Persistent Racial Wealth Gaps
Authors: Job Boerma, Loukas Karabarbounis
Discussants: Ellora Derenoncourt, Jonathan A. Parker

Guido Menzio opened the discussion with two points. First, he suggested that given beliefs do not enter the future value function, there is no benefit to experimentation. Second, he was concerned that all the wealth in the model is from bequests but the data the authors use is cross-sectional wealth at a given point in time, rather than at death. The authors responded by saying that in order to rationalize the belief gaps we see today, one needs learning from experimentation to be noisy. They also agreed that the wealth data is not specifically bequests and that they could certainly look at the wealth of older people (e.g., 65-year-olds). The authors further responded that there is a lot of work highlighting the importance of bequests for wealth inequality generally and that, statistically, bequests are an important factor affecting the black-white wealth gap.

Robert Hall then asked about an alternative mechanism: the health trap. He said in earlier work by himself and Chad Jones, they showed that health is a luxury good. Therefore, a health trap could lead to a model with two equilibria where some people are poor and have poor health. He then noted that we also know there are substantial differences in health outcomes between black and white people. The authors welcomed the suggestion and noted that they should think more about this.

Eric Swanson also asked about an alternative mechanism: education. He argued that the some of the empirical evidence of differential beliefs about equity returns could be explained by education differences, given that there is evidence of a black-white education gap and that less educated households typically have lower expectations for equity returns. He added that if less educated households earn lower returns, then the solution should focus on reducing the black-white education gap. Finally, he asked why the black-white education gap has persisted. He argued that if there are concerns about expropriation (e.g., because of events like the Tulsa Race Massacre), then we would expect greater investment in human capital, because it is not subject to expropriation risk in the same way as other forms of capital. He cited the Jewish community as another example of a historically marginalized group that was subject to expropriation risk (especially from pogroms in Europe, which occurred many times over history), which led them to invest heavily in human capital. The authors agreed that human capital can play an important role. They highlighted that in their model, when the close the wage gap, which proxies for the human capital gap, they eliminate most of the wealth differences. However, they pointed that wealth differences remain for the right tail (i.e., above the 95th percentile).

Eric Zwick commented that to the extent the authors are focused on settings where entrepreneurial wealth is important, he has ongoing work that shows not only expected returns differing across groups, but also realized returns. In his work, he shows that upfront barriers to entry are not able to explain the differences in returns and it seems ongoing barriers (such as discrimination in the product or labor markets) or the accumulation of human capital appear more likely to generate the right tail of entrepreneurial outcomes. The authors responded in their model the right tail is driven by high-return entrepreneurs. They added that their model is also consistent with return varying by size of the business.

Martin Eichenbaum then asked how the authors distinguish between different hypotheses? He argued that while the experience of black people in the United States is unique, there are many other
immigrant groups that have come to the country, but it is not clear whether they have converged as slowly. He noted that while immigration might be prone to selection issues, as highlighted by Jonathan Parker, there are periods of time where there is little choice (e.g., during the Second World War). The authors responded that they specifically looked at different race identifiers. They found that the beliefs of both Hispanic and Asian Americans aligned with the mean wealth across these racial groups which lends support to their model.

Andrea Eisfeldt found the evidence presented by discussant Jonathan Parker compelling. Specifically, that much of the return differential between black and white people comes from downside risk. As such, she asked whether policies such as social safety net would be worth exploring. The authors explained that one way to think about such policies is the return subsidy in their model. This subsidy protects against some downside risk by effectively acting as a guarantee.

Joel Mokyr commented that previous work by Bruce Meyer found little evidence that liquidity constraints prevented black people from pursuing self-employment or that black people concentrated in capital-light self-employment. He then concluded that there must be some unobserved cultural differences. Joel Mokyr then added that there is also a role for discrimination in housing. He pointed out that this is exacerbated by education being funding by local taxes in the United States. Therefore, being discriminated in housing may also result in worse educational outcomes.

The authors explained that they had cited Bruce Meyer’s paper and the missing cultural factor in their model is beliefs. They then concluded by thanking the discussants and responding to an overarching comment about what is driving the difference in returns. The authors suggested that this difference has two components. The first is compositional differences which is the story of their model. That is, black people invest in low-risk assets while white people invest in high-risk assets. The second component relates to within asset differences. The authors agreed that this could be a potential factor driving wealth gaps and they would try and look into it.