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NEWSLETTER

Welcome to the East Asian Bureau of Economic Research (EABER). EABER aims to be the premier East Asian economics research forum and provide a single point of reference for the economics, finance and governance research community throughout the region and beyond. Through building research capacity and partnering initiatives, EABER facilitates the creation of high-level analysis and forward thinking on issues of importance to the East Asian economy.

Analysis

Financing Higher Education in East Asia

Bruce Chapman and Peter Drysdale*

Human capital plays a key role in all economies, developed and developing. A decade ago, investment in primary and secondary education were seen as the main elements in human capital formation in developing economies. The priority was on broadening and deepening the base of literacy and numeracy in schools and not in building a cadre of liberal arts and science graduates through expanding higher education in the colleges and universities. Certainly effective and broad-based schooling is fundamental to expanding the skills-base in poor countries and a focus on earlier stage education has powerful appeal on equity grounds.

Today, higher education is recognised as a key input into the acquisition of know-how, technology and participation in the global knowledge based economy. The growth of Europe and America in particular is important because of the success of their universities. These knowledge based economies require high levels of human capital which influences a large number of economic outcomes and boosts long term productivity. Investment in higher education is a priority in industrialising economies as they seek the benefits from knowledge-based growth in the global economy. Strong and more broadly based higher education is now seen as a development policy priority. The constraints on investment in higher education are large even in the richest economies. They are palpable in a region like East Asia where the experience of, and ambition for, human capital to support rapid economic growth is so strong. The benefits of investment in higher education must be weighed carefully against the large costs associated with a quality higher education sector – particularly in developing countries with tight fiscal constraints.

Investment in higher education has a public payoff. That is why governments commonly invest significantly in providing it. But it also has a private payoff to those who benefit from it through the higher wages and salaries they earn in later life. An appropriate funding system for higher education needs to take into account both these elements (as well as others like providing easier access for the less well off). It needs help to overcome market failure in investing in higher education. But it should also mobilise investment in higher education by its recipients who benefit from it.

Countries in East Asia have tried various strategies for encouraging the expansion of higher education through private funding. Different forms of government supported student loan schemes are a common way of trying to expand the private financing of higher education. There is a real question of how best to arrange the resources to make sufficient investment in education that is accessible to everyone that can benefit from it. This is not easy particularly in the early stages of economic success where resources are stretched towards achieving many objectives.

There is much policy experience that can be drawn from other countries. This experience illuminates the challenges and options that face, and are open to, developing countries in East Asia. One role of government is to correct for market failure which occurs from the existence of the large positive externalities derived from a highly educated, capable workforce. Without government

Paper of the Month

The paper of the month for July 2008 was **RMB Exchange Rate and Local Currency Price Stability: The Case of China and ASEAN+3** by Xiao Bing Feng, Shanghai Academy of Social Sciences.

Latest News

South Asia-East Asia Workshops announced for Mumbai and Beijing later this year.

Conference on Institutional Strategies for Improving Micro Economic Policy Foundations was held in Columbia University, New York in June 2008.

DPU-ANU conference on Financing Higher Education was held in Bangkok last month.

The East Asia Forum has a new blog at eastasiaforum.wordpress.com

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subsidies these externalities lead to sub-optimal levels of investment in education. This is amplified by the inability of individuals to use human capital as collateral to make investments in their own education.

Because the market fails in the higher education sector there is a clear role for government to intervene, but possible interventions need to be carefully planned. One key element must be clear recognition of what the government wishes to achieve as this will play a large role in the optimal type of intervention.

The three main objectives of a government intervention into the higher education sector are: increasing the quantity, quality and access to higher education. Economic insight offers a number of lessons for the proper design of higher education schemes. These include promoting competition both amongst universities, and those wishing to attend. A corollary is the importance of promoting access to the sector for people from all segments of society. Many government supported schemes for financing higher education have failed. The student loans scheme in Indonesia was suspended. The student loans scheme in Thailand was transformed into an income contingent loan scheme and that in turn was abandoned.

Governments need to recognise the strengths of different types of support systems. They need to be designed to increase resources to the higher education sector and to provide an element of consumption smoothing on the lifetime of the individual beneficiaries of higher education, mainly the middle income classes.

Grant based or interest rate subsidy schemes on the other hand may be necessary to improve access to higher education – particularly for poorer segments of society.

Making a higher education financing system work requires the fiscal infrastructure to collect debts, through lending agencies or the tax system. A big question then is whether a country has these capacities for implementing and administering a student loan or higher education financing scheme. Countries need strong political support which is long term, enough bureaucratic capacity to ensure an effective administration and widespread public acknowledgement of the need for a higher education system and private contribution to its financing.

Country specificity is important in the design, implementation and ultimately, the effectiveness, of higher education financing schemes. In principle, income contingent loans for individual financing of higher education, repaid though the tax system when an appropriate income threshold is reached, are the preferred scheme for financing higher education. But in some countries the institutional framework might not be sufficiently robust to allow efficient, workable, collection of income contingent loans.

The Australian system offers some useful insights into the application of higher education financing in East Asia although it would be wrong to suggest that income contingent loans schemes are a panacea for all the challenges to financing higher education funding. There are many difficulties in design as well as other problems beyond the design of income contingent loans schemes that need to be part of effective strategies for funding higher education in East Asia and elsewhere.

**Bruce Chapman is Professor of Public Policy and Peter Drysdale is Emeritus Professor of Economics in the Crawford School of Economics and Government at the ANU. Over the past year, EABER from Crawford School, has been working with DPU in Bangkok on a large collaborative project on Financing Higher Education in East Asia(http://www.eaber.org/intranet/publish/Public/Project_DPUANU.php). A conference was held on the results of this work on 15-16 July 2008 in Bangkok.*

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