

Policy Research and Dialogue
Student Loans Schemes in Asia

A review of the student loans scheme in China

Hong Shen and Wenli Li



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**Hong Shen
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List of abbreviations

ABC	Agricultural Bank of China
BC	Bank of China
ICBC	Industrial and Commercial Bank of China
CCB	China Construction Bank
PBC	People's Bank of China
MOE	Ministry of Education
MOF	Ministry of Finance
GCSLS	General-Commercial Student Loans Scheme
GSSL	Government-Subsidized Student Loan
GSSLS	Government-Subsidized Student Loans Scheme
RHEI	Regular higher education institutions
SLS	Student loans scheme

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Foreword

UNESCO's mandate – both globally and in Asia and the Pacific – is the important mandate to serve as a standard setter, a clearing house, a capacity builder, a catalyst for international co-operation and a provider of impartial policy advisory services to governments and other partners in the region.

In the furtherance of this mandate, the UNESCO Asia and Pacific Regional Bureau for Education in Bangkok (UNESCO Bangkok) is developing an active portfolio of research and policy analysis studies which will serve as input into ongoing policy debates on education development and reform. Such studies will explore a wide range of issues found both within all levels and forms of education and in the linkages between education and other development sectors. Major policy challenges and priorities in the Asia and Pacific region will guide the selection of operational research topics. The ambition is to support and publish action-oriented, state-of-the-art research grounded in longstanding practical experience of countries in the region and of UNESCO. The series aims at providing education practitioners and advisors working in government institutions and the private sector with a comparative information and knowledge base to support policy dialogue and decision-making in education sector management and reform.

Most of the research to be published under the series will be part of ongoing UNESCO work in the areas of education sector policy and management of countries in the region. Relevant research prepared by partner institutions and individuals will also be considered for publication.

Sheldon Shaeffer
Director
UNESCO Bangkok

Preface to the series

This book is part of a series of in-depth studies on the functioning of government-sponsored student loans schemes in Asia. It was written in the framework of a regional comparative policy review on student loans schemes undertaken by the Bangkok-based UNESCO Asia and Pacific Regional Bureau for Education (UNESCO Bangkok) in association with the International Institute for Educational Planning (IIEP). This regional project covered five countries and territories including P.R. China, Hong Kong S.A.R. China, the Republic of Korea, the Philippines and Thailand. Additional studies are being commissioned by IIEP, and a regional comparative assessment prepared by UNESCO Bangkok is forthcoming.

Most countries in Asia are experiencing a dramatic increase in demand for higher levels of education at a time of both severe public budget constraints and profound overhaul of education systems aimed at significantly increasing their impact and relevance. In an attempt to ease the burden on public budgets, a number of countries have introduced student loans schemes, hoping to recover costs and increase the revenue base for the expansion of education, while at the same time providing opportunities for poorer segments of the population to access higher levels of education.

In an attempt to increase the knowledge base available to governments and provide practical insights which might be useful for national education policy, the UNESCO Asia and Pacific Regional Bureau for Education initiated in 2001 a regional comparative study to examine the performance of student loans schemes in a number of countries in Asia. The study is intended to be instrumental in improving the efficacy and financial efficiency of existing schemes and in providing a comparative information base for countries intending to introduce a student loans scheme.

A joint endeavor by UNESCO Bangkok and IIEP, this regional policy study was initiated and its implementation co-ordinated by the Planning and Sector Analysis Unit (PSA) at UNESCO Bangkok. It benefited from technical support by IIEP and was able to draw on a wide range of regional and international expertise available at research institutes, universities and ministries in the participating countries. Five research teams led by academics and senior-level practitioners were involved in producing the monographs. UNESCO Bangkok and the Korean Educational Development Institute (KEDI) hosted several research seminars bringing together research teams and practitioners from the countries participating in the project.

Partner institutions involved in the study included the Korean Educational Development Institute (KEDI); Huazhong University of Science and Technology (Graduate School of Education), Wuhan; Peking University (Graduate School of Education); the Chinese University of Hong Kong (Department of Educational Policy and Administration); the Commission for Higher Education (CHED) in the Philippines (Office of Student Services, Office of Policy Planning, Research and Information) and the Asian Development Bank collaborating in the framework of an ongoing Education Sector Development Program in the Philippines. Researchers and officials from several universities, education and finance ministries and national agencies such as student loans offices in the participating countries collaborated in the preparation of the case studies. UNESCO Bangkok and IIEP would like to thank all those individuals who provided their expertise and professional experience to this research and therefore helped to assemble a considerable cross-sectoral information base required for comparative loans policy analysis. The important contributions by individual researchers and authors are acknowledged in this book.

The policy study benefited from the technical expertise of Adrian Ziderman, Professor of Economics at Bar-Ilan University, Israel, acting as UNESCO international lead consultant. He provided methodological guidance to research teams along the lines of his earlier study on loans in Thailand, prepared under a joint UNESCO Bangkok – Asian Development Bank project, ‘Education management and financing study’, in 1999. Igor Kitaev, Programme Specialist (education financing), served as resource

person from the IIEP in addition to authoring one of the studies. Dominique Altner, Chief, Planning and Sector Analysis Unit, UNESCO Bangkok, with support from Toshiyuki Matsumoto, Assistant Programme Specialist, PSA, initiated and ensured the professional co-ordination for this study.

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Section 1

Economic transition and the Chinese education system

1.1 The economic transition and reform of the higher-education system

The socio-economic background

Since the People's Republic of China was founded in 1949, the Chinese economic and education systems have experienced two stages of development: one was from 1949 to 1978, the other was from 1978 to now. From 1949 to 1978, the Chinese economic system was a central planning model. In 1978, following the end of the Cultural Revolution, the Chinese people realized that the old planned economic model no longer worked for China. Mr Deng Xiaoping, the leader of China at that time, proposed to bring a market mechanism to the planned model. In 1992, the socialistic market-oriented economic model was formally established, regulated as a policy and implemented throughout the whole nation.

The economic reform was gradually implemented in China. The first reform step was initiated in the rural area and peasants started a contracted production responsibility system (Min, 2002). Under the responsibility system, peasants contracted for farming. They turned in a certain amount of farm produce to the governmental departments, keeping what remained, so that the more they produced, the more farm produce they could own.

Gradually, the economic reform extended to the urban areas. The reform of state-owned enterprises and the appearance of joint ventures and private enterprises drove the reform of the financial system and brought the capital market into being.

With the development of economic reform, the labour market gradually appeared. In the labour market, demand and supply influence the price of the labour supply. As an important element of economic life, the labour

market plays a balancing role. The graduates from higher-education institutions, as human resources of higher quality, choose their jobs in the labour market. The starting salary, the benefits, the career opportunity and the social status form the price signals of a job. The students may have monetary and non-monetary expectations of their future jobs. Their expectations, ability and family background corporately influence the demand for higher education. The demand for higher education draws the supply of higher education. Such interaction between demand and supply of higher education may decide the tuition and scale of higher education.

The operation mechanism of higher education under the condition of a planned economy

The system of higher education under the condition of a socialistic market-oriented economy showed essential differences from that under the condition of a planned economy. Under the condition of a planned economy, there was no dynamic labour demand and supply between educational institutions and places of employment. The relationship between the government, higher-education institutions, employers and college graduates was very simple. The core of their relationship was the government. The government made regulations and policies. The higher-education institutions had to make enrolment plans according to the planned enrolment number set by the government. The employment units had to recruit new staff conforming to the personnel plan made by the government. The college graduates were assigned to workplaces where they began and ended their careers (Li and Bray, 1992).

Under the condition of a planned economy, higher education was totally free in China, but graduates had no freedom of choice in their careers. The rationale was that college students were enrolled as specific talents to meet the specific needs of the nation's construction and each graduate was assigned to the workplace as an element of national construction. They could neither move nor change their workplaces freely and willingly. The wage of those with a higher-education degree was not decided by the labour market, but by the government's personnel departments. Thus, the private monetary benefit from higher education was so little that some scholars thought there existed a reverse of income between workers with higher-education degrees and those without higher-education degrees. Under such conditions of each worker seen as an

element of construction with low private monetary benefit, students did not need to pay for their higher learning. On the other hand, they could obtain living stipends and grants.

The operation mechanism of higher education under the condition of a market-oriented economy

The process of economic transition has led to a series of tremendous changes to the society. Market demand and supply, taking over from the government plan, is beginning to play a fundamental role in resource allocation and utilization. The governmental administrative function in higher education is changing from direct administration to indirect macro-control.

Under the condition of a market-oriented economy, labour market demand and supply has become important to higher-education institutions. Although the private monetary benefits, as indicators by Mincer of private rates of return to higher education, appear relatively low against the world average, even lower than those of developing countries, they have increased greatly in recent years. As shown in *Table 1.1*, the private rates of return to all levels of education greatly increased from 1996-1998, while with different growth rates. The private rate of return to four-year higher education with a bachelor degree is much higher than those to general secondary and two-year college education and reaches 11.35, exceeding 10 per cent of rate of return to physical capital in 1998.

Table 1.1 The private (Mincer) rate of return to education, 1996-1998

	Junior secondary education	Senior secondary education	Secondary professional education	Two-year higher education	Four-year higher education	Total
1996	3.53	4.90	5.67	5.90	8.23	5.33
1997	2.97	8.35	10.72	5.96	9.68	7.20
1998	n/a	8.02	12.52	8.01	11.35	8.00

Source: Chen, Ran and Chen. 2001.

Fleisher, Dong and Liu (1996) estimated the productivity of workers by level of schooling for a sample of 30 state-owned enterprises in the paper industry, using data for the years 1985, 1987 and 1990. They

estimated a marginal product of labour for production workers with less than secondary-school education of 10,399 Yuan in 1990 prices; for production workers with at least a secondary-school diploma, the estimated marginal product was 19,700 Yuan. For managers and engineers who had not received degrees from a four-year college or university, their estimated marginal product was negligible, whereas for those who had successfully completed four years of college or university, the estimated marginal product was extraordinary, nearly 2,000,000 Yuan per year. This figure implied that by adding one additional college-trained manager or engineer, it was estimated to have raised output by 0.756 per cent (Fleisher, 2002).

Although the research offers valuable evidence to show the importance of investment in higher education to economic growth, investment in higher education lags. As outlined below, low investment pertains not only to higher-education enrolment and financing, but also to all education levels.

1.2 Student enrolments and higher-education expansion

Student enrolments

The formal education system of China consists of six years of elementary schooling, three years of junior secondary schooling, three years of senior secondary schooling, four years for a bachelor's degree, three years for a master's degree, and three years for a doctoral degree. In China's education system, compulsory education corresponds to elementary and lower-secondary education for a nine-year learning period.

China has been making vigorous efforts to realize its goal of nationwide nine-year compulsory education, in an effort to wipe out youth illiteracy. In February 1993, the central government and the State Council issued an 'Outline for China's educational reform and development', stating that on the basis of safeguarding the necessary educational input and school management, the goal of educational institutions of all levels in the 1990s was to universalize nine-year compulsory education nationwide (including vocational schools). In large cities and coastal cities where the economy was fairly advanced, schools should aim for the goal of universal senior education. The illiteracy rate among youth was to drop below 5 per cent through a campaign of illiteracy elimination. To further the above two goals, the State Council put forward implementation proposals in 1994, reaffirming that by the year 2000, the whole nation was to realize the goal

of nine-year compulsory education. Areas incorporating 85 per cent of the population would target this goal. The enrolment rate at lower secondary level would be around 85 per cent and 99 per cent for primary. The development goal and the speed with which it was achieved might vary in line with circumstances (Chinese Experts Panel, 2002).

The number of students and gross enrolment ratios by education level are shown in *Table 1.2*. The elementary-level gross enrolment ratio was 99.05 per cent and the lower secondary-level enrolment ratio was 88.7 per cent in 2001. In China, the obligatory six years of elementary education and three years of lower secondary are followed by upper secondary education which is non-compulsory and has dual tracks: general and vocational. Overall, the enrolment ratio of compulsory education has targeted the goal set by the government. However, only 11.5 per cent of the cohort aged 18-21 years was enrolled in higher education (including adult and private educational institutions) by 2001.

Table 1.2 Numbers of students and enrolment ratios by education level, 2001

Education level	Age group (thousands)	Student enrolment (thousands)	Gross enrolment ratio (percentage)
Pre-school education	3-5	20,218	-
Elementary education	(1)6-11 or 7-11	125,435	99.05
Lower secondary	12-14	65,144	88.70
Upper secondary	15-17	26,009	(2)81.00
– general education	15-17	14,050	(2)38.20
– vocational education	15-17	9,758	(2)42.80
Tertiary education	18-21	12,392	(2)11.50
– regular students	18-21	7,191	-
– adult students	-	4,560	-
Postgraduate	-	393	-
– master students	-	86	-
– doctoral students	-	307	-

Source: MOE of China. China Education Statistics Yearbook. 2000, 2001.

Note:

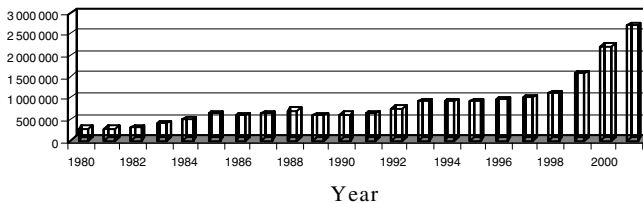
- (1) There are two kinds of elementary-schooling systems in China: six years and five years.
- (2) The data were for 2000.

Regular higher-education expansion

Since the People's Republic of China was founded in 1949, Chinese higher education has developed greatly. In 1949, there were about 0.1165 million full-time students in 205 regular higher-education institutions. In 1998, this number had grown to 3.41 million full-time students in 1,022 regular higher-education institutions. In 2001, there were 7.19 million full-time students in 1,225 regular higher-education institutions.

Chinese regular higher education has really expanded since 1999. In 1978, there were about 400,000 new entrants enrolled in regular higher-education institutions. In 1998, after 20 years, the new number of entrants was about 1.08 million, and the average annual increase rate was 6.11 per cent. However, in 1999 enrolment increased greatly. In 1999, 1.56 million freshmen were enrolled in regular higher education. Enrolment grew continually in 2000 and 2001. Around 2.20 million freshmen, in 2000, and 2.68 million freshmen, in 2001, were enrolled in regular higher education. The regular higher-education expansion is shown in *Figure 1.1*.

Figure 1.1 Number of annual new enrolments in regular higher education, 1980-2001



Data source: MOE, China Education Statistics Yearbook, 1980-2001.

Why did enrolment to regular higher education increase so much in 1999 and continue to increase in 2000 and 2001? The rationale behind it was to encourage human capital investment to higher education, to drive economic growth, in order to counteract negative effects of the Asian financial crisis. The Chinese economy experienced rapid growth from the

period of the implementation of reforms and opening up in 1978 to 1998. During the 1980s and 1990s, the GNP's growth rate reached 8-9 per cent. The Chinese economy showed great strength and was playing an important role in the world economy. Simultaneously, with the appearance and development of the knowledge-based economy in the world, knowledge innovations and technology advancement were playing increasingly important roles in economic growth. The economic growth and social development called for knowledge, technology and higher education. However, the Chinese economic growth rate appeared to decline after the Asian financial crisis occurred in 1998. As a result of the Asian financial crisis, the Chinese showed little consumer demand in many markets, such as housing, automobiles, finance, insurance and so forth. In contrast to the low demand in the markets listed above, some economists thought that the private demand greatly exceeded supply in the higher education market. Many Chinese people hoped to enter higher education in order to improve their monetary and non-monetary situations. There existed great demand for higher education in Chinese society. In order to encourage individual investment to education, to change the condition of weak consumption, the government made a decision, in 1999, to expand higher education to meet the demand of the people for higher learning, on the one hand, and to appeal for investment to higher education, on the other hand.

Although higher education has expanded greatly since the reforms and the opening up in 1978, with even greater expansion since 1999, there has still existed some degree of inequality of educational opportunities between the urban and rural areas. Data in *Table 1.3* taken from a college student survey conducted by Li and Min (2001) in December 1999, highlighted the difference in enrolment opportunity between rural and urban students. This indicates that equal educational opportunity has the same importance and should attract the same attention as higher-education expansion.

Table 1.3 Enrolment distribution across four types of higher-education institutions, by student residence, selected survey data, 1999

Residence of students	Four-year university		Two or three-year college		Vocational college		Non-government post-secondary schools	
	Persons	%	Persons	%	Persons	%	Persons	%
Urban	685	78.1	761	81.0	776	85.3	773	82.1
Rural	192	21.9	178	19.0	134	14.7	169	17.9

Source: Li and Min, 2001.

1.3 Higher-education budgets and financing

With the transition from a centrally planned economy to a socialistic market-oriented economy, the Chinese economy is growing fast. Science and technology develops rapidly and education is having a positive effect on economic growth. Meantime, the increase in individual incomes and living standards has stimulated demand for higher education (Min, 2002).

Public education expenditures

Public education expenditure, as well as its proportion to GDP, has shown an upward trend over recent years, as shown in *Table 1.4*. The state appropriation (excluding earmarked education levies) from national budgets to education was 208.568 billion Yuan in 2000, while it was just 121.191 billion Yuan in 1996. Despite the increase of the state appropriation, total education expenditure increased much more rapidly. The gap between state appropriation and total education expenditure has widened considerably.

Although China is running a huge public education system and higher education has expanded greatly in recent years, its public education financing is still weak by international standards. Through international comparison, it was found that public education expenditure as a proportion of GDP in China was much lower than in most other countries. The world average public education expenditure as a proportion of GDP was around 4-5 per cent in the 1990s, while the proportion in China was around 2.79 per cent in 1999, 2.87 per cent in 2000 and 3.19 per cent in 2001, though increasing annually (MOE, 2001; MOE, 2000).

Although the state appropriation for education increases annually, this increase cannot meet the increase in governmental budgets. The share of state appropriation plus earmarked education levies in the overall governmental budget has shown a clear, downward trend. In order to increase public expenditure as a proportion of GDP, the central government decided to increase its allocation to education by 1 per cent of its total budget of the previous year and to repeat this for five years from 1998 to 2002, which means that in the year 2002, 5 per cent more of the total central budget of the country will be allocated to education (Min, 2002).

Table 1.4 Public expenditure on education, 1996-2000

	1996	1997	1998	1999	2000
Total education expenditure (billion Yuan)	226.234	253.173	294.906	334.904	384.908
Public expenditure	167.117	186.254	203.245	228.718	256.261
State appropriation	121.191	135.773	156.559	181.576	208.568
Public expenditure as percentage of GDP	2.44	2.49	2.55	2.79	2.87
State appropriation plus earmarked education levies as percentage of governmental budget	16.28	15.67	15.36	14.49	13.80

Source: MOE in China, Statistics Yearbook of Chinese Education Finance, 1996-2000.

Note: Public expenditure includes state appropriation, earmarked education levies, support from school or university-affiliated enterprises and other public expenditures.

Diversification of sources for financing higher education

In the late 1980s and early 1990s, China began to explore more channels to mobilize the sources for financing education. According to the regulations of financing education in the Education Law implemented in 1995, the framework of sources for financing education is as follows. Public education expenditures are the major sources for financing education, in which the state appropriation is an essential feature. In addition, funds should be raised from non-public sources, especially through a cost-recovery and cost-sharing system of non-compulsory education. The potential of social organizations and individual citizens to invest in education should be explored.

At the present time, a higher-education financing system of diversification of sources has come into being. There are in all nine sources for financing higher education in China: state appropriation, earmarked education levies, tuition costs and fees, support from school or university-affiliated enterprises, donations from individuals and social organizations, educational foundations, research funding through competitive mechanisms, educational loans, and revenue from financial capital market operation (Min, 2001).

Data in *Table 1.5* give the total amount and proportion of expenditures for financing higher-education institutions by source. The data indicated that state appropriation was the most important source for financing higher education and it was increasing annually. In 1993, the state appropriation to higher education was 13.88 billion Yuan, while it reached 32.51 billion Yuan in 1999. The earmarked education levies and other public expenditures were also increasing from 1993 to 1999. Support from school or university-affiliated enterprises increased from 1.44 billion Yuan in 1993 to 3.28 billion Yuan in 1997, though it declined to 1.24 billion Yuan in 1999.

Meanwhile, non-public expenditures were playing an increasingly important role in the financing of higher education, tuition costs and fees increasing especially rapidly. The revenue from tuition costs and fees was only 1.04 billion Yuan in 1993, but reached 12.75 billion Yuan in 1999; this was a great increase. Donations increased from 0.12 billion Yuan in 1993 to 1.62 billion Yuan in 1999.

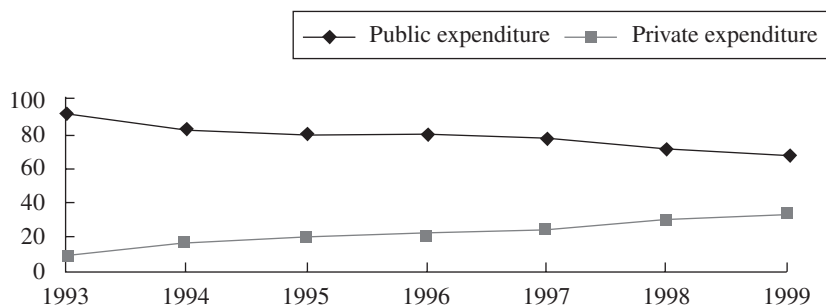
Table 1.5 Sources for financing higher education in China, 1993-1999

	1993	1994	1995	1996	1997	1998	1999
Amount (billion Yuan):							
1. State appropriation	13.88	16.07	18.24	21.07	24.41	25.68	32.51
2. Earmarked education levies	0.02	0.06	0.09	0.29	0.38	0.75	0.69
3. Support from school or university-affiliated enterprises	1.44	1.97	2.54	2.70	3.28	1.12	1.24
4. Other public expenditures	0.12	0.09	0.26	0.40	0.61	1.33	2.28
5. Donations	0.12	0.29	0.42	0.51	0.86	1.15	1.62
6. Tuition costs and fees	1.04	2.62	3.56	4.48	5.90	7.64	12.75
7. Other non-public expenditures	0.22	1.04	1.12	1.60	2.12	3.48	3.52
Total	16.84	22.14	26.23	31.07	37.56	41.15	54.61
Percentage distribution							
1. Public resources	91.81	82.16	80.56	78.73	76.36	70.18	67.24
2. Tuition costs and fees	6.18	11.83	13.57	14.42	15.71	18.57	23.35

Source: Statistics Yearbook of Chinese Education Finance, 1993-2000.

Revenue structure has also greatly changed in recent years. Public expenditure as a proportion of total expenditure was 91.81 per cent in 1993 declining, however, to 67.24 per cent in 1999. Meanwhile, tuition costs and fees as a proportion of total expenditure increased gradually from 6.18 per cent in 1993 to 23.35 per cent in 1999. *Figure 1.2* indicates that public expenditure as a proportion of total higher-education expenditure was declining, whereas private expenditure as a proportion of total higher-education expenditure was increasing, though the amounts of public and private higher-education expenditures were increasing annually.

Figure 1.2 Public and private expenditure as proportions of total higher-education expenditure



Source: MOE in China, Statistics Yearbook of Chinese Education Finance, 1993-2000.

Tuition for higher education in China

Chinese higher education has faced serious financial constriction since the 1980s. In order to fill the gap between financial demand and supply, the Chinese Government and the departments concerned have been trying to solve the problem through two methods: one was to enlarge financial resources and explore more channels to raise educational funds, and the other was to improve the utilization efficiency of educational resources. Among some channels of fund-raising, the implementation of cost-sharing and cost-recovery policy has been regarded as having theoretical support and practical value. The Chinese higher-education financing system changed from a government-dominated appropriation system without tuition and fees to a cost-sharing and cost-recovery system from the late 1980s. The rationale to charge for tuition is as follows: (1) to address the financial difficulties in the higher-education system, (2) to meet the private demand for higher education, (3) private benefits to higher education have been increasing over recent years along with economic transition, (4) some studies from the World Bank conclude that the system of cost-sharing and student aid is more equitable and efficient than the free-of-charge education system.

Chinese higher-education institutions were totally funded by the government before the implementation of the opening up and reform policy. The Chinese central government produced a document: *Decision on Reform Educational Structure*, in 1985. In this governmental document, the section related to tuition policy declared that higher-education institutions “could enrol a small number of students who would pay tuition and dormitory fees (self-supporting students)”. In fact, a few institutions began to put this soon-to-be policy into practice before 1985. From the mid-1980s to 1992, the two-track enrolment of public-supported and self-supported (tuition-paying) students existed at the same time in the Chinese higher-education system. The majority of students did not need to pay tuition and dormitory fees, but a small number did. In 1992, the State Education Commission of China proposed a one-track enrolment policy of charging all students tuition and dormitory fees. Since 1993, more and more higher-education institutions have changed the enrolment policy from two-track to one-track. In 1997, all regular higher-education institutions throughout the country charged students tuition and boarding fees. A cost-recovery policy has been implemented in all regular higher-education institutions in China. In other words, governments, students/parents, industries and philanthropists have started to share higher-education costs

since 1997. At present, about 25 per cent of total recurrent higher-education expenditure comes from students.

Tuition costs rose year by year along with the expansion of higher education and the increase of the operational budget of higher-education institutions. In 1997, the average tuition-cost level in regular higher-education institutions was 1,620 Yuan (1 US Dollar = 8.26 RMB Yuan), while the average institutional recurrent expenditure per student (unit cost) was 8,350 Yuan, and the number of students was about 3.17 million. In 1998, the average tuition-cost level increased to 1,974 Yuan, while the average institutional recurrent expenditure per student increased to 11,020 Yuan and the number of students was 3.41 million.

Although the reform of financing higher education to generate diverse revenues began before the great expansion of enrolments in 1999, the expansion of higher education in the three years of 1999-2001 accelerated the reform and raised the tuition-cost level. In 1999, the average tuition-cost level reached 2,769 Yuan, while the average institutional recurrent expenditure per student increased to 14,400 Yuan and the number of students was 4.17 million. As shown in *Table 1.6*, the average tuition-cost level increased 40.3 per cent from 1998 to 1999. In 1999, tuition cost as a proportion of GDP per capita reached 42.4 per cent, and tuition cost as a proportion of disposable income per urban resident was 47.3 per cent, while tuition cost as a proportion of net income per rural resident even exceeded 100 per cent and reached 125.3 per cent (Li and Min, 2001).

Table 1.6 The increase of tuition cost and its proportion of GDP per capita and income per resident, 1996-1999

	1996	1997	1998	1999
Tuition cost (Yuan)	1,319	1,620	1,974	2,769
Increase in rate of tuition cost (%)		22.8	21.8	40.3
Tuition cost as a proportion of GDP per capita (%)	23.7	26.8	31.3	42.4
Tuition cost as a proportion of disposable income per urban resident (%)	27.3	31.4	36.4	47.3
Tuition cost as a proportion of net income per rural resident (%)	68.5	77.5	91.3	125.3

Source: (1) Statistics of tuition and unit cost are from the Ministry of Education.
 (2) The computation to the proportions is from Li and Min, 2001.

Section 2

The development of the student financial aid policy

As the costs of higher education were shifted from the government to the students and parents, more financial aid for the poor students was needed. In China there is a series of financial aids, including grants, scholarships, work-study, student loans and so on.

2.1 Grants, scholarships, work-study and tuition-cost waiving

Grants

During 1949-1988, the people could receive ‘free’ higher education without paying tuition costs, and at the same time all the college students could obtain grants for their living expenses. With the expansion of higher education, government revenues were insufficient to provide grants to all students, so reform of higher-education finance was needed.

In 1989, the former State Education Commission, State Price Administration Bureau and MOF issued documents stating that undergraduates would be charged for tuition and living expenses (except for teacher training majors). With respect to sharing the cost of higher education, some students have difficulty in paying for their tuition and are in need of financial aid. Therefore, in 1993 the central government established ‘Subsidy funds for special needy students’; this step was expected to ease the difficulties of the poor students. However, this kind of aid is often awarded just in winter to help the needy students to survive the cold spell. Moreover, every eligible applicant receives the same amount of money, between 200-400 Yuan per person, so it is a small sum for the poor student. An alternative form of aid is to send quilts or padded coats to the poor students in winter.

The State Grants Foundation was established in April 2002 according to ‘Regulations on the State Grant Administration’ by MOF and MOE. State grants will be awarded to the academically deserving needy undergraduates in the regular higher-education institutions. Every year 45,000 students will receive grants at two levels, i.e. 10,000 students will

receive 6,000 Yuan per year and the remaining 35,000 students will receive 4,000 Yuan per year; at the same time these students are exempt from tuition fees for the same year. The assessment for the 'state grant' starts in September of every year, when the students submit applications to their institutions. The higher-education administration agencies check these applications and send the list of those to receive the state grant to the MOF. The MOF finally allocates the money to institutions. The state grant will be initiated in September 2002 (Liu and Lan, 2002).

Scholarships

In July 1983, MOE and MOF issued 'Regulations on temporary arrangements for grants and scholarships in regular higher-education institutions (RHEI)', which stated that scholarships would gradually replace grants. In July 1986, the State Council approved a 'Report on the reform of the grant system in RHEI'. From then on the scholarship became the major means of aid to the college students. Because the scholarship funds came from higher-education institutions' budgets, the institutions had little incentive to award scholarships. Moreover, as the scholarships were awarded on a merit basis and not on a needs basis, the proportion of students from upper or middle-income families who received the scholarship was much higher than those from lower-income families. As a result, the scholarships could not really resolve the financial difficulties of the poor students.

Work-study

In 1994, the State Education Commission issued 'Regulations on building work-study funds in regular higher-education institutions', which asked all institutions to construct work-study funds with the objective of helping poor students. At the same time, all central ministries, provinces and provincial cities were asked to match the funds to institutions under their jurisdiction. Students can earn 1.5-2.0 Yuan per hour through work-study, and the average amount is 80-150 Yuan per month. If, however, the poor students must use the money for living expenses, the sums are obviously insufficient. On the other hand, the unemployment ratio has been rising in recent years and the redundant workers have joined the competition, so the work-study posts are diminishing. The opportunities for work-study are therefore inadequate for the increasing number of poor students.

Tuition-cost waiving

Tuition-cost waiving is another important measure to aid needy students. In 1995 the central government began the policy of waiving or excusing tuition costs but only very few students can obtain this kind of aid, and more and more higher-education institutions are gradually cancelling this aid form.

Project: 'Access to higher education for the needy of the underdeveloped western region'

In 1997, universities and colleges put in place reforms with regard to tuition costs, and all students had to pay a higher proportion of instructional costs than that in 1989. This has proved particularly difficult for the students from the underdeveloped western areas. Accordingly, a project was established in 2000: 'Access to higher education for the needy of the underdeveloped western region'. Every year 1,200 freshmen from central or local key institutions in 12 western provinces (or autonomous regions or municipalities directly under the central government) will be chosen to receive financial assistance. The aid amounts to 20,000 Yuan over the following four years, and is allocated according to the academic year, that is to say, each student will receive 5,000 Yuan for every year. At the same time, the students receiving financial assistance pay only half of the tuition costs. In 2002 this policy incorporated new measures:

- the areas aided were extended to include some provinces in the middle region;
- the number of students assisted increased to 2,080;
- the aid criterion has not changed, but the students receiving financial aid need not pay for the tuition, which is exempted.

2.2 Student loans

The 'old' student loans (from 1986)

In July 1986, the State Council approved a 'Report on the reform of the grant system in regular higher-education institutions' and the Student Loans Scheme (SLS) was introduced in 85 institutions out of 1,954 existing at that time.

In July 1987, the SLS was extended to the whole country following on the document 'The implementation method of the Student Loans Scheme in REHI undergraduates'. The loan size was small, only up to 300 Yuan per year per student for living expenses, and the target group was the poor undergraduates. Individual institutions managed the SLS. The range of expected loan coverage was up to 30-35 per cent, but actually the ratios in most institutions were much lower than that percentage.

In September 1993, the government modified the policy. There were two reasons for the amendment. First, the price index and consumption level went up, which required increasing the average loan size. In addition, the maximum loan should be decided flexibly, taking account of local living standards set by local governments or basic living demands identified by institutions. It meant that the individual loan could exceed 300 Yuan per year. Secondly, the higher tuition cost meant that more poor students were unable to afford to pay for higher education. There was a need therefore to extend the coverage of loan-receiving students; the coverage rate should be decided flexibly, according to the number of poor students.

The amendments were originally aimed to improve the loan implementation. However, the two modified items were contradictory to each other. The first one seemed able to increase the average loan money but the second one, in fact, decreased the number of students who could receive the loan because the total loan fund did not increase. Only when loan funds are increased by institutions themselves, can individual loan money and the coverage rate be improved. Nevertheless, the amendment in 1993 offered a possibility for student loan diversity in various institutions. Some institutions increased the student loan percentage from the total expenditure of institutions, and increased the average loan to 800 Yuan (about US\$ 100) or over 1,000 Yuan (about US\$ 120) under the framework of keeping the same number of loan recipients.

To sum up, the Student Loans Scheme, in 1986, was managed by institutions, the average loan money was small, only 300 Yuan per year, that is to say, the student received only 25 Yuan per month; the repayment period was short and the loan had to be repaid before graduation. This caused some problems:

- some institutions, especially local institutions, were short of funds, meaning that poor students might find difficulty in obtaining a student loan;
- the average amount of loan money was too small to resolve the difficulties of the poor students;
- it was unfair to ask the students to repay their loan money before graduation, as it is known that most students have no earnings.

From *Table 2.1*, we can see that the coverage of grants, scholarships, SLS, work-study, tuition-cost waiving is small and declining; in fact the SLS and tuition-cost waiving has almost ceased. Most of the poor students cannot obtain sufficient financial aid, therefore ‘new’ loan schemes might be their last hope.

Table 2.1 Grants, scholarships, SLS, work-study, tuition-cost waiving in some RHEI in Guangdong Province in 2000 (unit: 10,000 Yuan)

RHEI \ Type	Grants to the poor	Scholarships	SLS	Work-study	Tuition-cost waiving	Total
Zhongshan University	118.0	616.5	570.0	80.0	24.0	1408.5
Zhongshan Medical Science University	60.0	127.5	0.0	11.0	1.2	199.7
Huanan University of S&T	39.0	454.9	0.0	119.0	0.0	612.9
Jinan University	8.6	195.2	0.0	38.8	0.0	242.6
Huanan Agriculture University	23.6	102.1	0.0	8.1	0.5	134.3
Guangdong Industrial University	2.0	301.0	126.0	180.0	0.0	609.0
Guangdong Business College	33.3	131.8	69.6	5.0	5.9	245.9

Source: Based on statistics of the Guangdong Education Bureau.

The 'new' student loans (from 1999)

(a) General-Commercial Student Loans Scheme (GCSLS)

In December 1999, the 'Regulation on Student Loans Administration' submitted by the three ministries (PBC, MOE and MOF) opened the General-Commercial Student Loans Scheme and its implementation started in the spring of 2000. The scheme applied to all post-secondary-education students and their parents or guardians. The target group was all students over 18 years old in higher-education institutions (including public and private institutions). The General-Commercial Student Loan (GCSL) has to be guaranteed, and students can borrow from local banks of the student's family location. The interest rates of the GCSLS are market interest rates without subsidy from the government. The purpose of the GCSLS is to extend student-loan coverage and to aim for a financially sound student loans scheme. The amount of GCSL a student can borrow is 2,000-20,000 Yuan maximum, which provides much more aid than does the GSSLS. The repayment periods are flexible because different commercial banks have different regulations. This kind of loan has its special advantages. First, the local banks are familiar with the situation of the students' families. The banks can easily contact the students or parents and they are not quite as worried about repayment defaults. Second, the poor students can apply the loans according to their needs, making full use of the limited funds. Third, the flexible repayment period fits in with the students' conditions more than that of the GSSLS and gives them more time to repay the loan, thus avoiding loan default.

Why are the commercial banks or rural corporative unions willing to hand out loans under the GCSLS with little intervention from the government and higher-education institutions?

- The commercial banks or rural corporative unions only lend to local citizens (students or parents) who have permanent residence. It is convenient for the banks to communicate with borrowers and it is easy to track the students or their parents. In addition, the collection cost for the banks is much lower.
- The second reason is that the GCSL is guaranteed through the assets of parents/guardians, thus the possibility of default can be minimized and the risk for the banks is lessened.

- Thirdly, the banks are familiar with the economic status of students' families; they can choose to give loans to the financially secure borrowers. Moreover, usually the parents of the college students are their former customers or borrowers, i.e. there often exist relationships between the banks and the parents of the students, and the banks expect to expand their business.

Some problems exist in the GCSLS. The access to loans is unequal. The GCSLS is targeted more on the students from middle- or upper-class families than from the lower-income families in rural areas, because the families of the needy students cannot mortgage assets for the loans. The banks tend to loan money to the financially secure borrowers (not poorer students). So the GCSLS cannot quite enhance the equity of opportunity.

(b) The Government-Subsidized Student Loans Scheme

In May 1999, the 'Regulation on Government-Subsidized Student Loan Administration' was proposed by the People's Bank of China, MOE, and MOF. The government-subsidized student loan initiation was a pilot loan scheme in central institutions in the eight cities of Beijing, Shanghai, Tianjin, Chongqing, Wuhan, Shenyang, Xi'an, and Nanjing. The students who apply for the loan need guarantors, they have to adopt a commercial interest rate with 50 per cent of the interest subsidized by government finances, and the repayment term is four years after graduation.

In December 1999, a 'Regulation on Student Loan Administration' by the three ministries was based on government-subsidized student loan practice in eight cities in the autumn semester of 1999. The 'Regulation' states that the government-subsidized student loan takes a student's individual credit as a loan guarantee, and cancels the higher-education institutions' responsibility for repaying defaulted loan and interest which they were required to do previously by the 'Administrative Regulation on the Government-Subsidized Student Loan' proposed in May 1999. All needy students can therefore use their own credits to apply for student loans.

In August 2000, the 'Supplemental Regulation on Student Loan Administration' extended the GSSLS testing from eight cities to nationwide practice. The original bank, the Industrial and Commercial Bank of China, was replaced by four state-owned commercial banks: Industrial and Commercial Bank of China (ICBC), China Construction Bank (CCB), Agricultural Bank of China (ABC), and Bank of China (BC) to carry out

the business. The target group was extended from undergraduate level to both undergraduates and postgraduates.

In June 2001, the National Conference on Government-Subsidized Student Loans was held in Beijing. The modifications made were favourable to the lending banks because, generally speaking, the banks were instrumental in slowing down the GSSLS, compared with the attitudes of governments, institutions and students. The changes included cancelling the rule of 'one bank to one institution', to be replaced by the policy of one institution to multi-banks, exempting the banks from business taxes on GSSLS, and cancelling the 'dead debt' of defaults after verification.

In March 2002, the 'Regulation on Improving the GSSLS', with amendments to GSSLS policy, was released by the People's Bank of China, MOE and MOF. This requires that every RHEI should find a lending bank and that the loan coverage and loan size should reach a certain level. The central government expects to expand the GSSLS through these measures.

From the year 1999 to now, the GSSLS has seen many modifications following the changes in the country and the development of higher education. It possesses three advantages:

- The commercial banks are responsible for the GSSLS, which gives banks more power to operate the scheme.
- The regulations on the maximum loan money and ratio of receiving-GSSLS students protect the interests of students and ensure that the poorer students receive a GSSL which is sufficient for their needs.
- Lending banks will be exempted from business taxes on the student loans. The 'dead debts' of the loan defaults will be cancelled and the government would bear some of the loss from defaults.

As every coin has two sides, the GSSLS has found many difficulties in operating, shown mainly by four points:

- The banks would like to grant loans to the students having the most ability to repay the loan on time, but many poorer students do not come into this category (details in the following analysis).

- It has not yet established an exact criterion of what is a ‘poor’ student, which means that banks face many difficulties in deciding whether or not to grant a loan. This lack of clear guidance therefore tends to blunt the banks’ enthusiasm.
- Cancellation after verification is a kind of financial disposition taken by banks for the dead debt. GSSLS lending banks are all state-owned, so the cancellation of the dead debt must be authorized by the government. But the way of handling dead debt does not necessarily work to the banks’ advantages. The process is complicated and time-consuming for the banks. And even if the dead debt is cancelled after a very strict verification, it does not mean that the banks could get the principle back. In fact, the cancellation of the dead debt only enables banks to remove some bad assets in order to avoid further losses caused by the dead debts. The loss produced by dead debt will still exist, and nobody will pay for it, including the government, although banks will receive approval to use a different series of means to deal with it. And usually, the banks are expected to use their own profits to cover the loss.

(c) Some different features between the GCSLS and the GSSLS

There are certain different features between the GCSLS and the GSSLS.

- Their target groups are different. For GCSLS, all students who have enrolled in higher-education institutions or their parents are eligible. In practice, most of the GCSLS go directly to the parents/guardians of the students. For the GSSLS, only the poor students in regular higher-education institutions are eligible for GSSLS, and the loans go to the poor students.
- Their lenders are different. For the GCSLS, not only the state-owned banks but also the other commercial banks and credit cooperative unions are encouraged to give commercial student loans. The Rural Credit Cooperative Union, consisting of local rural financial institutions, is the major provider of GCSLS. For the GSSLS, only four state-owned banks participate.
- Their interest rates are different. The interest rates for the GCSLS are at commercial interest rates. The government provides no subsidy

for the GCSLS, while for the GSSLS the government subsidizes half of the interest rate. But the commercial banks or rural credit corporative unions participating in the GCSLS can obtain preferential tax treatment from the government for their lending to students.

- Their maximum amounts of individual loan are different. The maximum of GCSLS is much larger than that of GSSLS. For GSSLS, it has been 8,000 Yuan for an academic year (6,000 Yuan as of fall 2002) but for GCSLS it is 20,000 Yuan.
- The guarantee requirements are different. Loans for the GCSLS are co-signatory in nature, and they have to be guaranteed with assets by the parents. The GCSLS is not as strictly means-tested or needs-based as the GSSLS, and the GSSLS guarantee requirement consists of just the student's own credit.

A brief outline regarding the student loans schemes in China is given in *Table 2.2*.

Table 2.2 Student loans schemes in China (unit: Yuan)

	SL	GSSLS	GCSLS
Starting time	1986	1999	2000
Scope	National (1986 testing, 1987 nationwide)	National (8 cities, nationwide from Aug 2000)	Nationwide
Target group	Full-time, poor undergraduates in RHEI ¹	Full-time, poor undergraduates and postgraduates, in RHEI	All students over 18 years old in higher-education institutions
Public/private	Public	Public	Public/private
Type	Living expenses loan	Tuition loan for undergraduates, living expenses loan for postgraduates	Tuition, living and study expenses
Maximum/year (Yuan)	300 (1986), 800 (1993)	8,000 6,000 from 2002	2,000-20,000
Administration⁴	Institutions	4 state-owned banks	Commercial banks

Fund providing	Institutions	Banks	Banks
Interest rate	0	Commercial rate, government subsidy 50%	Commercial rate, non-subsidy
Repayment period	Policy: 6 years after graduation. Practice: before graduation	4 years after graduation	Various by banks
Legal basis	Governmental 'report' ³	Governmental 'regulation' ⁴	Governmental 'regulation' ³
Guarantor	Parents	Without co-signature	Parents
Sanction	Institutions keep diplomas	Publish defaulter name	Like mortgage loans
Features	High repayment, low risk, small size	High repayment risk	Big funds, lower risk, not only for the poor
Money accumulated by June 2002	n/a		n/a
[1] Approved by banks		[1] 3 billion	
[2] Allocated factually		[2] 1.7 billion	
Number of borrowers accumulated by June 2002	n/a		n/a
[1] Approved by banks		[1] 351,000	
[2] Received factually		[2] 327,000	

1. RHEI: Regular Higher-Education Institutions.
2. Administration includes loan distribution, applicants' eligibility review, loan collection and repayment.
3. Governmental report: *Report on reforming the grant system in regular higher-education institutions*, July 1986.
4. Governmental regulation (document): *Regulation on Student Loan Administration*, 23 December, 1999.

2.3 Summary

From the development of student financial policy, described above, the following are the main points:

- With the expansion of higher education and economic reforms, the central government reformed higher-education financing, including the system of financial aid to students.
- Student financial aid takes five forms in China: grants, scholarships, work-study, tuition-cost waiving, and student loans.
- Because of the introduction of tuition fees in higher education, and the spread of higher education, the existing system of financial aid was insufficient to cope with the difficulties of the poorer students. The central government therefore issued the new Student Loans Scheme (incorporating GSSLS and GCSLS).
- To make the GSSLS more workable, the central government made several amendments to it, including legislation on loan limits, repayment period etc. These changes have achieved good results, but the GSSLS still has certain problems that need to be resolved.

Because the GCSLS cannot reach the most needy students and cannot greatly improve poorer students' access to higher education, the government focuses more on the GSSLS. The government and the higher-education institutions are not as involved in the GCSLS as they perhaps should be. Now, it appears that accurate data on the GCSLS are unavailable and it is likely that the GCSLS will decline with the growth of GSSLS. Therefore, the report focuses on the GSSLS in China.

Section 3

Objectives of the Government-Subsidized Student Loans Scheme

3.1 The general objectives of the student loans scheme

The student loans scheme is a method widely used all over the world to aid needy college students. The policy is not oriented towards a single purpose, but is a kind of multi-objective operation. The general objectives of the world's current student loans schemes are as follows (Ziderman, 2001):

- facilitating the expansion of higher education;
- cost sharing and cost recovery;
- easing the financial burden of both the country and the students attending colleges;
- improving the equality of access to higher education;
- increasing the human capital.

3.2 The special objectives of the GSSLS

Demographic and geographic background

It is well known that China has a huge population. Today, the population of China is about 1.3 billion, and exceeds 20 per cent of the world's population. There is no doubt that the enormous population brings a heavy burden to the education system in China, especially for the higher-education system. Furthermore, the people's demand for higher education will increase substantially in the process of mass higher education. This means that there will be a violent impact on the Chinese higher-education system in the future.

There are great differences in geographic features between the western and the eastern parts of China. In addition, the population

distribution has an imbalance; the population in the east is much higher than that in the west. On this foundation of the geographic and demographic diverse characteristics of China, its economy shows an unavoidable imbalance, which appears not only between the west and the east, but also within each area. Generally speaking, the economy in the east of China is much better than that in the west of China, and the economy in the cities is much better than that in the rural areas. But even in cities, there is still a big income gap between rich and poor. This kind of imbalance creates large obstacles for the widespread modernization of China.

At present, the poor students, who mainly come from rural families and lower-income families, account for 20 per cent of the total number of students in the RHEI of China, and the most needy students account for 5-7 per cent (Jiao, 2001). According to a survey sponsored by the MOE at the end of 2000, there are about 5,600,000 undergraduate students. This means that there are about 1,120,000 poor undergraduate students, and 280,000-392,000 most needy students in the higher-education institutions of China.

Special objective 1: Helping the needy students to gain access to higher-education institutions and continue their studies

In the process of transition from the tuition-free policy to the higher-tuition policy, an important issue to be considered is how to ensure that those students from poor families will register in the colleges and universities and how to enable them to complete their education smoothly. This issue is related not only to the educational equity, but also to the stability of higher-education institutions and the whole society. China is a socialist country, thus ensuring that everyone has equal opportunity of education should be one of the most important goals of the current political system.

In order to solve this problem, the GSSLS was implemented from 1999 according to the 'Regulation on Government-Subsidized Student Loan Administration' jointly formulated by the PBC, MOE and MOF:

'The Government-Subsidized Student Loans Scheme is intended to help those really needy students to pay for the tuition and daily living expenses while studying; it also plays an important role in supporting education by financial means and aiding the

needy students to complete their education' (PBC, MOE and MOF, Administration Regulation, 1999).

As described above, the GSSLS is an important measure to ensure educational equity and maintain social stability, and is also an effective way to settle the contradiction between “the expansion of the higher-education scale” and “the fact that many poor students cannot afford to pay for their education”. It can help many young students, especially those financially needy students, to gain access to higher-education institutions and to complete their education smoothly. It is clear that a very important purpose of the GSSLS is to aid those students who are disadvantaged and suffer unfavourable conditions, to complete their education.

Special objective 2: Supporting education by financial means

Although many countries in the world have already resorted to financial and market means to regulate higher education, China has still preserved its traditional planned appropriation model due to the influence of the planned economy. In other words, the higher-education financing is still in a kind of ‘government-controlling’ mode, which is opposed to the ‘cost-sharing’ model initiated by Professor D. Bruce Johnstone in 1986. The funds for the student loans also came mainly through government appropriation until 1999. The problems caused by this model severely hindered the reform of the higher-education system, whereas by applying the flexible financial means of the market economy to aid the students, there is now a real breakthrough in higher-education financing reform.

For the reasons mentioned in Section 1, the government could not invest sufficiently in education and face the immense financial burden from such widespread aids as scholarships and grants offered to all poor students. As for the GSSLS in China, the funds are provided by state-owned commercial banks and the central and local governments offer the subsidized interest rates. The state-owned commercial banks lend and collect the loans. If this scheme works well, China can overcome the obstacles caused by its limited educational resources, help more students to accomplish their education and thus promote the development of higher education with the help of the non-governmental revenues. At the same time, the ‘financial’ features of loans can give full play to the limited capital. Commercial banks have experienced staff to administrate the capital and operate the loans scheme, so that it will be more effective and efficient

for banks to manage the whole loans scheme independently. In this sense, the student loans scheme and its administrative model prove effective in the following aspects: making the fullest possible use of the social capital, benefiting the largest possible segments of the population, increasing the efficacy of the capital, easing the financial burden of the government and ultimately enhancing the development of higher education. It is no exaggeration to say that the GSSLS is a new and worthwhile effort by the government to support education by financial means; it is also the most efficient way to aid the poor.

Special objective 3: Helping to cultivate the students' awareness of independence and self-support

It is very beneficial for young students to apply for student loans with their own personal credits. Student loans cannot only help poor students to invest in human capital, they can also help the students to establish their own credit records and cultivate their awareness of self-support. Although they have to repay the loans with their own future earnings, they can be well prepared and sufficiently qualified because of the education they receive; they are actually the beneficiaries of both the education and the loans. The student loans also have a great social impact in helping to propagate some related financial and legal knowledge, as well as strengthening the awareness of credits of both the students and the public. The student loans are especially favourable to those extremely poor families in urban and rural areas. With the help of the student loans, students from these families can complete their education more easily.

Special objective 4: Helping to establish a system of individual credits in the whole society

In China, a nationwide credit system has not yet been established. The GSSLS, therefore, has a quite special goal: to help to establish an individual credit system by recording the credit history of the borrowers. With the help of the governments, the lending banks distributing the student loans can explore an effective administrative model of individual consumption credits and extend the experiences in this field to the administration of other types of loans. With the development of the national economy, people's living standards will be higher; the national credit system will be improved and people's awareness of individual credits will be stronger. This will help in the development of the individual consumption

credits and the individual short-term, small-sized loans. The banks in China will increasingly grant credit loans to individual citizens, and they will have more possibilities to make profits; nowadays, such loans in China are still on quite a small scale. Apart from the student loans, another important type of credit loan is the individual short-term, small-sized loans, which are directed mainly to those groups with a stable income and very limited mobility, such as the civil servants in the governments and public security units. What kind of angle should we look at to consider the individual credit guarantee? On the one hand, it represents a future tendency. In the future, competition in the banking business will be increasingly fierce and the individual credit loans will become the focus of competition; on the other hand, the implementation of student loans expands the business of individual credits, the banks can thus accumulate valuable experience and also explore an effective administrative model of individual consumption credits.

The state-owned banks in China have already realized that individual consumption credits (including the student loans) have a great potential market. As pointed out by Mr Gang Xiao, the Vice-President of the People's Bank of China, the implementation of student loans encompasses not only the practical needs of young college students, but also the objective needs of expanding the business of individual consumption credits (Xiao, 2001). In order to promote the national student loans, banks have made worthwhile efforts; they have also expressed their willingness to intensify this business to meet the objective of 'reviving China through science and education'.

3.3 Summary

Higher education is a costly kind of business. The needy students cannot pay the tuition and living expenses. With the spread of higher education, this problem will become more and more serious because the number of the needy students will increase sharply. It is very important to give equal opportunities to those students with lower socio-economic status. To solve this problem, more and more countries have to resort to student loans, including China.

The GSSLS was designed to help the Chinese needy students to finish their higher education. In addition, the GSSLS is expected to remove part of the financial burden of higher education and part of the burden of the government.

Moreover, as was mentioned in the beginning of Section 3.2, China shows an imbalance in many fields such as population, the economy, medical care and education. Through the GSSLS, the needy students may finish their higher education more easily, and higher education can help them to find higher-income jobs and put an end to poverty. Therefore, it can be said that the GSSLS can help to lessen the imbalance between the poor and the rich and to promote the stability of the society further. In other words, it can prevent the ‘Matthew effect’ to some extent, which makes the rich richer and the poor poorer.

Section 4

Implementation procedure of the Government-Subsidized Student Loans Scheme

4.1 Organizational structure of the GSSLS

Our study will focus on the RHEI because the GSSLS provides loans only for these higher-education institutions. By the end of 2000, undergraduates in these higher-education institutions totalled 5,600,000, and the needy students accounted for 1,120,000, statistically about 20 per cent of all enrolments (National Centre, Proceedings, June 2001a). The number is still increasing with the expansion of higher education.

The administrative organization of the GSSLS in China consists of three parts: the government loans administration system (composed of the Central Leading Group and the National Centre for the Administration of GSSLS, the local leading groups and local centres for the administration of the GSSLS), the higher-education institutions, and the banks. These three components function together in the student loan administration (*Figure 4.1*).

Government loan administration system

(a) Central leading group

The central leading group is mainly responsible for handling relations between MOE, MOF and PBC, making policies and national plans of student loans, holding related workshops, and announcing policy decisions.

The functions of the three ministries are as follows: MOE is responsible for the student loan policy, made according to the national education-development conditions; MOF raises and allocates the subsidized interest funds to higher-education institutions affiliated to the central

ministries and supervises the arrangement of these funds; the People's Bank of China appoints the undertaking banks, confirms the operational procedures and supervises the operation of the student loans; the lending banks are mainly involved in ratifying, allocating and collecting the loans.

(b) National Centre for the Administration of the GSSLS

The National Centre is the standing organization of the above-mentioned leading group. Its office is located in the MOE and it handles many complicated tasks:

- signing contracts regarding student loan administration with the headquarters of the lending banks;
- providing annual national guidelines for student loans, receiving and ratifying the loan application reports submitted by the RHEI affiliated to these central ministries, checking and deciding the loan size for each institution affiliated to central ministries, reporting all the related information to the headquarters of the lending banks;
- administering all the student loan interest-subsidy funds allocated to the higher-education institutions by the MOF, receiving domestic and overseas donations for student aid, enlarging the resources of the subsidized-interest funds, depositing all the interest-subsidy funds quarterly into the lending banks, according to the actual loan transactions of the banks;
- providing the banks with related information, helping the banks to supervise and manage the operation of the loans, helping the banks to recover the loans;
- directing the local centres; reporting its work to the central leading group and handling other affairs assigned by it.

(c) Local leading groups of the provinces, autonomous regions and the municipalities directly under the central government

Based on decisions of the central leading group, the local leading groups also make and announce some related policies, direct and administrate the operation of student loans in their regions, handle the

relations among the education system, the local government financial system, the banking system and all the higher-education institutions involved; provide annual guiding plans for the higher-education institutions.

(d) Local Centre for the Administration of GSSLS

The Local centres are the standing organizations of the provincial leading groups; their duties are very similar to those of the National Centre:

- signing contracts regarding student loan administration with the local lending banks;
- providing annual local guiding plans for student loans, receiving and ratifying the loan application reports submitted by the local higher-education institutions, checking and deciding the loan size for each institution affiliated to the local governments, reporting all the related information to the lending banks;
- administering all the student loan interest-subsidy funds allocated to the higher-education institutions by the local government, depositing all the subsidized interest funds once per quarter into the lending banks, according to the actual loan transactions of the banks;
- providing the banks with related information, helping the banks to supervise and administer the operation of the loans, helping the banks to recover the loans;
- providing statistical data to the national centre, reporting to the local leading groups and handling other affairs assigned by them.

University Loan Offices

Each institution should have a special administrative office to handle all the business with regard to student loans. The loan officers in the universities are usually the staff with experience in student loans or student affairs. Some higher-education institutions have yet to establish the offices. The duties of the office personnel are as follows:

- signing contracts regarding student loan administration with the lending banks;

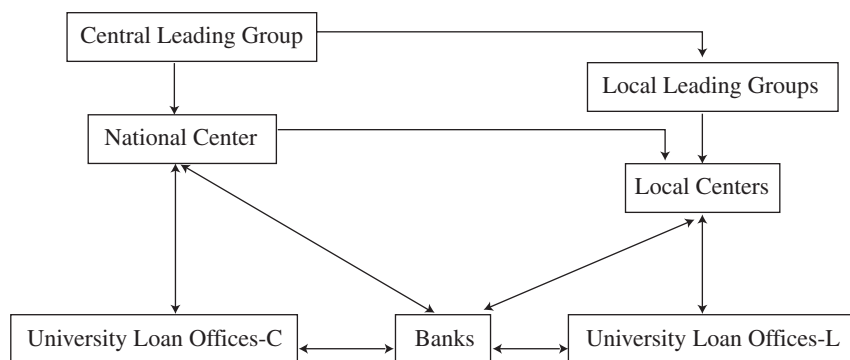
- conducting preliminary evaluation on the eligibility of the loan applicants of the higher-education institutions;
- submitting the annual loan application reports to the relative administrative offices on a regular basis;
- sending the ratified loan application forms to the lending banks;
- helping the banks to allocate loans, collect the loans and press for the loan repayment;
- providing timely statistical data on the changing situation of the students (such as employment, further study at graduate level, transfer to another institution, or drop-out) and the actual operation of the loans to the central or local centres for student loan administration; submitting statistical reports to the national centre or local centres and handling other affairs assigned to them.

Lending banks

Four state-owned commercial banks undertake the GSSLS. Each bank has its headquarters, with thousands of lending banks and their branches. The lending banks are under the jurisdiction and supervision of the People's Bank of China. Their duties are as follows:

- deciding the specific administrative procedures for the student loans according to national policies;
- signing contracts with each institution involved in the loan schemes, checking and ratifying the individual loan applications submitted by the higher-education institutions, then deciding whether to allocate the loans or not, signing loan contracts with the students;
- allocating and collecting the loan funds; deciding whether additional loan funds should be allocated according to the conditions of recovery and co-operation among the organizations.

Figure 4.1 Organizational structure of the GSSLS



Notes:

University Loan Offices – C: University Loan Offices of the higher-education institutions affiliated to the central ministries

University Loan Offices – L: University Loan Offices of the higher-education institutions affiliated to local governments

Banks: The whole banking system involved in the GSSLS.

4.2 The main features of the GSSLS

The targeting, guarantee and repayment term of the GSSLS

(a) The target groups of the GSSLS: the poor students

As is prescribed in the ‘Administrative Regulation on Government-Subsidized Student Loans’, “the Government-Subsidized Student Loans Scheme is intended to help those really needy students to pay for the tuition and daily living expenses while studying”, the ‘loan recipients’ should be “those students whose income and their families’ income during the process of studying cannot afford to pay their basic expenses” (including both the tuition cost and the basic living expenses).

In China, we generally recognize those students with family income below the local lowest living standard (poverty line) as needy students. Each local government decides the specific poverty line. In the operation process, the loaning banks usually demand that the students present a family ‘economic condition’ testimonial, that is produced by the local

government of their family's residence, to justify their eligibility to apply for the loans.

Since the risks are quite sizeable, it is impossible for the banks to provide excessive amounts for the student loans. Therefore, the limited number of loans that are available should go to those most needy students. Of course, it is also very difficult to judge who are really needy and to identify their degree of poverty. Accordingly, in the process of verification of eligibility, despite the family 'economic condition' testimonial, the university loan officers and the bank clerks mostly depend on their experience to judge the applicants' eligibility. Most important is that the banks really trust the university loan officers' judgement, because it is easier for the university loan officers to pinpoint the real background of the students. If an applicant can pass the audit of his/her university loan officer, he/she will obtain the loan in all probability.

(b) The guarantee mechanism of the GSSLS:
students' individual credit

The current loan practice in China counts on the students' individual credit as the guarantee, no other mortgage or warrantor is demanded, so the banks are faced with quite sizeable risks. It is thus necessary to establish a system of personal credits to accommodate and efficiently administrate this kind of credit loan. In China, the credit loan system is yet to be developed, because national and local systems of credit records have not been established to date. It was said that except for Shanghai, no other provinces or cities have set up such credit systems as personal credit records and credit accounts, so the banks still cannot effectively restrict the borrowers. College students are usually very mobile and difficult to track after their graduation, and as the banks cannot restrict them through the credit system, the banks have to shoulder quite tangible risks when the repayment period and repayment size are taken into account. It is very hard to predict default rates and the feasibility of the long-term operation of this system.

When students borrow money from banks on their own individual credits, in fact the government guarantees the student loans. The GSSLS in China carries this loan. As the warrantor, the government should take related financing responsibility and default risk. However, most of the responsibility and the risk of the GSSLS are taken by the banks. In China's case, the loan funds are raised by banks and the collection of loans is also

conducted by banks. It is a rather complicated ‘theory-and-practice’ issue, needing investigation, and it will be the next stage of the study.

(c) The repayment period of the GSSLS: four years

According to the regulations of the national Student Loans Scheme, students should repay both the principal and the 50 per-cent interest on the loan in four years after their graduation. This also means quite sizeable risks to the students, because they will have to enter the repayment period immediately after graduation. They are not sure whether they can graduate on time, they cannot predict what kind of job they will take and what their income level will be after employment. Moreover, they need quite a lot of money for their living expenses, social activities and certain basic items then. The short repayment period to some extent reinforces the uncertainty of the repayment expectations and thus increases the difficulty of repayment, together with the possibility of repayment default.

We find that the shorter the repayment period, the heavier the risk of defaulting on the loan. The reason is quite simple. If the repayment period is longer, the ability of the student to repay is stronger, the possibility of loan return is higher, the amount of pay-back to the loan fund is larger, so that if the loan scheme can be run in a long-term perspective, more students can receive the benefit. The point is that a repayment formula based on China’s particular condition must be designed and the formula will include the starting repayment time, the reply rate based on loan recipients’ income or on loan amount by year, and finishing repayment time and so on. It is future, continuing work to keep in mind for the study.

Interest rates of the GSSLS

(a) Adopting the same interest rate as the commercial loans within the same repayment term

According to the regulations of the People’s Bank of China, the rates of the GSSLS are the same as those of the commercial loans within the same repayment term. The current interest rates are: within six months (including 6 months): 5.58 per cent; six months to one year (including 1 year): 5.85 per cent; one year to three years (including 3 years): 5.95 per cent; three years to five years (including 5 years): 6.03 per cent; longer than five years: 6.21 per cent. The Student Loans Scheme is also adopting this rate standard. It is easily seen that the student loans are not low-

interest loans at all; on the contrary, the rates are even higher than for the commercial housing loans (the interest rates of the individual housing loans are: one year to five years: 5.31 per cent; longer than five years: 6.03 per cent). Student loans in other countries often have zero interest or very low interest rates. For example, in Japan, Germany and some developing countries of Asia, Africa and Latin America, the student loans are interest-free; low-interest loans are widely operated in other countries. Another kind of student loan in Japan has applied a low interest rate, which is of 3 per cent; in Singapore, the interest rate of the 'Student Loan Funds of the Central Reserved Funds' is also 3 per cent; in Hong Kong, the annual interest rate of the student loans is 2.5 per cent. In some countries, the 'most favoured interest rates' are adopted for the student loans; this takes the possible risks into full consideration and yet still allows the banks to make some profit. In China, the commercial interest rates adopted for the student loans are quite high, but the actual rates paid by the students are also very favourable since the government provides a certain proportion of interest subsidy (the central financial authority offers 50 per cent of interest subsidy to students from the higher-education institutions affiliated to the central government ministries; the local financial authorities offer a certain percentage of interest subsidy to students from local higher-education institutions, with the percentage of the central financial authority offered as a reference). Because the funds for student loans in China are provided by the commercial banks, the direct purpose of maintaining the same interest rate is to reduce the risks to the banks, ensure that banks can make some profit from the loan lending and stimulate their enthusiasm for participating in the loan business.

(b) The inequity caused by the unitary interest rates

Compared with student loans schemes in other countries, China did not offer different interest rates to students from different economic backgrounds, although generally speaking, the extremely poor students need more aid than other needy students. In the USA, the interest rates of the student loans are diverse in different loan programmes according to the various economic situations of applicants. For example, the interest rate for the Perkins Loans Programme is about 5 per cent, while the interest rate for the Stanford Loan Programme is about 8 per cent. The student loans schemes in China also did not take the majors of the students into consideration, but according to the income-expectation theory and the return rate of higher education, the students studying popular majors

can earn much more after graduation than those who study common or even unpopular majors. In this sense, the policy of unitary interest rates will undoubtedly lead to inequity for students from different backgrounds and for the students with different income levels after graduation.

(c) The risks caused by the fixed interest rates

At present, the interest rate of banks in China is a kind of regulated rate. The Central Bank of China (People's Bank of China) has the power to regulate all the important interest rates for the commercial banks in China. All of the commercial banks should adhere to these rates set by the People's Bank of China and none of them have the right to establish their own interest rates according to the market circumstances. Obviously these fixed rates may not conform to the market interest rate. Therefore, the commercial banks unavoidably have to bear the interest risk when the lending interest rate is lower than the market interest rate. Moreover, once the student loan contract is signed, the interest rate is then fixed according to the commercial loan interest rates of the time and will not undergo any changes over the period of the contract. If the market interest rate or the lending interest rate of commercial banks change during this period, the banks will bear another kind of interest risk.

The administration model of GSSLS and its characteristics

(a) The administration model of the banking system

According to the Administration Regulation on the Government-Subsidized Student Loans Scheme:

“The specified tasks of allocating, administering and collecting the GSSLS funds are conducted by the undertaking banks. The student loans are also a kind of general commercial loan and should be administrated in the same way as the commercial loans” (PBC, MOE and MOF, Regulation, 1999).

This means that the state-owned commercial banks in China apply the same administrative method to monitor the student loans. The loan funds come from the banks' own credit loan funds, so the banks must take the profitability, security and circulating possibility of the funds into consideration. They not only must conduct many detailed tasks for the student loan businesses, but they also have to shoulder great responsibilities in recovering the loan funds.

In order to ensure the smooth implementation of the student loans scheme, certain special-purpose organizations, such as leading groups, have been established in China. In fact, they only play a role in guiding and helping the banks, but seldom conduct the specified administrative tasks in the loan businesses. The real functions and responsibilities of the national centre and the local centres have not been sufficiently defined; they are requested to help and guide the banks, but very little is mentioned on how to guide, how to help, how to administer. The responsibilities of the higher-education institutions in the implementation of the student loans are comparatively more definite, but they only play a supplementary role because they are not responsible for the security of the loan funds. To sum up, the administration model of student loans in China can be reasonably described as a banking administration model, with the guidance and participation of the higher-education institutions and other special-purpose organizations.

(b) Characteristics of the model

Most of the administrative costs are borne by the commercial banks. Undoubtedly, by undertaking the student loan business banks will pay large amounts in administrative costs, but no subsidy is offered and the banks must shoulder these costs.

The lending banks are all state-owned commercial banks. Only four state-owned commercial banks are authorized to lend the GSSLs. There are many advantages to having the commercial banks run the student loans scheme, such as: reducing the financial expenditures of the governments, comparatively lower costs and higher efficiency. We can therefore consider it as an effective model. But the student loan businesses also bring heavier workloads, higher risks, less profit-making possibilities and more social responsibilities to the banks, thus not many banks are willing or courageous enough to conduct this kind of business.

4.3 Implementation of the GSSLs

GSSLs funds

The GSSLs lending banks are appointed by the People's Bank of China; there are currently four state-owned commercial banks involved in the loan operation: Industrial and Commercial Bank of China (ICBC),

China Construction Bank (CCB), Agricultural Bank of China (ABC) and Bank of China (BC). The student loan funds are raised by the banks themselves and occupy a certain proportion of the banks' credit funds.

Application and distribution of the loans

As mentioned in Section 1, the higher-education institutions in China can be divided generally into two kinds. One is the higher-education institution affiliated to central ministries, the other is the higher-education institution affiliated to local government. As far as the flowchart of the allocation and distribution of the GSSLS funds is concerned, there exist some slight differences between the higher-education institutions affiliated to the central ministries and the local higher-education institutions, as shown in *Figure 4.2*. We will outline these differences in the following paragraphs.

(a) The quotas of the GSSLS

The quotas here are the limits of the loan volume. It is just a guide or plan produced by the government. Usually the total amounts of loans cannot exceed the quotas because the funds to subsidize half of the interest rate are appropriated according to the quotas. The lending banks can use it as a reference to decide their own loan volume. The establishment of the quotas for the GSSLS is a complicated matter. At the very beginning, the central leading group will make national plans for student loans. Then, the national centre or local centres will produce annual national guidelines for student loans accordingly and will communicate these guidelines to all the higher-education institutions and the lending banks. At the same time, the loan offices of higher-education institutions make their annual loan-application reports to the relative administration offices, on a regular basis, according to the guidelines and their own situations and submit them to the national centre/local centre. It is up to the national centre/local centre to check the reports and decide or confirm the specific loan size for each higher-education institution. Once the loan amount for each higher-education institution is authorized by the national centre or local centre, it will be the final quota for this higher-education institution. All the authorized loan amounts for the higher-education institutions form the whole sum of quotas of the GSSLS. The quotas of the GSSLS will be reported to the lending banks as an important policy parameter of the loan funds they grant.

(b) The application procedure

There are five main steps in the application procedure:

Step 1. Before the start of the application procedure, the university loan offices or the lending banks should provide several training lectures for all the applicants, or at least once for each higher-education institution.

Step 2. After that, the application forms will be distributed to the students. With the guidance of the loan officer from whatever university or lending bank, the applicants will correctly complete the forms and then the university loan offices will collect them.

Step 3. The university loan officers will conduct preliminary evaluations on the eligibility of the loan applicants, mainly according to the information on the economic status of the applicants' families, and send the ratified loan-application forms to the lending banks.

Step 4. The banks will check and ratify the individual loan applications submitted by the higher-education institutions, and then decide whether to provide the loans or not. Incidentally, the verification of lending banks is mainly focused on any technical errors in the application forms. The most important task of their audit is to control the gross amount of loan funds granted to the higher-education institution according to the quotas.

Step 5. Once the lending bank accepts an application, it will sign a loan contract with the applicant. However, the applications are dealt with by the bank in batches, regarding each higher-education institution as a unit.

(c) Loan granting

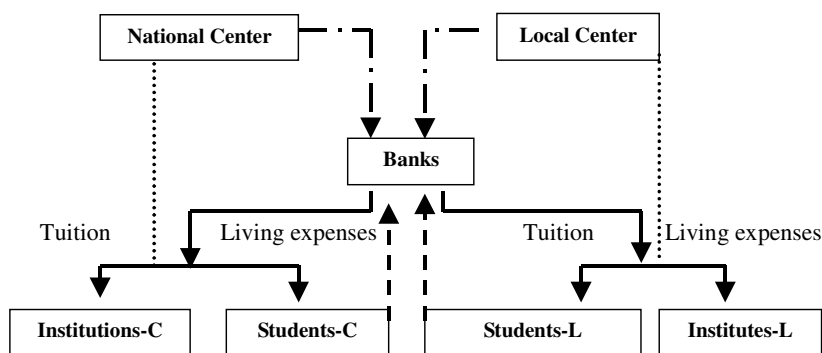
Once the credit and debit relationship is established, the banks should grant loans according to the contracts. To simplify the process of disbursement, the loan will not be granted to the students in cash. The GSSLS tuition loans will be transferred directly to the institutions' accounts opened at the lending banks. That is to say, the money for the tuition loan will be paid directly to the institutions by banks, not via the students. Of course, it is the students and not the institutions who are the real debtors of the banks. The living expenses loan will be transferred to the students' individual accounts opened at the lending banks.

(d) Interest subsidies of the GSSLS

For the loans granted to the higher-education institutions affiliated to the central ministries, the interest-subsidy funds are transferred to the lending banks by the national centre once every three months according to the actual loan transactions. The subsidized-interest funds held by the national centre are allocated by the central government financial authority, and the funds also absorb some social donations.

For the loans granted to the higher-education institution affiliated to the local government, the subsidized-interest funds are transferred to the lending banks by the local centres once every three months, according to the actual loan transactions. The discounted-interest funds are appropriated by the local financial authority.

Figure 4.2 Cash flow chart



- ▶ providing loans
-▶ the origin of subsidized interest and towards whom
- ▶ providing repayment and to whom

Notes:

- Institutions C: Institutions affiliated to central ministries
- Students C: Students in institutions affiliated to central ministries
- Institutions L: Institutions affiliated to local government
- Students L: Students in institutions affiliated to local government

4.4 Summary

- The organizational structure of the GSSLS is composed of three parts: the government administration system, the university loan offices and the lending banks. This is a complicated organizational structure. The role of the leading group, including the central leading group and local leading groups, is as co-ordinator of the relations between these three parts. From the aspect of organization, we can see that the GSSLS is under the supervision and plan of the government.
- The implementation of the GSSLS is mostly undertaken by the lending banks. The functions of the government loan-administration system and the university loan offices are mainly to help the banks in certain aspects, such as the interest subsidy, collecting and providing information for banks.
- The GSSLs are a kind of individual consumer-credit loan. Four state-owned banks of China provide the loan funds, ratify the loan applications, grant the loans, collect the loans, and even undertake risks such as loan default, interest-rate risk, administrative-cost risk, etc. On the other hand, the lending banks can in theory profit from the loan business, without regard to loan risks, because the interest rates of the GSSLS are just the commercial loan interest rates.

Section 5

Review of the working of the Government-Subsidized Student Loans Scheme

5.1 Loan funds

The GSSLS is operated by state-owned commercial banks. These banks raise the loan funds themselves and take full charge of allocating and recovering the loans. The GSSLS is guarantee-free, the ‘student individual credit guarantee’ being applied, and is targeted at needy full-time college students. The central or local financial authorities provide a certain proportion of the interest subsidy.

5.2 Statistical data on the GSSLS

The number of students involved in the loan schemes

As shown in *Table 5.1*, by the end of January 2001, about 514,000 students from higher-education institutions all over China had applied for student loans, and 111,000 of them had signed the loan contracts. At the end of 2001, the number of loan applicants had reached 859,000 and 272,000 of them had signed the loan contracts. The ratio of loan recipients to applicants was only 31.66 per cent, which is not the loan coverage. Because statistical data are absent, we cannot calculate the loan coverage accurately.

Table 5.1 Some statistical data on the GSSLS (accumulated amount)

	By January 2001 of GSSLS	By May 2001 of GSSLS	By the end of 2001 of GSSLS
[1] Applicants number (thousands)	514	534	859
[2] Signed contractors number (thousands)	111	170	272
The ratio of [2]/[1] (%)	21.60	31.84	31.66
[3] Applied loan funds (million Yuan)	3,230.00	3,338.00	6,876.00
[4] Contracted loan funds (million Yuan)	1,260.00	1,263.00	2,435.00
The ratio of [4]/[3] (%)	39.01	37.84	35.41
[5] Distributed loan funds (million Yuan)	415.00	633.00	1,329.00
The ratio of [5]/[3] (%)	12.85	18.96	19.33
Planned interest-subsidy funds (million Yuan)	137.50	270.00	266.00
Actual interest-subsidy funds (million Yuan)	9.34	9.34	13.95

Sources: (1) National Centre, 2001a.
 (2) National Centre, 2002.
 (3) Tian, 2001.

Notes:

1. These figures are total amounts of GSSLS in different statistical data.
2. When contracted loans are shown, it does not mean that the money has automatically reached the students; for example, it takes time from the point when the loan is contracted, to the loan actually being granted and placed in the needy students' hands. Some students applied for four years' GSSLS, but the granting is according to the academic year and so on. The above phenomena account for the difference between the amount of contracted loans and the amount of granted loans.
3. Loan contracts need to be confirmed every year.

From *Table 5.1* we find a slow increase in the ratio (from 21.60 per cent at the end of January 2001 to 31.66 per cent at the end of 2001). At the same time, five provinces have not arranged interest-subsidy budgets and two provinces have not yet initiated the GSSLS (National Centre, Newsletter No.13, 2002). The reason for this is that the banks are worried about the high default rate. GSSLS are a sort of credit loan and students may change their workplace after graduation frequently. However, the individual credit system has not been established yet in China. Although the government has committed to cancel 'dead debt' when some loans are defaulted on, the possible high default ratio will bring large losses to the commercial banks.

The total amount of loan funds

By the end of January 2001, the total amount of the applied loan funds had reached 3,230 million Yuan, and the contracted funds totalled 1,260 million Yuan, accounting for 39 per cent of the applied funds; the granted loan funds had reached a total of 415 million Yuan, which accounted for 12.85 per cent of the applied funds (Liao, 2001). At the end of 2001, the total amount of the applied loan funds had reached 6,876 million Yuan, and the contracted funds 2,435 million Yuan, which accounted for 35.41 per cent of the applied funds; the granted loan funds reached 1,329 million Yuan, which accounted for 19.33 per cent of the applied funds. The loan funds applied for by the students from the local institutions reached 4,658 million Yuan, and the contracted funds totalled 1,213 million Yuan, which accounted for 26.04 per cent of the applied funds. The funds applied for by students from the institutions affiliated to central ministries reached 2,218 million Yuan, and the contracted funds 1,222 million Yuan, which accounted for 55.09 per cent of the applied funds (see *Table 5.2*) (National Centre, Newsletter No.13, 2002).

From the above data we find that, in particular, the difference between the local institutions and the institutions affiliated to central ministries is obvious (for detailed analysis see *Section 7*). Although the reasons are complicated, it is thought that the banks' concern regarding default is a main factor in limiting the granted loan funds. The banks are afraid of defaulted loans, they therefore restrict the granting of funds and prefer to provide for poor students in the institutions affiliated to central ministries.

Arrangement of the interest-subsidy funds

In 2000, the central government provided 49 million Yuan for subsidized interest and the local governments offered 88.5 million Yuan, therefore the total amount was 137.5 million Yuan (Bank, No.126, 2001). By the end of May 2001, the national financial authority had provided 270 million Yuan for subsidized interest, of which the central government provided 163 million Yuan, and the actual paid amount was 5.872 million Yuan. The local governments provided 107 million Yuan, and the actual paid amount was 3.468 million Yuan (National Centre, Newsletter No. 2, 2001b).

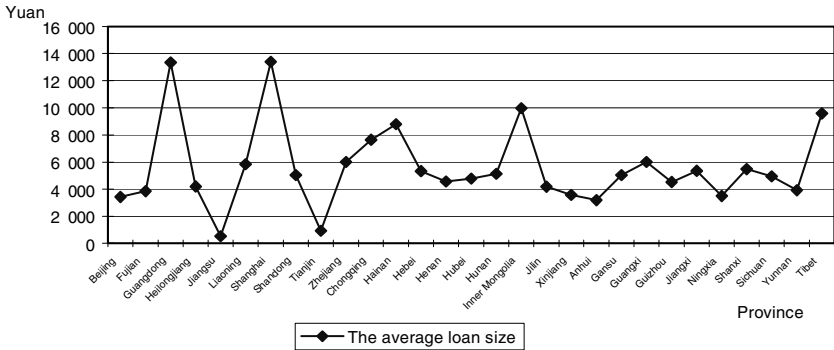
With regard to subsidized interest, the amount provided by the central government increased more rapidly than that which the local governments provided, causing the poor students to get different results. Especially in developing areas, the local governments could not provide sufficient subsidized interest, so that the conditions of the Government-Subsidized Student Loan were not satisfactory.

5.3 The loan size and the ratio of recipients to applicants

The average loan size

Appendix Table 1 shows the average size of the loans whose contracts had been signed by the end of May 2001 throughout the country. The average size of GSSLs for each recipient amounted to 7,425 Yuan. But among the 29 provinces or cities that had provided the statistical data for the student loans, the loan size in 23 of them was below the average level. Tianjin and Jiangsu are comparatively developed areas, but their average loan size was less than 1,000 Yuan, far below the national average level. The average sizes in six provinces or cities were above the average level; Shanghai City and Guangdong Province head the list, and their average loan sizes exceeded 13,000 Yuan. From *Figure 5.1* one can find some huge differences among the different provinces.

Figure 5.1 The average loan size by province, May 2001



Surprisingly enough, the average loan sizes in Inner Mongolia, Tibet and Guizhou were also above the national average level, being respectively 9,976 Yuan, 9,593 Yuan and 4,531 Yuan. As far as the types of institutions are concerned, the average loan size of the institutions affiliated to the central ministries was 8,603 Yuan, the size of the local institutions 6,634 Yuan. It is quite obvious that there exist distinct differences in the loan sizes of different areas and different types of institutions, and in developed areas and central institutions the GSSLS is better than that in developing areas and local institutions. But one cannot escape the fact that the number of poor students in the latter is generally higher than that in the former, leading to fears of the phenomenon of the ‘Matthew effect’. This should be solved by the government in future, and remedies need to be incorporated in the next policy.

The loan ratio

The ‘loan ratio’ refers to the quantitative relation between the loan recipients and the loan applicants. Because of the lack of relevant statistical data, we cannot calculate the percentage of the loan recipients to all enrolled students.

(a) Facts of the loan ratio of the whole country

By the end of May 2001, the number of students who had actually signed loan contracts accounted for 31.84 per cent of those who had applied for the loans; the amount of the contracted funds accounted for

37.84 per cent of the applied funds (National Centre, Newsletter No.2, 2001b). The ratio between the students who had signed contracts and the students who had applied for the loans can be analyzed on three levels: the national average ratio is 21.6 per cent; the average ratio of the local institutions is 17.2 per cent and the ratio of the institutions affiliated to the central ministries is 35 per cent (Liao, 2001).

(b) Facts of the loan ratio in different types of institutions

At the end of May 2001, the ratio of students who had signed the loan contracts accounted for 31.84 per cent of applicants, and the ratio of contracted funds accounted for 37.84 per cent of applied loan funds (see *Table 5.2*). By the end of 2001, the above-mentioned ratios showed a decrease, respectively 31.66 per cent and 35.41 per cent. In the institutions affiliated to the central ministries, 142,000 students had applied for student loans, 69,000 students had signed the loan contracts, the ratio between these two items is 48.59 per cent, and by the end of 2001 the ratio had ascended to 55.67 per cent. The applied loan funds had reached 1,143 million Yuan, the contracted funds had reached 591 million Yuan; the ratio between these two items was 51.71 per cent, and by the end of 2001 the ratio was 55.09 per cent. At the same time we may see that the average ratios of recipients to applicants and of amount contracted to amount applied for in the central institutions in total advanced, but in local institutions they dropped by 1.11 and 4.58 per cent; in the central institutions, on the other hand, they increased by 7.08 and 3.38 per cent. This shows that the gap between the two kinds of institution has increased, and a relevant policy is needed to solve the problem.

Table 5.2 The ratio of GSSLS by institution types, 2001

	Applicants number (thousands) (a)		Recipients number (thousands) (b)		The ratio of (b)/(a) (%) (%)		Applied loan funds (millions) (c)		Contracted loan funds (millions) (d)		The ratio of (d)/(c) (%) (%)	
	May	Dec	May	Dec	May	Dec	May	Dec	May	Dec	May	Dec
Total in country	534	859	170	272	31.84	31.66	3338	6876	1263	2435	37.84	35.41
Local institutions	392	665	101	164	25.77	24.66	2195	4658	672	1213	30.62	26.04
Central institutions	142	194	69	108	48.59	55.67	1143	2218	591	1222	51.71	55.09

Sources: National Centre (2001b, 2002), Newsletters Nos. 2 and 13.

Note: Due to rounding off, these figures may not be perfectly equal to those in *Appendix Table 1*.

5.4 Summary

As shown in the statistical data, by the end of May 2001, only about 32 per cent of the loan applicants had succeeded in signing loan contracts; the contracted funds only accounted for about 38 per cent of the applied funds (National Centre, Newsletter No. 2, 2001b). That is to say, two-thirds of the loan applicants failed to sign loan contracts with the lending banks. Generally speaking, at the end of 2000, there were about 5,600,000 full-time college students in RHEI; even if the loan coverage was only 10 per cent, there should have been 560,000 students who succeeded in obtaining the loans; but by the end of May 2001, the number of the students who had signed the loan contracts was less than 170,000. It is hard to say that the percentage of 170,000 loan recipients divided by the total of 5,600,000 students is the actual loan coverage, as up until then, recipients were mainly freshmen and sophomores, and all students from the four grades at undergraduate level were not covered. Theoretically, the central and local governments should have planned several billion Yuan for the interest subsidies (see *Table 5.1*) (National Centre, Newsletter No. 2, 2001b), but the fact is that by the end of May 2001, the total amount of loan funds in the whole country had only reached 1,263 million Yuan, and only 633 million Yuan from the funds had actually been allocated. Where the time-scale and figures are concerned, the student loan businesses seem to have developed very quickly; but when it comes to the immense needs and the poor coverage, the progress is far from satisfactory.

Section 6

Financial analysis of the Government-Subsidized Student Loans Scheme

The student loans scheme through the banking system is a brand-new issue in China. The society, especially the banking system, is worried about the repayment of student loans under the conditions of a no-credit system. This section has been completed with the advice and guidance of Professor Adrian Ziderman and follows both the format and methodology used in the Ziderman Thai study. It focuses on the financial viability of the GSSLS, and consists of four parts:

- presenting information on formal conditions for receiving a loan;
- answering the question of how much of a loan a typical student repays to the banking system;
- discussing the probability of repayment default and administrative costs;
- drawing conclusions concerning the overall financial viability of the GSSLS.

6.1 Formal loan conditions

To be eligible for a GSSL, a student must be a Chinese citizen with an identification card issued by the national or local public security departments, be studying in a regular public higher-education institution, have passed his/her academic examinations and be poor. The poverty line is defined by the civil affairs departments of government in terms of household income. For example, the basic cost of living accounts for 280 Yuan (about US\$35) per month in Beijing, according to the civil affairs departments. The qualified applicants include not only undergraduate students but also graduate students from regular higher-education institutions. Students from private or so-called non-governmental post-secondary institutions, including pilot diploma schools and schools for self-study students, are not qualified to apply for the GSSLS. They can apply for general commercial student loans, which do not have the advantage of the government's interest subsidy.

The GSSLS defines different loan sizes and ceilings for tuition and living expenses. A student from an RHEI can apply for a tuition loan and a loan for living expenses. The loan ceiling for tuition is always the same, regardless of the amount of tuition, and loans are disbursed from the banking system to the financial offices of educational institutions. The loans for tuition are allocated to educational institutions annually. Another kind of student loan is for students' living expenses; the ceiling varies with the local poverty line.

The repayment regulations require that the first repayment must occur within one year after student borrowers graduate from higher-education institutions. The 'grace period' is flexible from zero to one year, depending on the choice of the individual student. A student borrower can start to repay his/her loan either from the first month after graduation, or from the last month of the first year after graduation. The maximum length of the 'grace period' is therefore one year and the average grace period is half a year. The authors take 'half a year' as a typical grace period for financial analysis.

A typical student borrower starts to repay a loan in the first year after graduation, and completes repayment in the four years after graduation. The principal begins to produce interest from the day of the student borrower receiving the loan. Student borrowers need to repay the principal and half of the interest amount, with the central/local financial authority subsidizing the other half.

6.2 The individual loan account

The repayment ratio and hidden grants

The principal of the GSSLS comes from the banking system; the government subsidizes half of the interest. The banking system manages the disbursement and collection of the student loans. The central objective of the GSSLS is to target the poor who otherwise could not afford their higher learning. However, the banking system runs the GSSLS on a commercial basis, and may need to achieve a return on loans. Therefore, the government, higher-education institutions and students may consider that the financial equity of the GSSLS is most important, while the banking system may concentrate on the financial efficiency.

The financial efficacy of loan schemes depends above all on the extent to which loans are repaid. The equity of loan schemes depends on whether the loan recipients are the targeted group and on the extent of hidden grants. The loan repayment ratio and hidden grants are two indicators to evaluate the financial efficacy. The repayment ratio means the relationship between amounts lent and amounts which should be received back according to repayment obligations. The repayment ratio on student loans depends crucially on two main factors, of whether repayments are linked to inflation and the amount of interest subsidy on the loans and indication as to the amount of hidden grants.

Computing the repayment ratio

The GSSLS was implemented in 1999. Most of the loans have not yet matured. The main bulk of loan repayments may occur in 2004 or 2005 because, generally, the number of freshmen and sophomore borrowers is much larger than that of junior and senior student borrowers. Therefore, at present it is hard to compute the exact repayment ratio because the repayments have not yet, in the main, begun. Nevertheless, we may conduct simulations to calculate such ratios according to the repayment plan in use.

Based on the formal repayment conditions and the repayment plan in use at the GSSLS, we compute the repayment ratio on typical loan programmes. For this initial calculation, we take an example of a typical four-year university student. The typical student borrower applies for a loan to cover tuition fees of 5,000 Yuan per academic year and 250 Yuan per month for living expenses to support four-year higher learning (the tuition fees may vary according to institution location, institution types, and majors. The loans for living expenses may vary according to institution location). The student pays back his/her first repayment to the banking system at the time of half a year after graduation, and then repays principal and interest quarterly. So it will take the student borrower 15 instalments to repay all of the loans and interest. The interest rate is 3.105 per cent annually for institutions affiliated to central ministries. The details of the methodology used for the current repayment scheme are as follows:

- The principal is 30,000 Yuan, within this, 20,000 Yuan is for tuition and 10,000 Yuan is for living expenses to support four years of higher learning. A typical student borrower needs to repay the student loans

plus interest within four years after graduation. Four years equals to 16 quarters. The typical student borrower has a ‘grace period’ of half a year. Therefore, there are in total 15 quarters for repayment. So the typical student borrower quarterly repays 2,000 Yuan of principal.

- The student loans have started to produce interest since the day of their being disbursed to the student borrowers. Half of the interest was 3.105 per cent annually in 2001. Therefore, the interest of tuition loans is 1,725 Yuan from the day of borrowing the loans to the day of starting to repay the loans. The equation (1) shows how the interest has been computed:

$$TI1 = \sum_{n=1}^4 TL(n+1/2)r \dots (1), \text{ where } n \text{ is year, TL is tuition loans for one academic year, } r \text{ is half of annual interest rate.}$$

- The interest of the living-expenses loan is 668.44 Yuan from the day of borrowing to the day of starting to repay the loan. The calculation of living-expenses loans’ interest is different from that of tuition loans’ interest; this is because living-expenses loans have been distributed monthly. Correspondingly, their interest has been computed monthly. The equation (2) indicates the calculation method of living-expenses loans’ interest.

$$LI1 = \sum_{n=1}^{40} LL \times r_m (40 - n) \dots (2), \text{ where LL is living-expenses loans for one month, } r_m \text{ is half of the monthly interest rate, } n \text{ is the month when the living-expenses loans have been distributed.}$$

- During the repayment period, the remaining non-repaid principal produces interest continually. The typical student borrower should therefore repay quarterly the interest of the non-repaid principal. This kind of quarterly repayment decreases by a certain amount quarterly with the decline of the remaining non-repaid principal.
- The interest of tuition loans is 1,086.75 Yuan from the day repayment starts to the day to complete repayment. Equation 3 shows the calculation of this type of interest.

$$TI2 = \sum_{q=1}^{15} (TP - TP/15 \times q) \times rate / 4 \dots (3), \text{ where TI2 is the interest of tuition loans from the day repayment starts to the day to complete repayment, TP is the total principal of tuition loans (in our example}$$

of a typical student borrower, the amount of TP is 20,000 Yuan), q shows quarter, rate is half of annual interest.

- The interest of living-expenses loans is 543.37 Yuan from the day repayment starts to the day to complete repayment. Equation 4 shows the calculation of living-expense loans. The equation is:

$LI2 = \sum_{q=1}^{15} (LP - LP/15 \times q) \times rate / 4 \dots (4)$, where LI2 is the interest of living-expenses loans from the day repayment starts to the day to complete repayment, LP is the total principal of living-expenses loans (in this example, the amount of LP is 10,000 Yuan).

- The principal plus interest should be repaid within four years after graduation. It means that the typical student borrower should make 15 repayments to the banking system.
- The total amount of quarterly repayments equals 2,000 Yuan of 1/15 of the principal and 159.56 Yuan of 1/15 of the interest, plus the quarterly interest of non-repaid principal during the repayment period. The equation is:

$$QR = ((TP + LP) - (TP + LP) \times q / 15) \times r / 4 + (TP + LP + TI1 + LI1) / 15 \dots (5)$$

We make use of the consumer price index and the inflation rate to calculate the present value of the loan repayments. The average consumer price index was about 1.022 from 1985 to 1999 (China Statistics Yearbook, 2000). We make the assumption of an inflation rate of about 1.022 to simulate the repayment ratio. For a typical student loans programme, the repayment ratio is 79 per cent, which is much higher than that of the Thai case. It means that 21 per cent of loans are hidden grants to the borrowers.

Repayment conditions

For the typical student borrower, his total principal amount is 30,000 Yuan, with total interest of 4023.56 Yuan. His repayment period is spread over four years, including half a year of ‘grace period’. The fraction for quarterly repayment is bracketed in the following *Table 6.1*.

Table 6.1 Quarterly repayment schedules (%)

Year	1				2				3				4			
Quarter	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16
Repayment	0	6.35	6.99	6.94	6.89	6.85	6.80	6.76	6.71	6.67	6.62	6.58	6.53	6.48	6.44	6.39

Note:

- (1) Repayment refers to percentage of principal plus interest.
- (2) The first quarter is in the grace period.

The repayment burden

The average income of a four-year higher-education graduate was 10,798 Yuan in 1996, 12,436 Yuan in 1997 and 13,530 Yuan in 1998 (Chen, Ran and Chen, 2001). The average income growth rate is 12 per cent annually in the three years. Assume that the typical student borrower starts to repay the loans from the end of 2005 after four-year higher learning from 2001-2004. With an assumption of nominal income growth of 12 per cent annually, the average income will be 29,910.52 Yuan in 2005, 33,499.78 Yuan in 2006, 37,519.76 Yuan in 2007, and 42,022.13 Yuan in 2008. According to computer simulation, a typical loan repayment is 6,897.86 Yuan in the first year, 9,290.30 Yuan in the second year, 9,041.90 Yuan in the third year, and 8,793.50 Yuan in the fourth year after graduation. The data in *Table 6.2* (according to the authors' simulated computation) show the annual repayment as a percentage of annual income, providing an indication of the weight of the burden of repayment falling on the borrower each year. The annual repayment burden in terms of annual income is around 20-30 per cent. The annual repayment as a proportion of incremental income indicates that the typical student borrower would take twice the incremental income to repay student loans.

The general conclusion emerging from this analysis is that the Chinese GSSLS provides borrowers with low hidden grants, which may require borrowers to make efforts to earn money in order to repay the principal and interest in the four years after graduation from a four-year higher-learning institution. The question is, how many college or university graduates are able to find jobs when they leave institutions?

Before the great expansion of higher education in 1999, the gross enrolment ratio of the cohort in higher education was 9.8 per cent. Even after the rapid growth in the number of higher-education students, the

gross enrolment ratio was 11.5 per cent in 2000. As an enrolment ratio, it is low and Chinese higher education is still at an ‘elite education’ stage. The proportion of college graduates across the country is low, yet graduates with a college or university degree have encountered employment difficulty. The reason for this is because most of the college graduates pursue jobs in economically advanced areas and high-benefit workplaces. The private rate of return to higher education is increasing, though the absolute data are still lower than the world average and that in most other countries. Up to the present time, there is no obvious evidence to show real unemployment in the college-graduate group, except for voluntary unemployment.

However, one cannot say that the labour market has a high absorptive capacity for the employment of the growing number of new graduates. The great expansion of higher education started in 1999. A high percentage of new students were enrolled in three-year professional or vocational higher-education institutions. These graduates from three-year colleges will enter the labour market in 2002, but their chances of finding employment are not great, for two reasons: (1) low competitive capacity in the labour market in comparison to the four-year regular higher education; (2) underdevelopment of the curriculum and teaching of vocational tertiary education.

Table 6.2 Annual GSSLS repayment burden
(for a typical 4-year-course undergraduate)

Year	Repayments (Yuan)	Annual income (Yuan)	Repayment as a percentage of annual income (%)	Repayment as a percentage of incremental income (%)
2005	6,897.86	29,910.52	23.06	-
2006	9,290.30	33,499.78	27.73	258.84
2007	9,041.90	37,519.76	24.10	224.92
2008	8,793.50	42,022.13	20.93	195.31
Average	8,505.89	35,738.05	23.95	226.36

6.3 Loan return to the banking system with repayment default and administrative costs

The repayment ratio shows hidden grants but fails to indicate the return to the loans distributed by the banking system. Generally speaking, the loans will receive back less than is indicated in the repayment ratio, because some students will not meet their repayment obligations and the administration of student loans is costly, despite the government subsidy of half the interest.

Repayment default

It is well known that the GSSLS is a brand-new programme. Only a small number of student borrowers have graduated from higher-education institutions. It is hard for researchers, policy-makers and even bank officials to accurately forecast repayment default under the conditions of loan-repayment inexperience in China. The bank officials are not overly optimistic that they will retrieve most of the loan funds and interest. There are two main reasons, as follows:

- The essential factor in impeding the student loans scheme's smooth progress is the underdevelopment of the repayment mechanism. The banks have worries about the repayment ratio and loan risks; there is no effective supervision regarding personal income in the Chinese financial system, meaning that banks take risks in lending money to individual students. At present in China, earnings are mainly paid in cash so that it is difficult for banks to trace how much people earn and to where their earnings flow. The banking system has no confidence in loan repayment as the high default ratio will bring about large losses to the commercial banks.
- The loan repayment burden, in terms of repayment as a percentage of annual income, is relatively high in China. The simulation result shows that the repayment burden is around 20-30 per cent, which means that borrowers will have to find 20-30 per cent of annual income to repay the loans. This will put considerable financial pressure on student borrowers when they enter the labour market, in the light of the existing unemployment.

With regard to the way that the current system is run, it is difficult to force borrowers to repay the loans. The only sanction for those who default on their loans is that their name, identification-card number and university will be published in the media, for example in newspapers and on the Internet. It is reported that a specific credit company has been established to help the banking system to chase borrowers to repay loans; but its sustainable benefits are doubtful and under investigation. It is believed that repayments will improve rapidly as the credit system develops and people's perception to credit increases.

While there is considerable variation in default rates amongst developing countries, many schemes display a default ratio in the range of 5-10 per cent. In the case of the Huazhong University of Science and Technology, the default rate of the 'old' Student Loans Scheme was around 10 per cent in 1995 and 1996. Given the underdevelopment of the credit system, one assumes that the default probability of the GSSLS is higher than 10 per cent.

Administrative costs

As in most developing countries, some students may not meet their repayment obligations. It is thought that default conditions may be a serious problem in the case of China. The worry about default is definitely an obstacle to the banking system budgeting more funds for the GSSLS. In contrast, the administration of the student loans scheme is not very costly in the short term, especially in the initial years of implementing the GSSLS. According to our investigations, neither the governmental departments nor the banking system and educational institutions recruited new staff, but added workload on the present staff. The present staff can support the work burden in the initial years of the GSSLS, the loan scheme having started only since 1999 and the loan scale being small so far. However, with the expansion of student loans, new staff will have to be recruited.

No reliable data on administrative costs are available at present. Administering the loans scheme is on a part-time basis, because officials from national and regional governments, the banks and educational institutions run the loans scheme as well as doing other work. The administrative costs are absorbed by these institutions running other schemes, because up to now the GSSLS is a subsidiary project to each level of the administrative institutions. To compute the loan return and

loss for the banking system, we assume the administrative costs from the aspect of international experience and simulate loan return and loss rate taking account of different levels of administrative costs from zero to 2 per cent.

Loan return and loss

Because the banking system runs the GSSLS on a commercial basis, it has to take account of cost and benefit. To the banking system, the cost of the GSSLS includes the present value of amounts lent, loan default and administrative costs of banking institutions. The benefit includes the present value of amounts received back, and interest on loans.

Taking account of the probability of repayment default and adopting a level of administrative costs in line with that from international experience, the loan return and loss rate is listed in *Table 6.3*. *Table 6.3* presents alternative estimates of the average return and loss rate in the GSSLS, with an assumption of 10 per cent default probability and differing administrative-cost assumptions. With an assumption of zero default and without administrative cost, 83 per cent of amounts lent are recovered to the banking system. With an assumed 10 per cent rate for default and 2 per cent rate for administrative costs, the loans recovered amount to 53 per cent, indicating that the banking system loses 47 per cent of the amounts lent in such a GSSLS. This means that the banking system has no monetary returns from the GSSLS; in contrast, 21 per cent of the loans have been disbursed as ‘hidden grants’.

Table 6.3 Loan return and loss rate on the GSSLS (under 10% default and alternative administrative costs, %)

Default rate	0	10				
Administrative costs	0	0	0.25	0.5	1	2
Loan return rate	83	70	68	66	61	53
Loan loss rate	17	30	32	34	39	47

6.4 Loan scheme sustainability

The cost and benefit of the GSSLS affects three bodies: the banking system, the government and student borrowers. Here, we would like to analyze the scheme sustainability from the positions of the three bodies, respectively.

From the position of a student borrower, a typical student borrower receives 21 per cent of loans as 'hidden grants'. Therefore, the needy student will have strong reasons to borrow through the GSSLS if he/she cannot find other sources to support his/her learning. This explains why so many students apply for the GSSLS.

However, a relatively high repayment rate and ratio may impose harsh burdens on borrowers, especially on the new employees graduating from institutes. This phenomenon is also a disincentive for the needy students to apply for loans. The success of the objectives of the GSSLS, achieving education-opportunity equality and helping the needy students to support their higher learning, will be doubtful.

From the position of the government, the government pays half of the interest rate to encourage the banking system to disburse the student loans, hoping meantime to encourage needy students to apply for them to support their higher learning.

The banking system shows relatively negative attitudes to the GSSLS, compared to the attitudes of students and the government. By the end of May 2001, only 170,000 students had benefited from the GSSLS among 534,000 applicants. Five provinces had not arranged subsidized budgets and two provinces had not yet initiated the GSSLS (see *Section 5*). The obstacle to the banking system contracting large-scale loans with students is the underdevelopment of the credit system. At present, the only sanction – to make the names of students and institutions public – is not sufficient. The establishment of an efficient and effective repayment system is becoming the core concern of the banking system. From the viewpoint of the banking system, the most urgent need is to establish a credit system and an effective repayment mechanism to guarantee the repayment of student loans. To establish a more dynamic capital market to attract loan funds might be feasible market behaviour. In addition, the government might take into account the possibility of guaranteeing a certain degree of

loan returns to encourage the banking system to run such a student loans scheme.

6.5 Summary

Through financial analysis of the GSSLS, we obtain the following findings:

- The repayment ratio for the GSSLS is 79 per cent, 21 per cent of the loans having been disbursed to student borrowers as ‘hidden grants’.
- The loan repayment burden, in terms of repayment as a percentage of annual income, is relatively high. The simulation result shows that the repayment burden is around 24 per cent.
- With an assumption of zero default and without administrative cost, 83 per cent of the amounts lent are recovered by the banking system. With an assumed 10 per cent rate for default and 2 per cent rate for administrative costs, the loans recovered amount to 53 per cent, indicating that the banking system loses 47 per cent of the amounts lent in such a GSSLS.
- The underdevelopment of the credit system becomes the obstacle for GSSLS. The banking system has no confidence in being able to retrieve loans. The establishment of an efficient and effective repayment system is becoming the core concern for the banking system.

Section 7

Targeting for equity and access of the GSSLS

With the rapid expansion of higher education, public higher-education institutions face increasingly severe public budget constraints. One important way to generate multiple resources is to increase the tuition costs and fees of the students and the families. Increasing tuition costs is a financial barrier for the poor students if financial aid cannot keep pace with the rising tuition fees. The central government and the public are quite concerned about this issue. The GSSLS was created in 1999 and has become an increasingly important way to make higher education accessible to the poor student.

The objective of the GSSLS in China is to help the needy students to pay for their tuition and their living expenses so that they can have access to higher-education institutions and finish their studies.

Whether the objective can be reached or not depends on three main points: reach, efficacy and equity. The three concepts are given the following descriptive definitions by Adrian Ziderman:

- *Reach of the Scheme: does the scheme indeed reach the target group? Which groups are not reached? Are some ineligible students in receipt of loans?*
- *Efficacy of the scheme: of those who are reached by the scheme and in receipt of a loan, does the loan indeed lead to continuation of study, thus preventing drop-out?*
- *Equity issues: are loan recipients treated equitably? Do all the potential recipients have equal chances of receiving a loan? (Ziderman, 2001).*

7.1 The reach of the GSSLS

Defining the target population

Many student loans schemes in place are open to all students, regardless of need or ability to pay tuition costs. Such loan schemes can impose excessive burdens on taxpayers or the governments. The primary advantage of open access to loans is that any one who needs financial aid can take loans. The chief disadvantage is that, usually, fewer funds are available for needy students, and limited available funds may often go to benefit those who can afford to pay.

A successful loan scheme needs to be targeted effectively, to those who are deemed most deserving of support. Without effective targeting, growing student numbers in the future, as well as less-than-full loan recovery, will result in increasing, and unsustainable, pressures on limited loan funds. Given that loan funds are subsidized, targeting will facilitate the task of limiting the extent of loans subsidization (Ziderman and Albrecht, 1995).

In order to target any benefits programme, it is necessary to develop clear definitions of the target group to which the scheme is directed. These definitions serve two purposes, at the macro and micro levels. At the macro level, a lack of a clearly defined target group (including information on the size and the population involved) will render impossible the task of developing an objective approach to the planning and budgeting of the scheme. It will also rule out any realistic attempt at assessing the degree of success of the project in reaching the target group that is also required at the micro level, for the accurate screening of individual eligibility for inclusion in the scheme.

But in China, insufficient attention is given to the need to define as clearly as possible the target population. The goal of the GSSLS is to ensure that any poor student who is recruited by a higher-education institution does not drop out.

The GSSLS is targeted at the most needy students; therefore the eligibility for a student loan is determined by a needs test. That test examines the financial status of the student's family and relates that status to the cost of attending college. But in practice, problems arise quite often.

Who are the poor students? Where is the poverty line or the income threshold? How to measure the socio-economic status? There is no clear working definition of poor students who are eligible for the loans; it is impossible to calculate the incomes of the families on a case-by-case basis. One therefore confronts the difficulties of administering a means test and obtaining reliable data on family income.

Estimates of the reach of the GSSLS

The GSSLS provides a mechanism for assisting poor students to gain access to higher education. Now technically the maximum loan ceiling (for tuition and living expenses) is about 8,000 Yuan per year. Up to the end of May 2001, there were 534,000 applicants, out of which 170,000 were approved and contracts made with banks. The ratio of recipients to applicants was about 32 per cent. The total contracted loans amounted to 1,263 million Yuan. The average loan size was 7,425 Yuan. That is to say, about two-thirds of applicants did not obtain loans. The loans size is too small; most of the applicants did not obtain the money they needed. The supply of the GSSLS cannot meet the demands of the poor students, whether in coverage or in loan size. Up to the end of 2000 there were about 5.6 million full-time students in regular public institutions. A survey says that the percentage of the poor students is around 20 per cent (the number is 1.12 million). That is to say, about half of the needy students ($0.534/1.12 \times 100\% = 48\%$) did not submit applications for loans. Why do so many eligible students fail to access loans? One reason is that some of the poor students have debt aversion. Some of them do not want others to know their economic status. Some of them are afraid of being in heavy debt and not having the ability to repay the debt in the future. Another reason is that some institutions have not taken part in the GSSLS and their students have nowhere to apply for the loans.

On the other hand, certain ineligible students obtained the loans because of the unclear definition of student eligibility and abuse of the loan administration. Some ineligible students received loans for no educational purpose; some even spent the loans in buying 'luxury goods' such as cell phones and computers.

7.2 Effects of loans on access, as well as prevention of drop-out

A key issue is the effect of student loans on access to higher-education institutions and drop-out prevention in particular categories of students, such as those from low-income families, minority groups, or women. In this section we consider the effect of receiving a loan. For those who are reached by the scheme and in receipt of a loan, does the loan indeed lead to continuation of study, thus preventing drop-out? What would happen in the absence of a loan? The GSSLS did increase the access to higher-education institutions of the low-income students and prevented drop-out. The availability of the GSSLS defers future repayment for college studies, thus making college studies more affordable to many poor students.

Generally speaking, most of the college students would continue at their higher-education institutions even if unable to obtain loans, because it is still not easy to gain places in higher-education institutions and they have sacrificed much even at the high-school level. For some poor students from the rural area, finishing studies at higher-education institutions is their only opportunity to escape from poor economic status. However, some surveys show that about 20 per cent of the college students are poor students. This has both affected their life and studies. The poor students not only bear economic pressure, but also psychological pressure; the heavy economic burden has made some college students feel worried, isolated and inferior. Quite a few students even consider dropping out. After they take out the loans and remove the economic barriers, they are more confident and able to concentrate on study. A survey conducted by Hangman University in Hunan province shows that 82.6 per cent of the loan recipients made academic progress, 9.8 per cent of whom were in the category of best students of the university (Wang and Li, 2001). Many loan recipients would find it easier to gain access to higher-education institutions and to stay there. The GSSLS stimulated incentives for the needy students, who took loans in order to study harder. This helps to improve the teaching and learning quality. Shanghai did best in the GSSLS and with other student financial aid in China. There has been no college-student drop-out in China because of financial barriers in the past eight years (Jin, 2001). On the other hand, in some provinces where the GSSLS did not work well, many students delayed in paying their tuition costs. But the GSSLS has had a positive effect on drop-out prevention.

7.3 Horizontal equity

Horizontal equity means that equals should be treated equally. There is an argument in the public-finance literature that, if everyone truly faces the same opportunity, then horizontal equity conditions will not be violated. In the student loans programme, again, equity would require that, regardless of province of residence or educational institution, students of similar socio-economic background should have equal opportunities for receiving a loan. Inequities arise when loan recipients of the same economic status and level receive loans of different size. These tenets of horizontal equity do not hold in practice in loans distribution in the GSSLS scheme of China.

Here, we will point out three kinds of inequities in the implementation of the GSSLS, which are inequities at provincial level, institutional level and individual level. The reason for choosing this angle is the special case of China. In the developed countries, such as the USA, Canada, and Australia, the eligible poor students can generally obtain student loans, but in China, it is not the same. China has its own tradition; an obvious example is that when allocating resources the developed areas are more privileged, which causes some inequity problems. In the higher-education field the condition is the same, the key institutions have more privileges than general institutions, and the former can obtain more support from the government and the society. The GSSLS has the same conditions, but in developing areas and general higher-education institutions there are more poor students who are eager to be aided. As a result, the angles of the analysis in this section are from three levels, which are based on the poor students.

The research results show that there are mainly three kinds of inequities in the implementation of the student loans: inequities at provincial level, institutional level and individual level.

Inequity between provinces

There are 31 provinces or municipalities directly under the central government and autonomous regions in China. According to the economic development, the Institute of Sociology under the Chinese Academy of Social Sciences conducted some evaluation and comparison studies on the comprehensive development level of the provinces and cities in China in 1998. Based on the research results, the 31 provinces, cities and autonomous regions were classified into three groups: the first group

includes those regions whose economy ranks in the top 10 places, and they are Beijing, Fujian, Guangdong, Heilongjiang, Jiangsu, Liaoning, Shandong, Shanghai, Tianjin and Zhejiang; the second group includes those that are ranked in the 11-20th places, and they are Chongqing, Hainan, Hebei, Henan, Hubei, Hunan, Inner Mongolia, Jilin, Shanxi and Xinjiang; the third group ranks 21-31st, and they are Anhui, Gansu, Guangxi, Guizhou, Jiangxi, Ningxia, Qinghai, Shanxi, Sichuan, Tibet and Yunnan (Zhu and Wu, 2001) (see *Appendix Table 1*).

The inequity at the province level can be expressed as: students studying in more developed regions can be in receipt of the loans more easily; while students studying in less developed regions will find it more difficult to receive the loans.

From *Appendix Table 1*, we can see that until the end of May 2001, the ratio of recipients to applicants between the provinces is quite imbalanced. In Beijing and Shanghai the ratios are 96 per cent and 95 per cent respectively. In Shanxi and Qinghai the ratios are 0 per cent. Beijing and Shanghai are among the most developed areas in China, while Qinghai and Shanxi are among the least developed areas in China. Also as shown in *Appendix Table 1*, we find:

First, on the whole, the loan-recipient ratio in first-group provinces is higher than that of the second-group and third-group regions, with very few exceptions, partly because the governments in these developed regions are more financially powerful and can provide the subsidized-interest funds for the student loans on time, and the implementation of the student loans will be comparatively smoother. Meanwhile, the level of economy of the regions is also directly related to the degree of smoothness in the implementation of student loans.

Second, we can note two exceptional cases, one is Shandong Province, the other is Tibet. In terms of economic development, the former is a first-group province, but only 1.5 per cent of the students are in receipt of the loans; this may have been caused partly by inharmonious relations between the local governments, banks and institutions. Tibet is a third-group region, but the students in receipt of loans account for 87 per cent of the total number; apart from the efforts of the local governments, banks and institutions, another important reason is that the number of the student loan applicants is quite small (only 1,702 students); special policies are

also implemented here to aid the ethnic-minority students and, at the same time, enhance the operation of student loans in this region.

Third, Hubei and Shanxi are both higher education institution-intensive provinces, but their ratios of the students in receipt of loans are sharply different. Statistical data show that their proportions of needy students are respectively 21 and 25 per cent among all the college students; while their ratios of the students in receipt of loans are respectively 3.7 and 0.4 per cent among all the college students, 18 and 1.7 per cent among the needy students; the loan-reaching ratio among all the loan applications is 28 per cent in Hubei, in Shanxi this ratio is 9.2 per cent (Hubei, 2001; Zhang, 2001). The economic level may cause the difference, while the action of banks is another important reason.

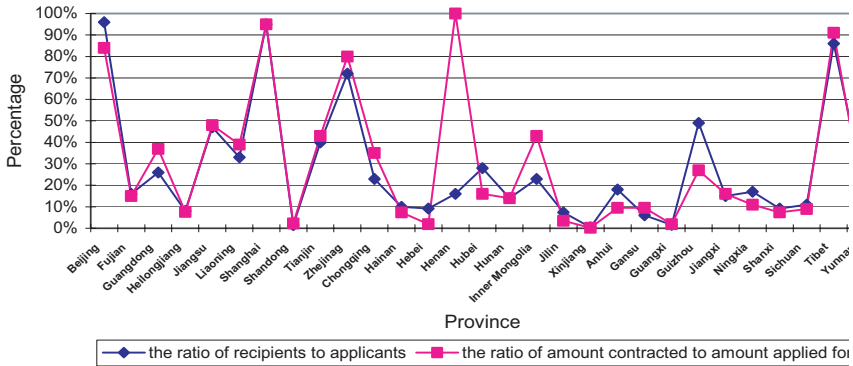
Fourth, the average ratio for the top 10 provinces or cities that did best in the GSSLS is 57.1 per cent, while the average ratio for the bottom 11 is 4.34 per cent. The average percentage of the top 10 is 13 times higher than that of the bottom 11. That is to say, that the opportunities to access to student loans for the needy students in the top 10 provinces are 13 times higher than for those students in the bottom 11. In addition, most of the top 10 provinces or cities are located in the economically developed areas and their budgets are better. Most of the bottom 11 provinces are relatively underdeveloped. So ratios of applicants to recipients are strongly correlated with the economic status of the provinces. But the percentage of the poor students in the bottom 11 provinces is much higher. Even so, by the end of May 2001, there were still five provinces or autonomous regions which had not arranged the subsidized-interest funds for the GSSLS; and another two provinces or autonomous regions had not even initiated yet the GSSLS. Effective measures should be taken to resolve the provincial inequity in the implementation of the GSSLS.

The ratios of recipients to applicants and the ratio of amount contracted to amount applied for of the GSSLS can be seen in *Figure 7.1*.

Much improvement could and should be made in student loan policies. If the interest-subsidy funds to local institutions are only provided through local government finance, cases will probably be like this: the poorer the regions, the less financially capable the governments will be; the fewer funds to be provided for the student loans, the more difficult it will be to implement the student loans in these poor regions, and fewer poor students will receive the GSSLS. If sufficient and timely interest-subsidy funds are

not provided, the less likely it will be that the student loans are implemented smoothly, the students' access to higher education will be influenced (please refer to *Section 8* for detailed suggestions), and the GSSLS target would be discounted in the implementation process.

Figure 7.1 The GSSL ratios by province, May 2001



Inequity among higher-education institutions

There exists huge inequity in access to the GSSLS between different levels of higher-education institutions (see *Table 7.1*). Inequity at institutional level mainly includes: inequity between key institutions and general institutions inside the same ministry; inequity among the key institutions and among the general institutions; inequity between the local institutions and institutions affiliated to the central ministries; also inequity between the four-year institutions and three-year institutions. Generally speaking, needy students studying at the institutions affiliated to the ministries can receive the loans more easily; it is comparatively more difficult for students of local higher-education institutions.

From *Appendix Table 1* we know that the loan applicants from central higher-education institutions can take out loans much more easily than the applicants from the local higher-education institutions. Up to the end of May 2001, 142,444 students of central institutions applied for GSSLS, 68,862 of which were approved. The ratio of recipient to applicant is 48.3 per cent; the average loan size for the central institution recipients is 8,603 Yuan. But in the local higher-education institutions, there are 391,520 loan applicants and only 101,227 loan recipients. The ratio of recipient to applicant is 25.9 per cent and the average loan size is

Table 7.1 Statistical data on the allocation of GSSLS funds by institutions (up to May, 2001)

Institution name	Applicant number (a)	Recipient number (b)	Ratio of (b)/(a) (%)	Applied loan funds (c) (Yuan)	Contracted loan fund (d) (Yuan)	Ratio of (d)/(c) (%)	Distributed loan funds (Yuan)
Key higher-education institutions affiliated to the central ministries							
Peking University	658	658	100	8,996,377	8,996,377	100	2,904,137
Fudan University (Shanghai)	2,464	2,430	99	30,557,000	30,050,300	98	14,476,240
Wuhan University	4,314	3,555	82	4,791,000	1,554,000	32	1,554,000
Zhejiang University	1,715	1,460	83	10,729,200	9,469,300	88	9,469,300
Zhongshan University (Guangdong)	960	700	73	11,958,708	11,958,708	100	2,867,804
Sichuan University	1,900	50	2.6	20,000,000	450,000	2.3	57,760
Xi'an University of Transportation	800	450	56	8,500,000	4,745,000	56	1,874,000
Lanzhou University	2,100	487	23	18,000,000	3,246,400	18	1,249,100
General higher-education institutions affiliated to the central ministries							
Xi'an Post College	289	7	2.4	4,950,000	54,000	1.1	33,890
South-west Forestry Institute (Yunnan)	1,021	23	2.3	3,221,000	52,060	1.6	52,060
Huabei Institute of Water Conservancy and Electric Power (Henan)	1,142	74	6.5	8,120,000	330,600	4.1	330,600

Table 7.1 Continued

Institution name	Applicant number (a)	Recipient number (b)	(b)/(a) (%)	Applied loan funds (c) (Yuan)	Contracted loan fund (d) (Yuan)	(d)/(c) (%)	Distributed loan funds (Yuan)
Chongqing Transportation College	950	97	10	8,000,000	875,960	11	349,480
Dalian Minority College	486	310	64	4,800,000	3,100,000	65	320,000
Beijing Normal College of Professional Technology	50	13	26	500,000	160,300	32	22,500
Guangzhou University of Traditional Chinese Medicine	262	49	19	3,170,000	290,000	9.1	n/a
Higher-education institutions affiliated to local governments							
Hubei University	1,456	1,044	72	1,484	917	62	n/a
Hubei Minority Institution	1,814	221	12	251	29	12	n/a
Wuhan University of Science and Technology	800	9	1.1	1,555	3.8	0.2	n/a
Wuhan Institute of Chemistry Industry	714	140	20	341	60	18	n/a
Hubei Agriculture Institute	940	15	1.6	700	7.9	1.1	n/a
Hubei Institute of Fine Arts	127	127	100	79	79	100	n/a
Wuhan Music Institute	25	19	76	47	33	70	n/a
Three-Gorge University	1,600	910	57	944	833	88	n/a

Sources (1) National Centre for Student Loan Administration, Newsletter No. 2, 2001b.
 (2) Hubei Province Centre of Student Loan Administration, 2001.

6,634 Yuan. The opportunity of access to loans for the applicants of the central higher-education institutions is almost double that for the applicants of the local higher-education institutions. But the percentage of the poor students in local institutions is much higher than in the central institutions. At the same time, some research shows that the poor students are more willing to choose the low-tuition institutions and majors (Ding Xiaohao, 2002). The above phenomenon should be given more attention.

First, on the whole, it is easier for students of key institutions in the ministry to receive loans than for those students of general institutions in the ministry, and the gap is quite sizeable. For example, Zhongshan University and Guangzhou University of Traditional Chinese Medicine are both located in Guangzhou City, the former is a key university of the MOE, while the latter is a general one, their loan-reaching ratios are separately 73 and 19 per cent. Of course, exceptions also exist. As a key university of the ministry, the loan-reaching ratio of Sichuan University is only 2.6 per cent, and only 50 students have signed the loan contracts. Chongqing Transportation College is a general institution of the ministry, but its loan-reaching ratio is 10 per cent, much higher than that of Sichuan University, and both universities are located in the same province.

Second, there are also considerable disparities among the key institutions of the ministry; the conditions in Xi'an University of Transportation and Lanzhou University are much inferior to Peking University and Fudan University; the loan-reaching ratios are 56 and 23 per cent in the former two universities, 100 and 99 per cent in the latter two. In fact, however, there is no difference between the interest-subsidy funds offered by the central and local finance authorities to the four universities, because their interest-subsidy funds are all offered by the central financial authority. Although the interest-subsidy funds can be guaranteed, the initiatives of the local branches of the lending banks are quite different. This may also be the case among the general institutions of the ministry. With the interest-subsidy funds guaranteed by the central financial authority, the location of the university may influence the banks' initiatives. The loan-reaching ratios of the Dalian Minority College in Dalian City and the Beijing Normal College of Professional Technology in Beijing are, respectively, 64 and 26 per cent, higher than the ratios of Xi'an Post College in Xi'an City, South-west Forestry Institute in Yunnan and Huabei Institute of Water Conservancy and Electric Power. The latter three are all general institutions of the ministry, their ratios are 2.4, 2.3 and 6.5 per cent respectively.

Third, the loan-reaching ratios are also different among the institutions within a province. Let us take Hubei Province as an example: the loan-reaching ratios of Hubei University, Hubei Institute of Fine Arts and the Three-Gorge University are respectively 72, 100 and 57 per cent, much higher than for other institutions. The ratios of Wuhan University of Science and Technology and Hubei Agricultural Institute are respectively 1.1 and 1.6 per cent (Hubei, 2001).

Fourth, the average ratio of all the institutions in the country is 17.2 per cent, while the ratio of the institutions affiliated to central ministries is 35 per cent. However, needy students in the local institutions account for two-thirds of all the needy students in the country, the needy students in the institutions of the ministry account for one-third. Surprisingly enough, the loan-reaching ratio of the institutions with more needy students is lower, while the loan-reaching ratio of the institutions with fewer needy students is higher. If the institutions are considered as individual entities, then the difference between the loan-reaching ratios of the general institutions of the ministry and the local institutions is not so obvious. But what cannot be denied is that there does exist distinct inequity at institutional levels in the implementation of the student loans.

Why does there exist so huge a gap in ratios among the different kinds of higher-education institutions? We think the reasons are the following. First, the location of the university/college is correlated with the ratios. Peking University and Fudan University are located in a developed area of China. Sichuan University and Lanzhou University are in the western part of China where the economic conditions are not so good as in the eastern part of China. Second, the reputation of the institutions or programmes and the future of their students affect the ratios. The banks do consider the risk of the loans. If the institutions have a good reputation in society and their students are expected to find good jobs easily, the banks are more willing to lend to their students. Third, the institutional loan administration also influences the access to loans. Some institutions are more active in co-operating with the banks and do their best to let the students know about the GSSL scheme.

Table 7.2 The statistical data of six institutions affiliated to MOE in Chongqing

Institutions	Applicants number (a)	Recipients number (b)	Ratio of (b)/(a) (%)	Applied loan funds (c) (Yuan)	Contracted loan funds (d) (Yuan)	Ratio of (d)/(c) (%)
South-west Normal University, 4-year	1,609	1,416	88.00	4,827,420	4,160,300	86.18
Chongqing University, 4-year	2,854	73	2.55	54,080,000	656,118	1.21
Chongqing Agriculture University, 4-year	830	807	97.20	7,175,200	6,976,500	97.23
Chongqing Transportation College, 4-year	950	97	10.20	8,000,000	875,960	10.95
Chongqing Electricity College, 3-year	63	0	0.00	0	0	
Chongqing Petroleum College, 3-year	184	0	0.00	0	0	

Source: National Centre for Student Loans Administration, Newsletter No. 2, 2001b.

Another inequity occurs between the four-year institutions and three-year institutions. In Chongqing there are six institutions affiliated to the central ministries. From *Table 7.2*, we can see that the ratios of recipients to applicants in South-west Normal University and Chongqing Agriculture University are much higher. The two universities have longer histories and a better academic reputation. But no students could obtain a loan in the two three-year colleges. We know that the percentage of poor students in three-year institutions is higher than that in four-year institutions (because the poorer rural students received poor-quality secondary education and eventually only managed to get into the three-year institutions for further education). The possible reason is that the banks are more willing to lend to students in more prestigious institutions than to those in the less eminent institutions. The banks might think that in this way they can reduce their risk, but this violates the horizontal equity.

There are many factors influencing the loan-reaching ratios of the institutions. The sources and reliability of the interest-subsidy funds play an important role. The reputation of the institutions, the forecast of the students' future employment and the social impacts of the graduates can all influence the ratio. Students from the institutions of the ministry generally have better employment expectations, those studying popular majors are especially welcome, and their future wage will be higher, so banks are

willing to provide them with loans. On the contrary, some key institutions and the general institutions do not enjoy prestigious reputations, their educational quality may be less, and their students have less promising employment expectations, thus the banks also feel less willing to offer them loans.

Inequity among individual student borrowers

There are several kinds of inequities at individual level: inequity among individuals with similar background from different institutions and in the same institution; inequity among individuals with different background in the same institution. The economic backgrounds and economic needs of the individual student loan applicants may be quite different. The differences may be caused by the various tuition standards of diverse institutions or majors, and different degrees of family poverty. If the policy-makers do not consider these differences, inequity in the implementation of the loan scheme is bound to occur.

Inequity among individual student borrowers with similar background from different institutions means that some students may have similar economic status, but they are studying in different institutions and they have access to a different loan supply. Because of the varied geographical locations and assorted affiliation ties, the tuition standards and consumption levels in various institutions are usually diverse, so even students with similar backgrounds will need different economic support. But the loan size for each student is generally the same, and some student loans are only tuition-cost loans, with loan funds directly transferred to the accounts of the institutions, students not actually taking part in this process. The loans for living expenses are uniform in the same region, but consumption levels may differ from institution to institution, and different students have diverse consumption needs, so the same loan size (tuition loan plus living-expenses loan) may cause inequity among individuals because of their different needs (Shen, 2001).

The GSSLS in China covers tuition and/or living expenses. When planning the size of the living-expenses loan, the minimum local living standard has been taken into consideration, but little attention has been paid to students' lodging needs. Actually, the difference between lodging expenses is very obvious, with a minimum of 300 Yuan per year and a maximum of 1,500 Yuan per year (*Table 7.3*). If the distance from the

Table 7.3 Tuition costs and fees for housing in institutions affiliated to MOE, 2000 (Yuan)

Institution name	Tuition					Fees for housing
	Common majors	Popular majors	Arts majors	Special majors	Vocational institutions	
Lanzhou University, Ganshu	4,200	4,800	5,400	-	4,500	700
South China (Huanan) University of Science and Technology, Guangdong	4,560~5,160	-	-	-	-	500~1,500
Peking University, Beijing	4,800~5,000	5,200	9,000	-	-	600~1,200
Centre China (Huazhong) Normal University, Wuhan	3,600	4,100~4,600	9,000	2,700	5,000	500~800
East China (Huadong) Normal University, Shanghai	5,000	5,500	-	5,000 ~10,000	7,500 ~10,000	300~1,200
Zhongshan University, Guangdong	4,560	5,160	-	-	4,500 ~5,500	1,500
Tongji University, Shanghai	5,000	6,000	10,000	-	7,500~10,000	500~1,200
Wuhan University	3,600	4,140~4,680	-	-	-	800~1,200
Fudan University, Shanghai	5,000	5,500~6,500	-	-	7,500	600~1,200
Xi'an University of Electronics and Technology	4,950	5,500~6,000	3,850	-	5,500	600~650
West-South Transportation University, Sichuan	4,300	4,500	8,000	-	-	480~1,200
Central Music Institute, Beijing	-	8,000	10,000	-	-	650

* Data from the brochures of related institutions.

student's family to the institution is also taken into consideration, then expenses may be even more. The loan policies actually give no consideration to differences, and inequity is likely to occur.

Inequity among individual student borrowers with similar background in the same institution is mainly caused by the differences of the majors. First, the tuition standards for different majors are different (as can be seen in *Table 7.3*); but the size of the tuition loans is just the same. As for students who must pay more tuition costs for their majors, they have to look for funds to bridge the gap. Moreover, the lodging conditions inside one institution may be different from another, and the average charge may be different. The above differences were analyzed in terms of the policies and procedures. As far as the recovery of loan funds is concerned, further inequity may occur. Students of different majors will have different employment expectations, and their wage level may also differ. Therefore, the same loan-recovery policy may be unfavourable and disadvantageous to those students of less popular majors.

Inequity among individual student borrowers with different background in the same institution is mainly caused by the individual differences. The needy students in the same institution may vary in many aspects, the location of their family may be different, the sources of their family income may vary, the number of income-earners in the family may also differ, the health status of their family members may also be different; all these factors will lead to different poverty degrees. The most needy students also differ in gender and nationality. Special assistance should be provided to them in the student loans scheme. But the current policies have not taken all these differences into account, and no special regulations have been formulated in terms of loan size, repayment means, and interest-subsidy rates; this also has led to inequity.

Among the above-mentioned kinds of inequity, some are understandable and even reasonable; some can be removed, but others can never be eliminated. We can only make every possible effort to modify and improve the current policies so that equity and equality of opportunity can be achieved in the implementation of the GSSLs (please refer to *Section 8* for detailed suggestions).

7.4 Summary

- The definition of the target population is clear at the macro level, but unclear at the micro level. An operational and measurable means-test formula needs to be developed.
- The GSSLS failed to adequately reach the target group. A vast majority of needy students were not in receipt of loans.
- The GSSLS is important in enabling students from low-income families to continue their studies and to avoid drop-out. After obtaining the loans, the poorer students are able to concentrate on studies and hopefully make academic progress.
- There exists inequity in access to loans between provinces, among institutions and among individual students. A large number of the targeted students, even some who are most needy, cannot yet obtain loans. The loan coverage and the average loan size are still too small.

Section 8

Policy conclusion and implications for reform

This section analyzes the causes of difficulties in conducting the GSSLs, and attempts to provide corresponding suggestions on policy reform.

8.1 Analysis of the causes of difficulties in conducting the GSSLs

Government: more responsibility to be shared

Maureen Woodhall, an economist, found that it is necessary to raise money for three types of costs for most government loan schemes, even if a country relies on banks for the basic funds: (1) payment of defaults, (2) subsidy of low-interest rates for students, and (3) administrative costs for loan-scheme management. The costs can amount to one-third to two-thirds of the schemes. Loans are not free (Cronin and Simmons, 1987). But the responsibilities the governments share in the GSSLs in China are not sufficient. The central and provincial governments only subsidize half of the interest rates and a small part of the administrative costs. They do not guarantee the GSSLs and bear the final risk of defaults. The lending banks shoulder most of the default risk. The big problem for the GSSLs is the potential high risk of defaults. Even though most of the GSSLs are not mature, there are signs showing that the default rate might be quite high. If the governments do not ensure the repayment of loans, the banks will be reluctant to lend or even refuse to participate in the GSSLs. Why are so many eligible applicants unable to obtain loans? The main reason is that the banks are quite reluctant to lend because they are worried about the high risk of defaults and the high administrative costs. The governments should share more risk-taking and more economic incentives should be given to the lending banks, or the GSSLs will fail in the future.

Banks: lack of an individual credit system and immense administrative costs

Technically speaking, banks can be quite interested in the business of student loans. On the one hand, they can achieve the social significance of helping to accelerate the development of education; most important of all, today's college students are most likely to be among the well-paid group of the future and thus potential customers of the banks. If a poor student can obtain his/her loan from a bank during his/her in-school years, he/she is likely to become a permanent customer of this bank. As a kind of financial business, student loans can also bring profits to the banks.

At present, the greatest difficulty in conducting the student loans is still on the banks' side because, in China, an individual credit system has not yet been established and the risks shouldered by the banks are still very high. According to policy, no guarantee is needed in the GSSLS. Theoretically, the operation of credit loans should be based on the establishment of a perfect individual credit system where punitive measures can form a powerful and effective restraint on those customers with bad records, but in China this is not the case. Therefore, the lending banks must take both profits and risks into account; it will be very difficult for them to trace students who disperse all over the country and get the loans repaid without any guarantee or mortgage to hand. The situation worsens if students deliberately escape repaying the loans.

In the practical operation of the student loans, the loan size is usually quite small, but the number of transactions will be quite large, so the banks have to spend a lot of time and manpower in dealing with the loan management, especially when a new academic year begins. Maybe the total amount of the student loans will be less than 10 million Yuan, but where loans to an enterprise are concerned, a single transaction may reach tens of millions of Yuan. At present, although no family visit is conducted before the release of the loans, the banks still have to pay sizeable costs in tracking the information, interviewing the loan recipients' colleges and their employment units, administering the loan accounts, and collecting the loans.

In order to offset the disadvantages caused by the absence of an individual credit system, Dai Xianglong, the president of the People's Bank of China, proposed some important measures in December 2001: in the

operation of the student loans, lending banks should try to take more effective precautions against the risks, try to keep records of students' individual credits and gradually link the network within the financial system, then link it with the national student status administration network of the Ministry of Education so that it will be more convenient for the banks to collect information about cases of contract breach, and to scrutinize the individual credit information of the loan recipients. The People's Bank of China will co-operate with other commercial banks to collect the names of students in cases of contract breach and publish the names of loan defaulters in the newspapers (Deng, 2001). This is thought to be a very powerful and effective measure, but there is no great optimism about the outcome. Before the establishment of an individual credit system, this measure can only be a kind of deterrent force that cannot exert virtual restraint. Within the system of the same bank, the information on the individual credits can be shared through the network, but such information will still be unavailable to other banks, so we can imagine the difficulty in tracking information on the people who figure on the 'blacklist'.

Students: poor credit awareness, complicated loan procedures and heavy repayment pressures

As the loan recipients, the needy students who require the loans most also have their troubles.

(a) The lack of understanding regarding student loans

Certain students do not understand their responsibilities with regard to student loans. For example, some of them have very poor credit awareness, some of them seldom think of the repayment obligation. A survey conducted in Guangdong Province in 2001 on the students who had applied for loans indicated that 29.71 per cent of the students surveyed had never heard of the 'individual credit system'; nearly 20 per cent of them had never thought of the repayment; 7 per cent of them said "it's hard to say whether the repayment will be made" (Liu, 2001).

(b) Complicated procedures and delayed granting of the loans

In order to take more effective precautions against the risks, banks initiated regulations, a series of complicated procedures from applying for the loans to signing the loan contracts. Many requirements are laid down

regarding the students' conditions, performances and family economic backgrounds. The students may well feel exhausted after all these procedures and lose their enthusiasm. At the same time, the complicated procedures lead to delays in the granting of the loans.

(c) Heavy repayment pressures

According to certain regulations, the term of the student loans is usually less than eight years, meaning that if the students apply for the loans when they are still freshmen, they must repay the loans in four years after graduation. Let us do some calculations here; if the loan size is 8,000 Yuan (including both the tuition and the living expenses) per year, the total amount for four years will be 32,000 Yuan. If all this has to be repaid in four years, even if no interest is charged the students still have to pay more than 600 Yuan each month, accounting for about 20-30 per cent of the average salary. In view of the current average income and consumption level, this amount is quite burdensome to those newly graduated students.

Higher-education institutions: ambiguous orientation and insufficient guidance

In the operation of the student loans scheme, higher-education institutions are actually the bridge between students and banks, and their role is too important to be disregarded. The student loans scheme is intended to promote needy students' access to education, so the institutions are also beneficiaries in this scheme. Most higher-education institutions support and welcome this scheme, but in practical operation the performance of some institutions is far from satisfactory.

(a) Ambiguous orientation in the Student Loans Scheme

In the process of promoting the Student Loans Scheme and reforming the recovery systems, a comparatively satisfactory student aid system has been established. There are mainly five measures to aid the students: scholarship, loan, grant, work-study and the waiving of tuition cost. According to this system, higher-education institutions should identify their own role and function correspondingly, but certain institutions rely too much on the government-subsidized student loans, they consider the loans as a 'miracle measure' in handling the problems of needy students, some

even mistake the loans for a kind of award. On the other hand, some higher-education institutions worry too much about the complicated procedures and the possible impacts and thus deliberately avoid their due responsibilities or even refuse the operation of the loans. According to the statistics, among all the higher-education institutions affiliated to the central ministries, 55 of them had not conducted the loan schemes by the end of May 2001.

(b) *Insufficient organization and guidance*

The higher-education institutions play a very special role in the loan-scheme chain; as for the banks, they are co-organizers; with regard to the students, they are ‘guiders’. But in reality, some institutions consider the loan operation is just the banks’ business and do not co-operate actively; this inevitably leads to the ideological obstacles in the loan schemes.

8.2 Suggestions for GSSLS reform

Banks: preventing and removing the possible loan risks

(a) *Establishing a nationwide system of individual credits*

At present, only two cities (Shanghai and Guangzhou) have tried to establish a system of individual credits and the system is merely citywide. In order to effectively prevent loan risks, the following steps may be worthwhile and necessary: first, build a nationwide system of the citizens’ individual credits and enable all the financial units to share the information; link this system with the National Student Status Administration Network of the Ministry of Education so that it will be more convenient for the banks to collect information regarding cases of contract breach, to examine the individual credit situation of the loan recipients, and to decide whether the loans should be granted or not. Since the rural population accounts for a very large proportion and there are many rural credit co-operative banks in the countryside, we do think it is an ideal way to make good use of this advantage and allow more students’ parents to apply for loans from the local banks or their branches. In this way, the students can obtain the loans more easily and promptly; at the same time, the risks of the GSSL can be minimized.

- (b) Establishing guarantee foundations and intermediate organizations for the student loans

The Jiangsu branch of the Industrial and Commercial Bank of China, the Jiangsu Provincial Bureau of Education and the Jiangsu Provincial Bureau of Finance advocated to set up ‘Jiangsu Guarantee Foundations for Student Loans’ to compensate for unpaid debts in regard to student loans, and to reward those advanced units or individuals in the operation of the student loans. The guarantee foundations not only mobilize people’s enthusiasm for participating in the student loans, but also remove the risks for the banks. Furthermore, it should be possible to resort to more social forces and establish intermediate organizations so that the risks of the student loans will not only be shouldered by the banks, but will also be shared by many sides involved in the loan schemes.

Students: flexible repayment conditions and stronger credit awareness

- (a) Prolonging the repayment period

Nowadays, the actual repayment period of the student loans is four years after graduation (most students are unable to repay the debts while still studying in college). Shortly after graduation, however, their earnings will be comparatively low and unstable. Consequently, the short repayment period forces them to suffer quite heavy repayment burdens. In some countries, the repayment period is more than 10 years, or even 20 years; students’ income levels after graduation are taken into full consideration. Actually, it is wrong to think that the shorter the repayment period, the easier to recover the loans. If the repayment period is prolonged, the loan recipients will be more financially capable of repaying the loans. If loans’ interest rate is the commercial interest rate, the banks will not suffer any loss in prolonging the repayment period. In this sense, the government will have to pay more subsidized-interest amounts, but the rate of subsidized interest can be adjusted in line with the repayment term. The reform should be a kind of ‘package reform’, not an isolated one. It would also be advisable to adjust the repayment according to the changes in income level: when the students earn more, they can choose to repay more and vice versa. This measure could not only alleviate the students’ repayment burden, but also reduce the cases of default.

(b) Strengthening the cultivation of credit awareness

As has been mentioned, in a survey in Guangdong Province, nearly 30 per cent of the student loan recipients had never heard of the ‘individual credit system’ and 20 per cent of them had never thought of the repayment; 7 per cent of them said “it’s hard to decide whether the repayment will be made” (Liu, 2001). In other words, nearly 57 per cent of them know very little about the regulations, credit systems and related laws of the student loans schemes. It is very urgent now to cultivate the credit awareness of the college students. Only if they realize the importance of credit in their social life will they try to safeguard their own individual credits.

Higher-education institutions: taking the loan business as their own responsibility

The student loans schemes made no special regulations regarding the responsibilities of higher-education institutions; but these institutions are also the potential beneficiaries of the loans. They should, for instance, attract more students, especially many excellent students to the institutions and allow tuition fees to flow into institution accounts more quickly. The institutions should co-operate actively with the banks. To be more precise, they should take initiatives in four aspects: promoting the student loans operation, guiding the students, co-operating with the banks, and sharing their due responsibilities. Special organizations should be set up and selected staff should be assigned to guide and help the students. For example, the institutions can help to target the needy students, gather and merge the information on the loan applicants, present the related documentation to the banks, and help to track the loan recipients after their graduation.

Government: making the GSSLS more feasible

(a) Reforming the procedures of verifying and cancelling the unpaid debts, sharing more risk and responsibility

Defaults are likely to occur when the students do not repay the loans in time and when it is difficult to track them after graduation. The current solution is the following: first, the commercial banks verify the ‘dead’ debts, then cancel them in the ‘reserved funds of the “dead” debts’ according to the actual pre-tax transaction amount, after the ‘cancel report’ has been approved by the headquarters of the lending bank. The banks

alone shoulder all the real losses, so their initiatives in operating the student loans will be severely affected. If the central government can share part of the risks, the flow of capital will not necessarily be restricted and the 'government-subsidy' features of the GSSLS can be better embodied.

- (b) Mobilizing the initiatives of the organizations and employees involved in GSSLS business

Independent statistics, settlement and checks should be conducted in the transaction of student loans so that the sale-tax-free policies can be better implemented. In addition, an attempt should be made to improve the procedures of verifying and cancelling the 'dead' debts. As long as the organizations and employees operate in a standardized and legal way, and their 'dead' debts are really beyond them, it will be unnecessary to be too harsh on them.

- (c) Improving the organizational structures and ensuring the financial funds for interest subsidy

By the end of August, 2001, appropriate local administrative organizations dealing with student loans had yet to be set up in 18 provincial bureaus of education, most of the student loan business was still conducted by other sections. Interest subsidies were still not in place in three provinces. All this will inevitably hinder the operation of the student loans schemes. As an important measure to promote higher-education reform, special organizations should be set up. The funds for interest subsidy should be guaranteed by the relative financial agency.

- (d) Perfecting the administration of the loans

Both the governments and the lending banks should attempt to perfect the administration of the loans in terms of procedures, checking systems, funds allocation and personnel assignment. If possible, the government should also decentralize the approving authority and simplify the procedures.

- (e) Deciding the subsidized interest rates scientifically

How to subsidize interest rates should be decided on two levels, as follows.

First, the rates of interest subsidy offered by central and local governments should be decided. Nowadays, the development of the economy in China is unbalanced; the disparity between the east and the west is still very distinctive. There lies a circulative relationship between economic development and the public-service level: the more backward the economy, the lower the service level. In order to offset this kind of disparity, the central financial authority should treat different regions in different ways when allocating the subsidized-interest funds. Based on the annual economic analysis of the State Statistics Bureau, the provinces, cities and autonomous regions can be grouped according to their economic status, and different rates of subsidized interest can be decided correspondingly. If the economic status is on the highest level, the central financial authority can request the local financial authority to provide all the funds for interest subsidy (50 per cent of the commercial interest rates); if the economic status is on the second level, central finance can provide 10-20 per cent of funds for interest subsidy and then request local finance to provide 30-40 per cent; if the economic status is on an even lower level, central finance can provide 20-30 per cent of funds for interest subsidy and then request local finance to provide 20-30 per cent; as for the extremely underdeveloped area, central finance can provide all the funds for interest subsidy so that the vicious circle in student loans can be avoided.

Second, setting the rates of subsidized interest provided to different students: at present, every student who obtains a loan can receive a subsidized interest rate of 50 per cent, if studying in an institution attached to a central ministry, regardless of family economic background. But, ideally, the government-subsidized interest rate should be student-oriented and should be decided according to the student's family economic status. If a rate of 50 per cent can be provided to averagely poor students, then the subsidized interest rate provided to the most needy students should be comparatively higher, maybe 70-80 per cent or even 100 per cent. Some countries have tried this method and we can refer to their experiences. The rate will be more reasonable and effective, as a result, and equity can be better achieved.

- (f) Favourable policies regarding exoneration from repayment of loans and interest

In order to minimize cases of repayment default and encourage the students to repay the loans on time, or even ahead of time, after graduation, favourable policies of exoneration from repayment should be established. If the students are willing to work in disadvantaged areas or take up work in much-needed professions, exemption from repayment should be granted to encourage and compensate them. Of course, restraints should also be set so that the loan beneficiaries can really make the choice by putting the benefits and needs of the country in paramount position within a certain period of time.

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Appendix
Table 1. Statistical data on the GSSLS by province (to May 2001)

	Applicants number (a)	Signed contracts number (b)	Ratio of (b)/(a) (%)	Applied loan fund (c) (Yuan)	Contracted loan funds (d) (Yuan)	Ratio of (d)/(c) (%)	Average loan (d)/(b) (Yuan)	Accumulative loan funds
Beijing	2,869	2,753	96	11,296,000	9,436,000	84	3,428	7,713,000
Fujian	1,242	200	16	4,991,000	770,000	15	3,850	770,000
Guangdong	7700	1995	26	71,530,000	26,620,000	37	13,343	6,354,000
Helongjiang	15,946	1291	8.1	71,490,000	5,420,000	7.6	4,198	4,270,000
Jiangsu	20,530	9655	47	10,700,740	5,188,550	48	537	2,559,980
Liaoning	20,800	6782	33	102,520,000	39,670,000	39	5,849	39,670,000
Shandong	7230	111	1.5	25,713,000	560,000	2.2	5,045	370,000
Shanghai	22752	21628	95	305,950,000	289,780,000	95	13,398	139,000,000
Tianjing	5118	2039	40	4,423,830	1,915,680	43	940	819,770
Zhejiang	8317	5997	72	45,282,600	36,000,000	80	6,003	30,157,359
Chongqing	13449	3069	23	66,592,000	23,470,000	35	7,647	15,172,000
Hainan	4135	415	10	49,600,000	3,650,000	7.4	8,795	1,460,000
Hebei	11958	1101	9.2	73,953,600	5,872,700	7.9	5,334	3,515,600
Henan	37658	5960	16	27,147,000	27,147,000	100	4,555	19,849,120

Hubei	44160	12444	28	364,190,000	59,450,000	16	4,777	59,450,000
Hunan	31903	4486	14	160,562,500	23,034,100	14	5,135	14,083,700
Inner Mongolia	11658	2680	23	61,598,000	26,737,000	43	9,976	12,576,000
Jiling	17636	1312	7.4	159,010,000	5,490,000	3.5	4,184	5,340,000
Shanxi	5000	—	—	15,000	—	—	—	—
Xingjiang	3417	12	0.4	17,360,000	43,000	0.2	3,583	43,000
Anhui	14406	2535	18	85,270,000	8,072,000	9.5	3,184	7,953,000
Gansu	7111	428	6	22,713,900	2,158,500	9.5	5,043	2,158,500
Guangxi	17721	286	1.6	92,544,800	1,718,400	1.9	6,008	286,400
Guizhou	9519	4673	49	78,083,000	21,172,000	27	4,531	11,343,000
Jiangxi	6253	923	15	31,594,600	4,935,000	16	5,347	2,496,900
Ningxia	1781	298	17	9,700,000	1,044,000	11	3,503	1,044,000
Qinghai	2598	—	—	9,820,600	—	—	—	—
Shanxi	10867	1000	9.2	74,219,300	5,480,000	7.4	5,480	1,214,300
Sichuan	7604	856	11	47,140,000	4,238,000	9	4,951	2,100,000
Tibet	1702	1472	86	15,620,000	14,188,000	91	9,593	4,799,000
Yunnan	18480	4819	26	94,145,440	18,884,600	20	3,919	10,976,710
Local institutions	392000	101000	25.8	2,190,000,000	670,000,000	30.6	6,634	—
Central institutions	142000	68000	47.9	1,150,000,000	585,000,000	50.9	8,603	—
Total in the country	533964	170089	31.9	3,337,525,828	1,262,994,870	37.8	7,425	633,068,004

Source: The National Centre for Student Loan Administration, Newsletter No. 2, 2001.

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