

# An Analysis of the Consequences of Relying on Human Capital Theory to Develop Educational Policies

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**Abstract:** The emergence and development of human capital theory is undoubtedly a major event in the labour market field. It has both positive and negative effects on the development of education. The key points are as follows: (1) Investment in human capital is important in the knowledge-based global economy and education is an important way of breaking the intergenerational cycle of poverty, which benefits people's lives and lifts their nations. (2) Overemphasizing human capital theory and the return of investment will lead to the lack of education quality. (3) Human capital theory optimistically connects the economic benefits with higher education investment, but it can also lead to the problem of over-qualification in the labour market, which may bring waste of human capital and education resources.

## 1. Introduction

Human capital is an important factor in economic growth. Investing in education can improve the stock of human capital. It has played a positive role in attaching importance to society and vigorously developing education to promote economic development. However, due to its own limitations and shortcomings, in a sense, it has brought many negative effects to the development of education, which has caused modern education to fall into various crises. This research briefing aims to understand the consequences of relying on human capital theory to develop education and training policies and find out the short come of this method in order to propose measures to improve education quality.

## 2. Literature Overview of Human Capital Theory

Labour force was considered to be the main force of economic progress (Adam Smith, 1776). Human capital investment can be done by private investment behaviours that pursue profit. Countries can promote, encourage, and even force all citizens to receive the most basic education. The theory of human capital was first brought up by American economist Schultz in the 1960s. Schultz (1961) believed that the accumulation of human capital was the source of social and economic growth. He also analysed the benefits of investment in education, arguing that investment in education can increase the income of both society and educators. The difference in income between people lies in the difference in the amount and the differences of education investment. He also calculated the rate of return of education at all levels, which proved that investing in different types and levels of education would bring different rates of return.

Human capital theory is the theoretical cornerstone of educational economics. This theory clearly points out the internal mechanism and external benefits of education and economic growth. The importance of human capital investment, including investment in education, lies in the growth of national economic and increase of personal and household income. In 1962, American economist Denison analysed the growth factors and pointed out that 23% of the US economic growth contribution from 1929 to 1957 came from investment in education. According to the results of empirical analysis, higher education investment has contributed greatly to the overall return on education investment. Becker (1993) clearly deduced the impact of investment in education on

personal income. It can be seen that the long-term return of education makes investment in education more prominent, that is, education can play a role in many areas of the future economy, such as promoting the increase of personal income.

### **3. Education and Economic Performance**

The introduction of human capital theory attaches importance to the promotion of the quality of laborers to the promotion of economic development, which has certain positive significance. Investment in human capital is important in the knowledge-based global economy. Human capital theory believes that education investment can continuously promote the sustainable development of the economy than other material investment, and the marginal benefit of education investment is increasing. Studies in the fields of economics and sociology have shown a positive relationship between education and income. What's more, individuals with a high degree of education have higher productivity and higher incomes and education is one of the best solutions of poverty, which benefits human lives and lift their countries. There is a very important point in the theory of human capital: Education investment is the core of human capital and the key to improving the quality of the population. This is because the aim of achieving better profits can lead to increasing numbers of labours with higher skills, more working experience, which can improve job satisfaction, commitment levels and better communication (Keep and Mayhew, 1988).

In order to measure the rate of return on investment in education, human capital theory also proposes a basic formula:  $\text{income} / \text{cost} = \text{rate of return}$ . To maximize the rate of return, the denominator must be minimized and the numerator maximized. This may greatly promote the development of those education that directly produces economic benefits, such as vocational and higher education. In China, government and individual investment in higher education has grown rapidly in recent years, and the number of people receiving higher education has also increased substantially. Under the background of enrolment expansion, China's higher education has gradually changed from elite education to popular education. From the perspective of human capital theory, this will increase the stock of human capital in China, which provides a reliable and sustainable development for China's economy and also brings certain economic benefits to individuals and families. However, after the implementation of higher education enrolment policy in 1999, the number of college graduates increased rapidly, and the employment situation became severe. The employment rate of college graduates from 1996 to 2004 were 93.7%, 97.1%, 76.8%, 79.3%, 82.0%, 90.0%, 80.0%, 70% and 73%, which was a downward trend overall (Lai and Tian, 2005). It can be seen that the unreasonable educational structure caused by China's excessive emphasis on the development of higher education is an important factor of over-education problem.

## **4. The consequences of relying on human capital theory to develop education**

### **4.1 Lack the Quality of Education**

Overemphasizing the output and rate of return of investment can lead to the loss of education development and make the pursuit of profit maximization as the fundamental goal. Human capital theory believes that human capital is an important factor in economic growth, and human capital is regarded as a supplier of power resources for economic development. Although it has its rationality in the economic field, it seriously violates the essence of education in the field of education. Because this kind of education has direct economic temptation, people are willing to invest more money and energy. However, for some basic education which is not closely related to the market, it may be difficult to produce obvious and direct economic benefits.

Human capital theory believes that special knowledge and specialized human capital are important factors in promoting economic growth. That is to say, it emphasizes professional education. However, those who are cultivated under such educational concepts are not a comprehensive and complete person. This will inevitably lead to narrow personal knowledge and reducing social adaptability. Especially in today's highly differentiated and highly integrated

disciplines, one-sided emphasis on professional education is even more difficult.

Judging from the current employment situation of higher education and its benefits, how to balance the investment ratio of education investment and other material investment is a more important issue. In reality, investment in education does not necessarily lead to productivity improvement, equality of national economic income, and decline in unemployment rate. The marginal benefit of education investment will be affected by social systems and economic environment in the actual process.

#### **4.2 Over-qualification in the Labour Market**

Since the late 1960s and early 1970s, the western developed countries have experienced the relative surplus of labour education to varying degrees. The specific performance is that some highly educated workers are engaged in work originally undertaken by low-educated workers, which exceeds the level of education required for the work they are doing. This phenomenon is called over-qualification in the labour market (Freeman, 1976). As illustrated in Table 1, it shows the demand and supply of different work-force level in UK, which can be seen that overeducation problem exists in every level of qualifications and this can lead to over-qualification when they go to work.

In the meta-analysis by Groot and Maassen van den Brink (2000), it analyses whether overeducation causes loss of personal income and explores the sources of income differences under different matching conditions. The study found that overeducators did not bear any increase of income compared to moderately educated people at the same level of education, while those with inadequate education enjoyed a certain income premium. In addition, the results of the analysis indicate that there is a significant difference in the income of individuals in different matching states, and the income is also significantly different in gender, education, work experience, work location and region, and the four variables of the department and the matching state have significant interaction effects on income.

Over-qualification can have a negative effect on personal productivity and income, reduce the rate of return on education, and even make the additional level of education fail to receive appropriate compensation. Although the rate of return on overeducation is positive, it is less than the rate of return to required education for work, indicating that the portion of overeducation still produces income, but its role in increasing income is greatly reduced.

Human capital theory incorporates education investment into human capital investment. Since it is an investment, it can take certain risks while obtaining economic benefits, regardless of country, family or individuals. Although the theory optimistically analyses and measures the economic benefits of higher education investment, it should also be clear that this investment may bring huge capital waste.

#### **5. Suggestions**

Firstly, return to the essence of education and seek the subjective value of individuals. Human capital theory emphasizes the economic function and benefits of education, and advocates that high income is connected to high-level education. Views such as these seriously deviate from the essence of education. Education should not be motivated by profit, but a way of exploring, understanding the purpose of life, and finding the right way through it. Although people can really get a lot of profit from education, but it is naturally formed as a result not the purpose of it. Therefore, awakening the subjectivity of individuals is the fundamental duty of modern education. Today's knowledge-based economy emphasizes innovation in particular, and innovation cannot be separated from human subjectivity. Promoting the subjective value of the human being should be the goal pursued by modern education.

Secondly, guide graduates to rationally plan their career path. Human capital theory encourages individuals to take further education and use temporary income losses to win future long-term income increase and career development. However, as the work life increases, the overeducation population does not have a faster income growth, which does not lead to higher income or faster

promotion. At this point, overeducation will cause waste of human capital for a period of time, which is a loss to individuals, enterprises and society. Therefore, educational institutions should guide graduates to find jobs that match their educational level and improve the quality of employment.

Thirdly, adjust the structure of education expenditure between higher education, secondary education, basic education, and vocational training. According to human capital theory, the higher the education levels of a person, the higher his income level. This will inevitably make society and individuals realize that in order to achieve high incomes; they must be educated in high education. The result is an unprecedented expansion in the demand for academic education. In order to survive and develop, many schools have to find ways to meet social needs as much as possible. Governments are supposed to take measures to stop wasting the scarce education resources, because overeducation caused by unreasonable input structure reduces the income of education investment and the efficiency of labour market operation.

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