Children’s savings accounts—whether designated for school or not—are positively associated with college enrollment and graduation, (b) having savings designated for school is more strongly related to educational outcomes than having basic savings, and (c) if children’s savings (school-designated or basic) are associated with college graduation. We also review a study of the association between parents’ college savings and children’s college loan debt. Based on evidence from the research, we suggest that policies and programs clearly state their goals. For example, if the goal is to improve expectations for attending and graduating from college, promoting small-dollar children’s savings accounts might make a difference. However, if the goal is to reduce college debt, policies must help children and parents accumulate enough savings to pay college costs and reduce reliance on loans.

Small-Dollar Children’s Savings Accounts

Evidence suggests that having school savings might be as closely associated with college outcomes as the amount in it. Children with $1 to $499 designated
for school are 2.5 times more likely to enroll in and graduate from college than children with no account, which suggests that saving and wealth-building policies to improve college enrollment and graduation rates might have positive effects even when children save small amounts.

If improving college enrollment and graduation outcomes is the goal, programs that (a) incorporate accounts specifically for school savings and/or (b) encourage children to designate a portion of savings for school might be more effective than programs that promote saving without encouraging children to link savings to college. Previous research\(^4\) has suggested that programs promoting children’s savings for school have a positive effect on college enrollment and that the positive effects are more likely to occur for LMI children than HI children.\(^5\)

### Mental Accounting

The positive effects of having a savings account—even if it contains a very small amount of money—could be the result of mental accounting. Mental accounting is the process of assigning money to categories,\(^6\) which affects when and how people use it.\(^7\) It also might affect formation of identities by influencing the way children view themselves. Small-dollar accounts with money mentally designated for school might affect educational outcomes\(^8\) positively by helping children see themselves as college bound. They also may signal to children that future savings\(^9\) can finance college. Expected future savings might be as important as current savings—or at least a sufficient reason—for believing that college is within reach and requires action.\(^10\) Finally, designating money for college indicates that children believe that people like them can go to college. These findings suggest that school-designated savings are more effective than basic savings in influencing college outcomes.

### Household Income and College Outcomes

Overall, findings suggest that having even a small amount of savings designated for school can have a positive effect on LMI children’s graduation rates (Figure 1). When contrasted with an LMI child with no savings account, an LMI child with school savings of $1 to $499—either in a physical savings account or mentally set aside—before college age is more than three times more likely to enroll in college and more than 4.5 times more likely to graduate from college. In addition, an LMI child with school savings of $500 or more is about five times more likely to graduate from college than a child with no savings account.

Findings also suggest that designating less than $1 for school is associated with college enrollment, which may be based on the cumulative psychological effects of having savings. That is, children with school-designated savings—even very small amounts—may be better prepared academically for the rigors of college because of early engagement and achievement in school.\(^11\)

While having a small-dollar account might signal to a child that financing college is possible, it is less realistic to expect children to save money for school once they are in college. Therefore, part of the effect of school savings on college persistence might have to do with having enough savings on hand to pay actual college expenses and avoid accruing detrimental amounts of student loan debt.

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**Figure 1. LMI children who graduate from college by savings amount**
Student Loan Debt

Rising college costs, stagnant or decreasing family wages, and changing federal and state policies are pressuring students to rely more on borrowing. Since the late 1970s, the federal government increasingly has attempted to promote equal access through policies that make college loans accessible to more students. The amount of student debt is growing:

- During the 2011-2012 school year, 37% of all undergraduate financial aid received ($70.8 billion) came from federal loans.
- The percentage of undergraduate students who obtained federal loans increased from 23% in 2001-2002 to 35% in 2011-2012.
- In 2010-2011, nearly 57% of public four-year college students graduated with debt.
- On average, students who attended public four-year colleges borrowed $23,800.
- Total borrowing for college hit $113.4 billion for the 2011-2012 school year, up 24% from 2007.

Policymakers tend to believe that individual students should bear more personal responsibility because they benefit most from attending college, so there might be very little political will to increase the number of scholarships and grants available to students. The shift from need-based aid—determined solely by assets and income (i.e., financial need) of prospective students and their families—to merit-based aid—most commonly scholarships that are awarded based on test scores—also determines the amount that students potentially must borrow to pay for college.

Students with little financial need have the same entitlement to merit-based aid as students with significant financial need.

High-Dollar Student Loans

Research suggests that (a) high-dollar student loans ($10,000 or more) in particular can reduce the probability that students—especially those from lower income households—persist in and graduate from college and (b) parents’ college savings may reduce the probability that LMI students accrue high-dollar student loan debt.

A particularly strong predictor of whether students take out high-dollar loans is the amount of money they expected as children to borrow in the future. Students who expected to borrow $10,000 or more were far more likely to have taken out high-dollar amounts. Some research suggests that students may gain a boost in self-esteem and a sense of mastery from taking out student loans, which may encourage them to take out additional loans. However, this sense of mastery begins to fade over time.

Undesired Effects of High Student Debt

As a policy mechanism, student loans are designed to ensure that more students have access to college by providing funds at the time of enrollment, but graduation rates may decrease once borrowed amounts reach a certain level. Students may be more likely to drop out of college once loans become too high ($10,000 or more). Those who take on high-dollar loans early in their college careers may not have realistic expectations about what they can afford to pay back and may become averse to taking out additional loans necessary to graduate. Research also suggests that student loans may be a more effective strategy for middle- and high-income students because of low-income students’ aversion to borrowing.

These findings suggest that continuing to increase the amount of loans available to students without the inclusion of other complementary financial aid policies might not result in higher rates of college persistence.

Parents’ College Savings

Research on CDAs has focused primarily on educational attainment and children’s college expectations, but one policy argument for adopting CDAs is that they can help reduce college debt. Given this, it seems important to determine whether an association exists between assets—such as CDAs or parents’ college savings, as in this discussion—and college debt. Evidence indicates that parents’ having college savings helps reduce the likelihood that students will take out high-dollar loans in all subsamples except HI students. Also,

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5This section is based on Elliott, W., & Nam, I. (2013). Reducing student loan debt through parents’ college savings (CSD Working Paper 13-07). St. Louis, MO: Washington University, Center for Social Development. This paper uses longitudinal data from the Educational Longitudinal Survey of 2002 (ELS:2002) from the National Center for Education Statistics (NCES). The survey began in 2002 when students were in 10th grade, and follow-up waves took place in 2004 and 2006.
students are more likely to report paying for four-year college attendance with family contributions when their parents have college savings accounts. Reducing the amount of college debt accrued by LMI and male students—for whom debt may have a more negative effect on persistence—may be more important than finding ways to reduce debt amassed by HI students. ²¹

The continually increasing number and amount of student loans suggest that grants are doing very little to reduce the need for them. This implies that there is a need to increase the amount of grant aid available or that other strategies that align better with the American ideal of personal responsibility (e.g., saving).

Conclusion

Evidence suggests that college savings can be part of a strategy to help increase college enrollment and graduation rates and reduce student loan debt amounts. However, savings must be sufficient to pay for actual college expenses to effectively reduce the amount of student loan debt accrued. Some research suggests that debt over $10,000 can have adverse effects on students’ persistence in college,²² but students who do graduate have about $24,000 in debt on average.²³ How can we expect students and their parents, particularly those who are low-income, to save at least $14,000 for college? One way to overcome this obstacle might be to open savings accounts as early as birth. In addition to starting early, CDAs and other savings policies that provide students with financial incentives such as initial deposits, savings matches, and the opportunity for third-party deposits might achieve the greatest effect on college enrollment and graduation rates and reduce the amount of student loan debt.

Endnotes


3. I would like to thank Dr. Terri Friedline for suggesting the phrase “small-dollar accounts.”


5. Income categories used in Elliott (2012) and Elliott, Song, & Nam (2012) are based on data from the PSID and CDS are as follows: LMI families are those whose income is under $50,000, and HI families are those whose income is $50,000 or more.


9. The median age at the time of the CDS was 16.10 years.


15. The following income categories used in Elliott & Nam (2013) are based on data from ELS:2002: low-income ($35,000 or below), moderate-income ($35,001-$75,000), middle-income ($75,001-$100,000), high-income ($100,001 or higher).


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