;
   (b) to pay the living allowance and residential expenses of the Borrower, provided such costs do not exceed the normal student rate applicable to the specific educational institution;
   (c) to pay tuition, book allowance and any other allowances required for the course of training as spelt out in the official prospectus of the particular institution.
3. In the payment of the loan, the Borrower undertakes to repay
   (i) 100% of the loan if he decides not to work within Lesotho after the completion of the course of training;
   (ii) 65% of the loan if he decides to work in the private sector or for a para-statal organisation of which the Government has no controlling interest;
   (iii) 50% of the loan if he works in the Public Service or in Government-controlled para-statal organisation.
   (iv) For purposes of repayment of the loan by students training overseas, the loan fund to be repaid will be considered equal to the equivalent fees payable in Lesotho.
   (v) For students with a record of outstanding performance a 10% credit will be given i.e. for students in the public service or Government controlled parastatals and students in the private sector to pay 40% and 55% of the loan respectively.

SOURCE: Woodhall;1987:66

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