The Economics of Racism

by Michael Reich

Michael Reich is Professor of Political Economy at U. C. Berkeley. This article was written in 1974, hence used only data available at that time. His research was repeated on later census data in his book Racial Inequality: A Political-Economic Analysis*, (Princeton, N.J.: Princeton University Press), 1981, and by other researchers, with similar results. His main thesis is that most workers are harmed by racism, regardless of their race. Reich believes this analysis to be based on ideas from Marx, but whether Marx would agree with his assumptions about how wages are determined is debatable.*

In the early 1960s it seemed to many that the elimination of racism in the U.S. was proceeding without requiring a radical restructuring of the entire society. There was a growing civil rights movement, and hundreds of thousands of blacks were moving to Northern cities where discrimination was supposedly less severe than in the South. Government reports pointed to the rapid improvement in the levels of black schooling as blacks moved out of the South: in 1966 the gap between the median years of schooling of black males aged 25 to 29 and white males in the same age group had shrunk to one-quarter the size of the gap that had existed in 1960.[1] By 1970, however, the optimism of earlier decades had vanished. Despite new civil rights laws, elaborate White House conferences, special ghetto manpower programs, the War on Poverty, and stepped-up tokenist hiring, racism and the economic exploitation of blacks has not lessened. During the past twenty-five years there has been virtually no permanent improvement in the relative economic position of blacks in America. Median black incomes have been fluctuating at a level between 47 percent and 63 percent of median white incomes, the ratio rising during economic expansions and falling to previous low levels during recessions.[2] Segregation in schools and neighborhoods has been steadily increasing in almost all cities, and the atmosphere of distrust between blacks and whites has been intensifying. Racism, instead of disappearing, seems to be on the increase.

Besides systematically subjugating blacks so that their median income is 55 percent that of whites, racism is of profound importance for the distribution of income among white landowners, capitalists, and workers. For example, racism clearly benefits owners of housing in the ghetto where blacks have no choice but to pay higher rents there than is charged to whites for comparable housing elsewhere in the city. But more importantly, racism is a key mechanism for the stabilization of capitalism and the legitimization of inequality. We shall return to the question of who benefits from racism later, but first we shall review some of the economic means used to subjugate blacks.

THE PERVASIVENESS OF RACISM

Beginning in the first grade, blacks go to schools of inferior quality and obtain little of the basic training and skills needed in the labor market. Finding schools of little relevance, more in need of immediate income, and less able anyway to finance their way through school, the average black student still drops out at a lower grade than his white counterpart. In 1974 only 8.1 percent of blacks aged 25 to 34 were college graduates, compared to 21.0 percent of whites in the same age bracket.[3]

Exploitation really begins in earnest when the black youth enters the labor market.

[1] U.S. Department of Labor, Bureau of Labor Statistics, Report No. 375, "The Social and Economic Status of Negroes in the United States, 1969," p. 50.

[2] The data refer to male incomes: see Table 10-A, p. 360.

[3] U.S. Bureau of the Census, Series P-60, "Educational Attainment."

A black worker with the same number of years of schooling and the same scores on achievement tests as a white worker receives much less income. The black worker cannot get as good a job because the better-paying jobs are located too far from the ghetto or because he or she was turned down by racist personnel agencies and employers or because a union denied admittance or maybe because of an arrest record. Going to school after a certain point doesn't seem to increase a black person's income possibilities very much. The more educated a black person is, the greater is the disparity between his income and that of a white with the same schooling. The result: in 1966 black college graduates earned less than white high school dropouts.[4] And the higher the average wage or salary of an occupation, the lower the percentage of workers in that occupation who are black.

The rate of unemployment among blacks is generally twice as high as among whites.[5] Layoffs and recessions hit blacks with twice the impact they hit whites, since blacks are the "last hired, first fired." The ratio of average black to white incomes follows the business cycle closely, buffering white workers from some of the impact of the recession.

Blacks pay higher rents for inferior housing, higher prices in ghetto stores, higher insurance premiums, higher interest rates in banks and lending companies, travel longer distances at greater expense to their jobs, suffer from inferior garbage collection and less access to public recreational facilities, and are assessed at higher property tax rates when they own housing. Beyond this, blacks are further harassed by police, the courts, and the prisons.

When conventional economists attempt to analyze racism they usually begin by trying to separate various forms of racial discrimination. For example, they define "pure wage discrimination" as the racial differential in wages paid to equivalent workers—that is, those with similar years and quality of schooling, skill training, previous employment experience and seniority, age, health, job attitudes, and a host of other factors. They presume that they can analyze the sources of "pure wage discrimination" without simultaneously analyzing the extent to which discrimination also affects the factors they hold constant.

But such a technique distorts reality. The various forms of discrimination are not separable in real life. Employers' hiring and promotion practices; resource allocation in city schools; the structure of transportation systems; residential segregation and housing quality; availability of decent health care; behavior of policemen and judges; foremen's prejudices; images of blacks presented in the media and the schools; price gouging in ghetto stores—these and the other forms of social and economic discrimination interact strongly with each other in determining the occupational status and annual income, and welfare, of black people. The processes are not simply additive but are mutually reinforcing. Often, a decrease in one narrow form of discrimination is accompanied by an increase in another form. Since all aspects of racism interact, an analysis of racism should incorporate all its aspects in a unified manner.

No single quantitative index could adequately measure racism in all its social, cultural, psychological, and economic dimensions. But while racism is far more than a narrow economic phenomenon, it does have very definite economic consequences: blacks have far lower incomes than whites. The ratio of median black to median white incomes thus provides a rough, but useful, quantitative index of the economic consequences of racism for blacks. We shall use this index statistically to analyze the causes of racism's persistence in the United States. While this approach overemphasizes the economic aspects of racism, it is nevertheless an improvement over the narrower approach taken by conventional economists.

COMPETING EXPLANATIONS OF RACISM

How is the historical persistence of racism in the United States to be explained? The most prominent analysis of discrimination among economists was formulated in 1957 by Gary Becker in his book, *The Economics of*

[4] U.S. Bureau of the Census, Series P-60, "Income in 1966 of Families and Persons in the United States."

[5] See, for example, U.S. Department of Labor, *Manpower Report of the President*, various years.

Discrimination.[6] Racism, according to Becker, is fundamentally a problem of tastes and attitudes. Whites are defined to have a "taste for discrimination" if they are willing to forfeit income in order to be associated with other whites instead of blacks. Since white employers and employees prefer not to associate with blacks, they require a monetary compensation for the psychic cost of such association. In Becker's principal model, white employers have a taste for discrimination; marginal productivity analysis is invoked to show that white employers lose while white workers gain (in monetary terms) from discrimination against blacks.

Becker does not try to explain the source of white tastes for discrimination. For him, these attitudes are determined outside of the economic system. (Racism could presumably be ended simply by changing these attitudes, perhaps by appeal to whites on moral grounds.) According to Becker's analysis, employers would find the ending of racism to be in their economic self-interest, but white workers would not. The persistence of racism is thus implicitly laid at the door of white workers. Becker suggests that long-run market forces will lead to the end of discrimination anyway: less discriminatory employers, with no "psychic costs" to enter in their accounts, will be able to operate at lower costs by hiring equivalent black workers at lower wages, thus bidding up the black wage rate and/or driving the more discriminatory employers out of business.

The approach to racism argued here is entirely different. Racism is viewed as rooted in the economic system and not in "exogenously determined" attitudes. Historically, the American Empire was founded on the racist extermination of American Indians, was financed in large part by profits from slavery, and was extended by a string of interventions, beginning with the Mexican War of the 1840s, which have been at least partly justified by white supremacist ideology. Today, by transferring white resentment toward blacks and away from capitalism, racism continues to serve the needs of the capitalist system. Although individual employers might gain by refusing to discriminate and hiring more blacks, thus raising the black wage rate, it is not true that the capitalist class as a whole would benefit if racism were eliminated and labor were more efficiently allocated without regard to skin color. We will show below that the divisiveness of racism weakens workers' strength when bargaining with employers; the economic consequences of racism are not only lower incomes for blacks but also higher incomes for the capitalist class and lower incomes for white workers. Although capitalists may not have conspired consciously to create racism, and although capitalists may not be its principal perpetuators, never-the-less racism docs support the continued viability of the American capitalist system.

We have, then, two alternative approaches to the analysis of racism. The first suggests that capitalists lose and white workers gain from racism. The second predicts the opposite—capitalists gain while workers lose. The first says that racist "tastes for discrimination" are formed independently of the economic system; the second argues that racism interacts symbiotically with capitalistic economic institutions.

The very persistence of racism in the United States lends support to the second approach. So do repeated instances of employers using blacks as strikebreakers, as in the massive steel strike of 1919, and employer-instigated exacerbation of racial antagonisms during that strike and many others.[7] However, the particular virulence of racism among many blue- and white-collar workers and their families seems to refute our approach and support Becker.

SOME EMPIRICAL EVIDENCE

Which of the two models better explains reality? We have already mentioned that our approach predicts that capitalists gain and workers lose from racism, whereas the conventional Beckerian approach predicts pre-

[6] Gary Becker, *The Economics of Discrimination* (Chicago: University of Chicago Press, 1957).

[7] See, for example, David Brody, *Steelworkers in America*: *The Nonunion Era* (Cambridge: Harvard University Press, 1966); Herbert Gutman, "The Negro and the United Mineworkers," in *The Negro and the American Labor Movement*, ed. J. Jacobson (New York: Anchor, 1968); S. Spero and H. Harris, *The Black Worker* (New York: Atheneum, 1968), passim.

cisely the opposite. In the latter approach racism has an equalizing effect on the white income distribution, whereas in the former racism has a disequalizing effect. The statistical relationship between the extent of racism and the degree of inequality among whites provides a simple yet clear test of the two approaches. This section describes that test and its results.

First, we need a measure of racism. The index we use, for reasons already mentioned, is the ratio of black median family income to white median family income (abbreviated as B/W). A low numerical value for this ratio indicates a high degree of racism. We calculated values of this racism index using data from the 1960 Census, for each of the largest forty-eight metropolitan areas (boundaries are defined by the U.S. Census Bureau, who use the term *standard metropolitan statistical areas*—SMSA's). There is a great deal of variation from SMSA to SMSA in the B/W index of racism, even within the North; Southern SMSA's generally demonstrated a greater degree of racism. The statistical techniques used are based on this variation.

We also need measures of inequality among whites. Two convenient measures are: (1) the percentage share of all white income that is received by the top 1percent of white families; and (2) the Gini coefficient of white incomes, a measure which captures inequality within as well as between social classes.[8]

Both of these inequality measures vary considerably among the SMSA's; there is also a substantial amount of variation in these within the subsample of Northern SMSA's. Therefore, it is very interesting to examine whether the pattern of variation of the inequality and racism variables can be explained by causal hypotheses. This is our first source of empirical evidence.

A systematic relationship across SMSA's between our measure of racism and either measure of white inequality does exist and is highly significant: where racism is greater, income inequality among whites is also greater.[9] This result is consistent with our model and is inconsistent with the predictions of Becker's model.

This evidence, however, should not be accepted too quickly. The correlations reported may not reflect actual causality since other independent forces may be simultaneously influencing both variables in the same way. As is the case with many other statistical analyses, the model must be expanded to control for such other factors. We know from previous inter-SMSA income distribution studies that the most important additional factors that should be introduced into our model are: (1) the industrial and occupational structure of the SMSA's; (2) the region in which the SMSA's are located; (3) the average income of the SMSA's; and (4) the proportion of the SMSA population that is black. These factors were introduced into the model by the technique of multiple regression analysis. Separate equations were estimated with the Gini index and the top 1 percent share as measures of white inequality.

All the equations showed strikingly uniform statistical results: racism as we have measured it was a significantly disequalizing force on the white income distribution, even when other factors were held constant. A I percent increase in the ratio of black to white median incomes (that is, a 1 percent decrease in racism) was associated with a .2 percent decrease in white inequality, as measured by the Gini coefficient. The corresponding effect on top 1 percent share of white income was two and a half times as large, indicating that most of the inequality among whites generated by racism was associated with increased income for the richest 1 percent of white families. Further statistical investigation reveals that increases in the racism variable had an insignificant effect on the. share received by the poorest whites and resulted in a decrease in the income share of the whites in the middle income brackets.[10] This is true even when the

[8] The Gini coefficient varies between 0 and 1, with 0 indicating perfect equality and 1 indicating perfect inequality. For a more complete exposition, see H. Miller, *Income Distribution in the United States* (Washington, D.C.: U.S. Government Printing Office, 1966).

[9] For example, the correlation coefficient between the B/W measure of racism and the Gini coefficient of white incomes is r = -.47. A similar calculation by S. Bowles, across states instead of SMSA's, resulted in an r = -.58.

[10] A more rigorous presentation of these and other variables and the statistical results in available in Michael Reich, "Racial Discrimination and the White

Southern SMSA's are excluded.

Within our model, we can specify a number of mechanisms that further explain the statistical finding that racism increases inequality among whites. We shall consider two mechanisms here: (1) total wages of white labor are reduced by racial antagonisms, in part because union growth and labor militancy are inhibited; (2) the supply of public services, especially in education, available to low- and middle-income whites is reduced as a result of racial antagonisms.

Wages of white labor are lessened by racism because the fear of a cheaper and underemployed black labor supply in the area is invoked by employers when labor presents its wage demands. Racial antagonisms on the shop floor deflect attention from labor grievances related to working conditions, permitting employers to cut costs. Racial divisions among labor prevent the development of united worker organizations both within the workplace and in the labor movement as a whole. As a result, union strength and union militancy will be less the greater the extent of racism. A historical example of this process is the already mentioned use of racial and ethnic divisions to destroy the. solidarity of the 1919 steel strikers. By contrast, during the 1890s, black-white class solidarity greatly aided mineworkers in building militant unions among workers in Alabama, West Virginia, and other coalfield areas.[11]

The above argument and examples contradict the common belief that an exclusionary racial policy will strengthen rather than weaken the bargaining power of unions. Racial exclusion increases bargaining power only when entry into an occupation or industry can be effectively limited. Industrial-type unions are much less able to restrict entry than craft unions or organizations such as the American Medical Association. This is not to deny that much of organized labor is egregiously racist or that some skilled craft workers benefit from racism.[12] But it is important to distinguish actual discriminatory practice from the objective economic self-interest of most union members.

The second mechanism we shall consider concerns the allocation of expenditures for public services. The most important of these services is education. Racial antagonisms dilute both the desire and the ability of poor white parents to improve educational opportunities for their children. Antagonisms between blacks and poor whites drive wedges between the two groups and reduce their ability to join in a united political movement pressing for improved and more equal education. Moreover, many poor whites recognize that however inferior their own schools, black schools are even worse. This provides some degree of satisfaction and identification with the status quo, reducing the desire of poor whites to press politically for better schools in their neighborhoods. Ghettos tend to be located near poor white neighborhoods more often than near rich white neighborhoods; racism thus reduces the potential tax base of school districts containing poor whites. Also, pressure by teachers' groups to improve all poor schools is reduced by racial antagonisms between predominantly white teaching staffs and black children and parents.[13]

The statistical validity of the above mechanisms can be tested in a causal model. The effect of racism on unionism is tested by estimating an equation in which the percentage of the SMSA labor force that is unionized is the dependent variable, with racism and the structural variables (such as the SMSA industrial structure) as the independent variables. The schooling mechanism is tested by estimating a similar equation in which the dependent variable is inequality in years of schooling completed among white males aged 25 to 29.

Once again, the results of this statistical test strongly confirm the hypothesis of our model. The racism variable is statistically significant in all the equations and has the pre-

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Income Distribution" (Unpublished Ph.D. diss., Harvard University, 1973).

[11] See footnote 44 above.

[12] See, for example, H. Hill, "The Racial Practices of Organized Labor: the Contemporary Record," in *The Negro and the American Labor Movement*, ed. J. Jacobson (New York: Anchor, 1968).

[13] In a similar fashion, racial antagonisms reduce the political pressure on governmental agencies to provide other public services that would have a pro-poor distributional impact. The two principal items in this category are public health services and welfare payments in the Aid to Families with Dependent Children program.

dicted sign: a greater degree of racism results in lower unionization rates and greater degree of schooling inequality among whites. This empirical evidence again suggests that racism is in the economic interests of capitalists and other rich whites and against the economic interests of poor whites and white workers.

However, a full assessment of the importance of racism for capitalism would probably conclude that the primary significance of racism is not strictly economic. The simple economics of racism does not explain why many workers seem to be so vehemently racist, when racism is not in their economic self-interest. In non-economic ways, racism helps to legitimize inequality, alienation, and powerlessness—legitimization that is necessary for the stability of the capitalist system as a whole. For example, many whites believe that welfare payments to blacks are a far more important factor in their taxes than is military spending. Through racism, poor whites come to believe that their poverty is caused by blacks who are willing to take away their jobs, and at lower wages, thus concealing the fact that a substantial amount of income inequality is inevitable in a capitalist society. Racism thus transfers the locus of whites' resentment towards blacks and away from capitalism.

Racism also provides some psychological benefits to poor and working-class whites. For example, the opportunity to participate in another's oppression compensates for one's own misery. There is a parallel here to the subjugation of women in the family: after a day of alienating labor, the tired husband can compensate by oppressing his wife. Furthermore, not being at the bottom of the heap is some solace for an unsatisfying life; this argument was successfully used by the Southern oligarchy against poor whites allied with blacks in the interracial Populist movement of the late nineteenth century.

Thus, racism is likely to take firm root in a society that breeds an individualistic and competitive ethos. In general, blacks provide a convenient and visible scapegoat for problems that actually derive from the institutions of capitalism. As long as building a real alternative to capitalism does not seem feasible to most whites, we can expect that identifiable and vulnerable scapegoats will prove functional to the status quo. These non-economic factors thus neatly dovetail with the economic aspects of racism discussed earlier in their mutual service to the perpetuation of capitalism.

Reich's Later Research

Using later Census data, Reich was able to make a statistical estimate of the effect of two race-related variables to the rate of profit for employers. BW = the ratio of black to white median family income in a given industry. %NW = the percent of non-white workers in an industry. We then have the following equation for the rate of profit in various industries:

Rate of Profit = 20.5% - 14% x BW - 21.7% x %NW

This equation implies that more racial inequality is associated with higher profits, and also that a lower percentage of non-white workers in an industry is associated with higher profits.

See M. Reich, Racism: A Political Economic Analysis*, Princeton, 1981.*