How Much College Debt Is Too Much?

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(NAPSA)—Student loans are usually classified as “good” debt. Like a mortgage or a business loan, borrowing for education can be a smart investment in your future. Too many of today’s students and their parents, though, are taking a good thing too far.

Some people are $30,000, $40,000 or more in debt from student loans, yet can’t find work in their fields. Even if you graduate with the average level of education debt—about $18,000—you may be jeopardizing your finances. Many graduates find their loan payments are so big that they can’t save for other goals, such as a house or retirement.

Putting off these goals to pay debt is an expensive choice. A 22-year-old’s $3,000 Roth IRA contribution, for example, could grow to more than $95,000 by the time she’s eligible for full Social Security benefits. Start at age 32, and the contributions grow less than half as big, to about $44,000.

It’s up to you to put limits on how much debt you’re willing to incur. How much is too much? Obviously, the less borrowing you have to do, the better:

- If you’re a student, your payments shouldn’t exceed 10 percent of your expected monthly gross income once you graduate.
- If you’re a parent, all your debts—including mortgage payments, credit cards, car loans and education loans—shouldn’t eat up more than 35 percent of your gross pay.
- Once you start borrowing, keep track of your debt. It’s easy to get confused about how much you owe.

At eight percent, each $1,000 you borrow will cost you about $12 a month to repay. If you’re a student and you borrow the maximum allowed under current federal student loan programs—$23,000 in subsidized and unsubsidized borrowing—your monthly payments will be around $276.

That payment level should be manageable if you’re making at least $33,000, which means you’d better be an accounting or business major. Starting salaries in those fields currently range from around $36,000 for business administration types to $43,000 for management information systems graduates. Liberal arts grads, on the other hand, generally have to settle for salaries under $30,000 to start.

Before they get into debt, parents and students should discuss how much they need to borrow.

Yes, your salary should go up over time, which should in theory make your payments more manageable. But your financial obligations also will multiply. You’ll want to buy a home, hook up with that special someone, perhaps have kids. You’ll need cars, furniture, retirement savings and college savings for your own offspring.

No heroics from the parents

Parents, too, need to put limits on their borrowing, since too much debt can keep them from adequately funding their other goals, such as saving for retirement.

Parents should avoid the temptation to tap all their home equity to pay for a child’s college education. If you borrow more than 80 percent of the value of your home, including your first mortgage, you pay higher interest rates and have little cushion left for emergencies.

Some alternatives

What if you find you can’t prudently borrow the amount you need for school? Then you should consider some alternatives, such as:

- If you’re the student, look for a college that wants you. Your financial aid package will be much more attractive at a school that’s trying to recruit you.
- Consider lower-cost alternatives. Attending a two-year school and then transferring to a four-year institution is a good way to cap costs. So is opting for a public university rather than a private one.
- Get a job. Most students can help contribute at least some of their college costs.

For more college budgeting tips and tools, visit the planning section on CNBC on MSN Money (www.money.msn.com), or use the budgeting tools offered in the Microsoft Money software.

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