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Racial Wealth Gap: Historical Roots and Systemic Barriers

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Lowell Ricketts, Lead Analyst

**These are my own views, and not necessarily the views of the Federal Reserve Bank of St. Louis, Federal Reserve System, or the Board of Governors*



Executive Summary

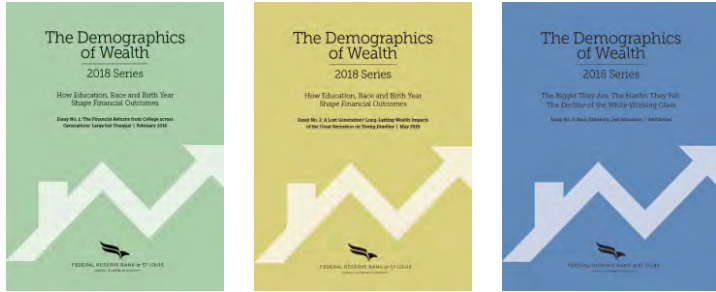
- Black and Hispanic families experiencing worse housing distress during pandemic, but inequities existed well before.
- Lack of assets (wealth) linked to greater risk of hardship.
- Long-running and persistent racial wealth gaps contributing to chronic fragility across many different outcomes.
- Racial wealth gaps have long historical roots (e.g. “redlining”) and systemic barriers to closing them.
- Evidence for bold policy is thin due to the scale of the interventions proposed; shouldn’t preclude consideration.

Why Do Assets and Wealth Matter?

- Accumulated wealth is central for both economic resiliency in the short-term and long-term upward mobility.
- Access to assets (especially liquid assets) is a form of private insurance for events such as an income shock.
- Liquid assets appear to be salient factor reducing risk of instability such as a missed housing payment. ([Gallagher and Sabat](#) 2017, [Ricketts and Boshara](#) 2020)

The Demographics of Wealth Series

2018 Series



2015 Series

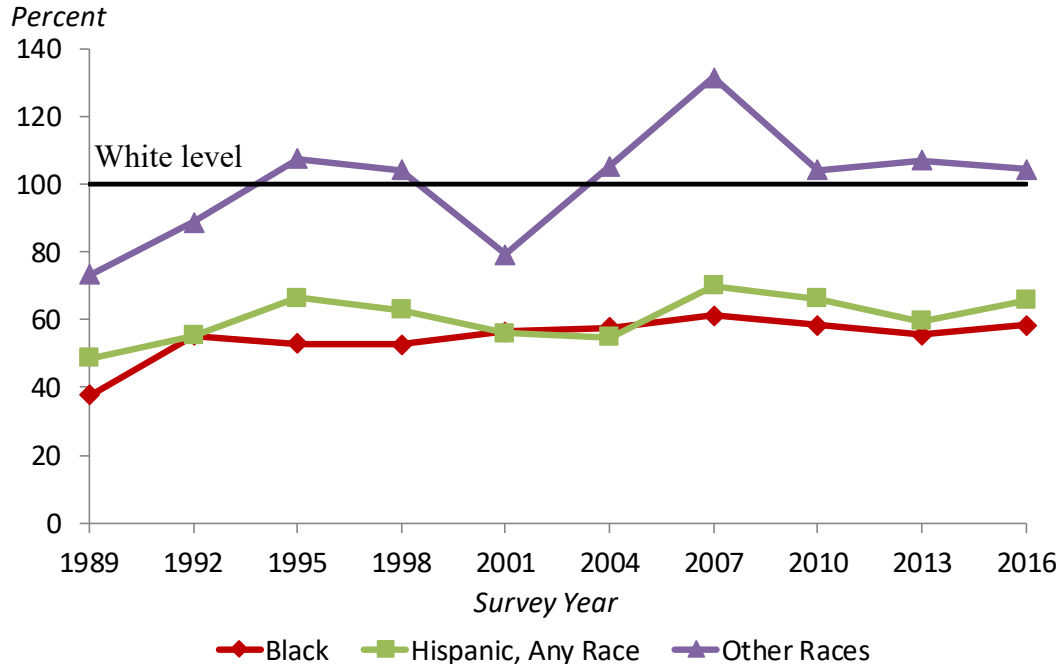


- Essay series links income, wealth and other socio-economic outcomes to a family's:
 - Race/ethnicity
 - Education (own and parents')
 - Age and birth year
- Your race/ethnicity, education and birth year are strong predictors of your adult outcomes.

[Demographics of Wealth Essays](#)

Black & Hispanic Income Gaps Closing Slowly

Median Real Income, Relative to Non-Hispanic White Families



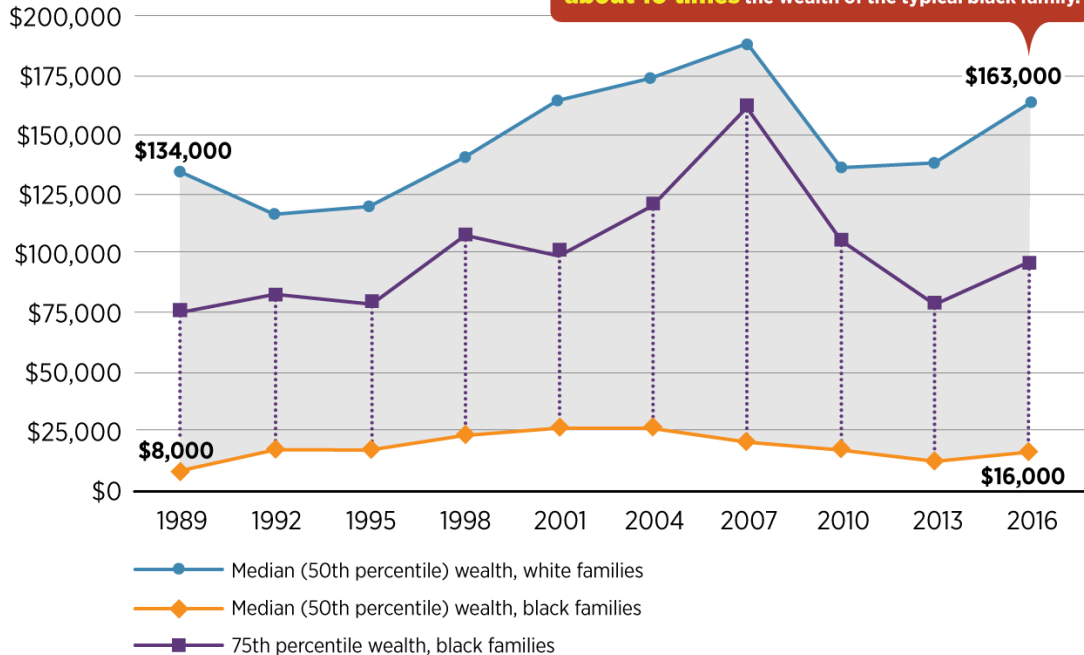
Source: Federal Reserve Board's Survey of Consumer Finances.

- Data from the Federal Reserve's Survey of Consumer Finances.
- Typical (median) income of black and Hispanic families has moved closer to that of white families but remains 40% lower.
- The typical "other" race family has surpassed the typical white family's income.

Racial/Ethnic Wealth Gaps are Wide and Persistent

White/Black Wealth Gap

In 2016, the typical white family had **about 10 times** the wealth of the typical black family.



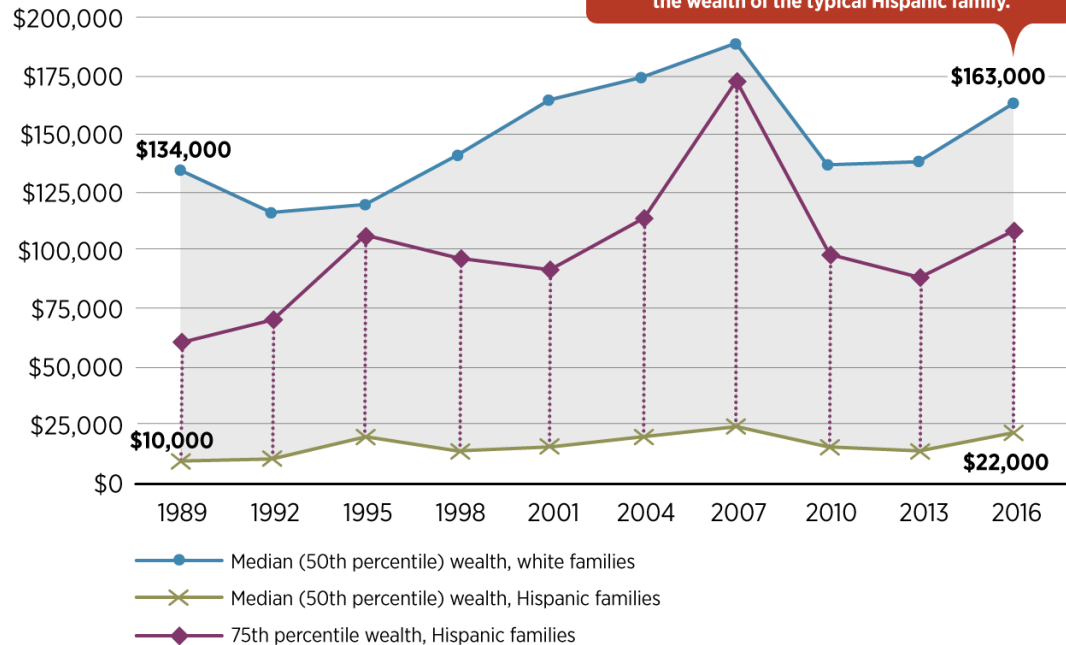
- Despite other progress, the large racial and ethnic wealth gaps remain essentially unchanged.
- Typical white families had about 10 times wealth of typical black families.
- Even wealthier black families (75th percentile) fall short of white medians (50th percentile).

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Source: [Kent, Ricketts, Boshara \(2019\)](#)

Racial/Ethnic Wealth Gaps are Wide and Persistent

White/Hispanic Wealth Gap



- Over a nearly three-decade period, the U.S. has seen very little progress in narrowing racial and ethnic wealth gaps.
- In terms of the total wealth pie, white families in 2016 owned 89% of it, while black and Hispanic families owned 3% each.

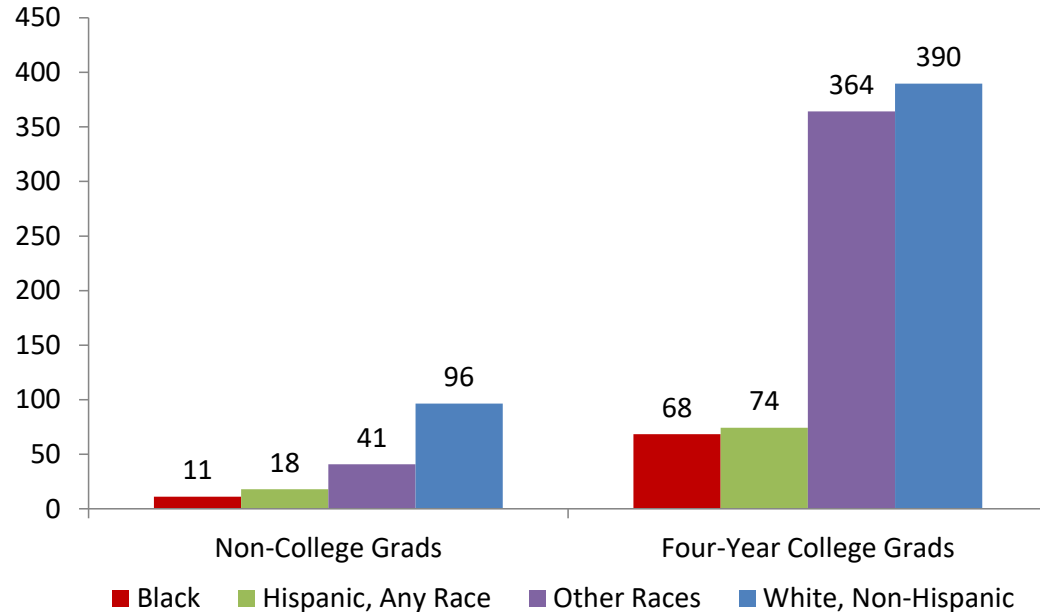
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Source: [Kent, Ricketts, Boshara \(2019\)](#)

Racial Wealth Gaps Remain Despite College

Median Household Net Worth, by Race/Ethnicity and Education, 2016

Thousands of 2016 \$



Note: College grads include any family headed by someone with a four-year degree or higher.

Source: Federal Reserve Board's Survey of Consumer Finances.

- Importantly, a college degree is associated with greater median wealth for *all groups*.
- However, the racial wealth divide remains even among college-educated families.
- Among college-educated peers, the black-white gap is 17 cents per dollar.

What Explains the Racial Wealth Gap?

- [Thompson and Suarez](#) (2015): “Observable factors account for most of the gap between white and black families, but a substantial unexplained portion remains.”
- Observable factors include everything and the kitchen sink.
- They cede that “some of the key factors that account for the wealth gap in our regression analysis, including income and homeownership, *could reflect themselves the effects of racial biases as well.* [emphasis added]”

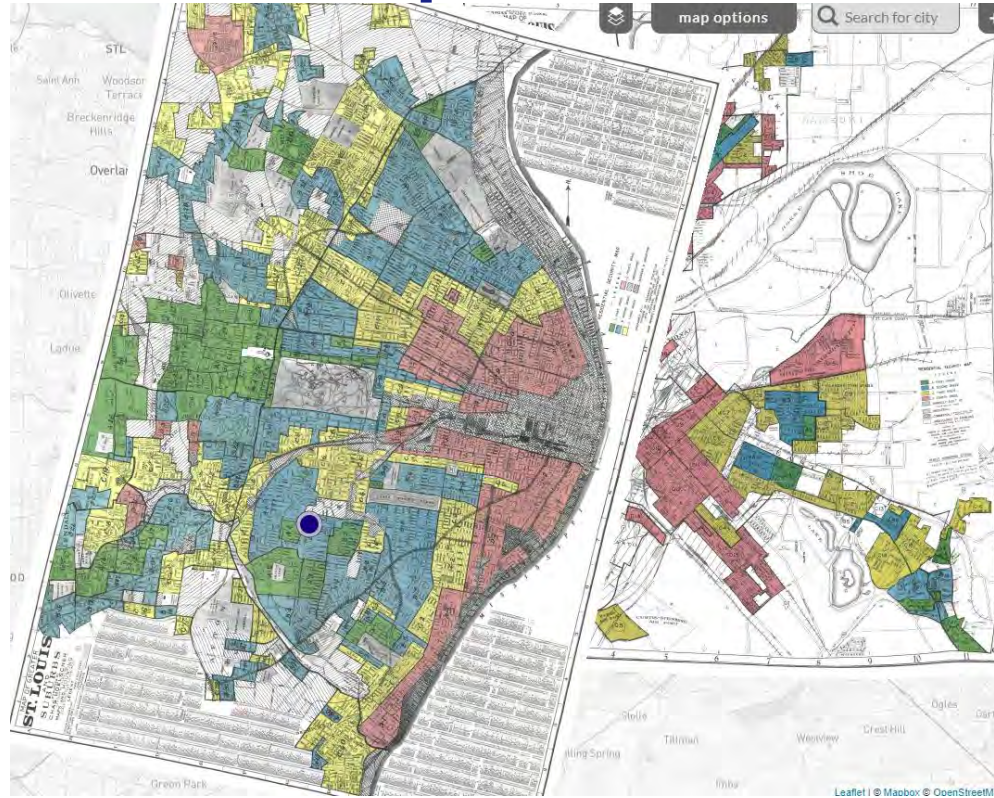
What Explains the Racial Wealth Gap?

- [Emmons and Ricketts](#) (2017) presents alternative theoretical framework that attributes racial differences in observables to systemic or structural factors in the past and present.
- A comparison of frameworks provides suggestive evidence that Black- and Hispanic-White wealth gaps *may lie beyond the scope of individual actions or marginal policy changes.*
- Instead, the gaps appear to be deeply rooted in unobservable factors that may include discrimination or other long-lasting disadvantages.

The Practice of Redlining

- In wake of Great Depression, the Home Owners' Loan Corporation (HOLC) was created in 1933 by the Federal government to stabilize housing markets.
- HOLC created maps for over 200 cities to grade (A = least, D = most risky) the riskiness of lending to neighborhoods.
- In addition to common factors, racial and ethnic makeup was also included (e.g. “infiltration of a lower-grade population”.)
- Neighborhoods deemed to have the highest risk were drawn in red, consequently borrowers in these neighborhoods were denied credit based on racial composition.

HOLC Maps in St. Louis



Source: Robert K. Nelson, LaDale Winling, Richard Marciano, Nathan Connolly, et al. "Mapping Inequality", *American Panorama*, ed. Robert K. Nelson and Edward L. Ayers, accessed July 30, 2020, [Link](#)

“The Effects of the 1930s HOLC Redlining Maps”

- The maps affected the degree of racial segregation: areas graded “D” became more heavily Black than nearby C-rated areas.
- The maps also had a meaningful negative effect on homeownership, house values, rents, and vacancy rates.
- Effects rose steadily from 1930 until about 1970 or 1980 before declining thereafter.
- The maps could account for 15-30% of the D-C differences in segregation and homeownership; 40% of gap in house values over the 1950 to 1980 period.

Source: [Aaronson, Hartley, and Mazumder \(2019\)](#)

Systemic Barriers Continue to Undermine Black and Hispanic Homeownership

- Lack of access to traditional mortgages lends itself to “contract for deed” financing in communities of color ([Carpenter, George, Nelson](#) 2019).
- Nonstandard appraisal process features subjective selection of neighborhood comps (or lack thereof) leading to appraisal gaps ([Howell and Korver-Glenn](#) 2018).
- Late entrance into homeownership coupled with labor market vulnerability leads to greater foreclosure rates ([Bayer, Ferreira, Ross](#) 2016).



Conversation One vs. Conversation Two

([Jackson 2017](#))

- **Conversation one** outlines expedient, small-scale interventions aimed to solve tightly defined problems or improve existing institutions.
- **Conversation two** involves a deeper discussion about where wealth gaps come from and what larger-scale changes might close them.
- Both conversations are necessary but often in social sciences the first is preferred or crowds out the second.

Conversation One

- BankOn

- Close to 7% of U.S. households are “unbanked,” and lack a checking or savings account.
- About 20% of U.S. households are “underbanked,” meaning they still use some fringe financial services.
- BankOn focuses on providing an industry-standard for safe and appropriate accounts, particularly those without overdraft.
- Accounts help families to avoid using expensive alternative services and paying too much for basic financial transactions.

Conversation Two

- **Not** endorsing any specific policy but conversation two involves bold ideas such as:
 - Renewed pursuit of desegregation of primary and secondary schools.
 - Disassociate school funding from neighborhood wealth.
 - End residential segregation (by race and income).
 - Universal higher education.
 - Wealth taxation.

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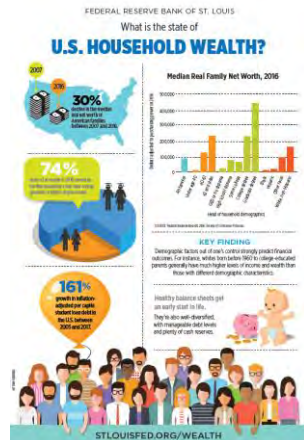
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