

The Roots of the Widening Racial Wealth Gap: Explaining the Black-White Economic Divide

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Growing concerns about wealth inequality and the expanding racial wealth gap have in recent years become central to the debate over whether our nation is on a sustainable economic path. This report provides critical new information about what has fueled the racial wealth gap and points to policy approaches that will set our country in a more equitable and prosperous direction.

All families need wealth to be economically secure and create opportunities for the next generation. Wealth - what we own minus what we owe—allows families to move forward by moving to better and safer neighborhoods, investing in businesses, saving for retirement, and supporting their children's college aspirations. Having a financial cushion also provides a measure of security when a job loss or other crisis strikes. The Great Recession of 2007-2009 devastated the wealth of all families except for those with the most. The unprecedented wealth destruction during that period, accompanied by long-term high unemployment, underscores the critical importance wealth plays in weathering emergencies and helping families move along a path toward long-term financial security and opportunity.

Extreme wealth inequality not only hurts family well-being, it hampers economic growth in our communities and in the nation as a whole. In the U.S. today, the richest 1 percent of households owns 37 percent of all wealth. This toxic inequality has historical underpinnings but is perpetuated by policies and tax preferences that continue to favor the affluent. Most strikingly, it has resulted in an enormous wealth gap between white households and households of color. In 2009, a representative survey of American households revealed that the median wealth of white families was \$113,149 compared with \$6,325 for Latino families and \$5,677 for black families.¹

Looking at the *same set of families* over a 25-year period (1984-2009), our research offers key insight into how policy and the real, lived-experience of families in schools, communities, and at work affect wealth accumulation. Tracing the same households during that period, the total wealth gap between white and African-American families nearly triples, increasing from \$85,000 in 1984 to \$236,500 in 2009² (see Figure 1). To discover the major drivers behind this dramatic \$152,000 increase, we tested a wide range of possible explanations, including family, labor market, and wealth characteristics. This allowed us, for the first time, to identify the primary forces behind the racial wealth gap. Our analysis found little evidence to support common perceptions about what underlies the ability to build wealth, including the notion that personal attributes and behavioral choices are key pieces of the equation. Instead, the evidence points to policy and the configuration of both opportunities and barriers in workplaces, schools, and communities that reinforce deeply entrenched racial dynamics in how wealth is accumulated and that continue to permeate the most

KEY FINDINGS

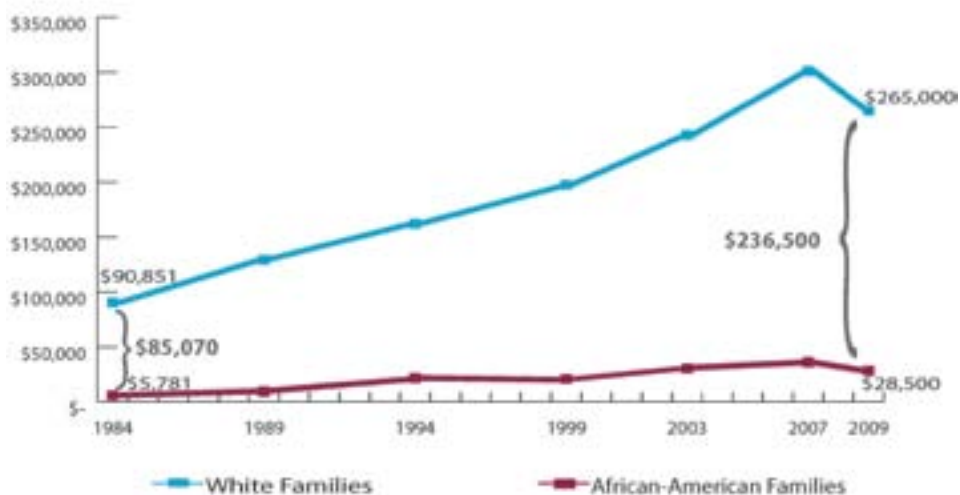
1. Tracing the same households over 25 years, the total wealth gap between white and African-American families nearly triples, increasing from \$85,000 in 1984 to \$236,500 in 2009.
2. The biggest drivers of the growing racial wealth gap are:
 - Years of homeownership
 - Household income
 - Unemployment, which is much more prominent among African-American families
 - A college education
 - Inheritance, financial supports by families or friends, and preexisting family wealth
3. Equal achievements, such as income gains, yield unequal wealth rewards for whites and African-Americans.

important spheres of everyday life.

Data for this analysis derived from the Panel Study of Income Dynamics (PSID), a nationally representative longitudinal study that began in 1968. We followed nearly 1,700 working-age households from 1984 through 2009. Tracking these families provides a unique opportunity to understand what happened to the wealth gap over the course of a generation and the effect of policy and institutional decision-making on how average families accumulate wealth. Unfortunately, there were not enough data that tracked wealth information in a sufficient number of Latino, Asian American, or immigrant households to include in this report. As a result, the specific focus here is on black-white differences. Yet, while each group shares different histories and experiences, we believe this examination captures important dynamics that can be applied across communities of color.

The wealth trends depicted in Figure 1 beg the question of what caused such dramatic racial wealth inequities. With a gap of close to a quarter of a million dollars, virtually every possible explanation will have some degree of accuracy, no matter how miniscule a factor. The challenge is to identify the major evidence-based factors affecting the growing racial wealth gap. To discover the major drivers behind the \$152,000 increase in the racial wealth gap, we tested a wide range of possible explanations that included family, labor market, demographic, and wealth characteristics, and we have determined how different factors affect the widening racial wealth gap over a generation. The compelling evidence-based story is that policy shaping opportunities and rewards where we live, where we learn, and where we work propels the large majority of the widening racial wealth gap.

FIGURE 1. MEDIAN NET WORTH BY RACE, 1984-2009



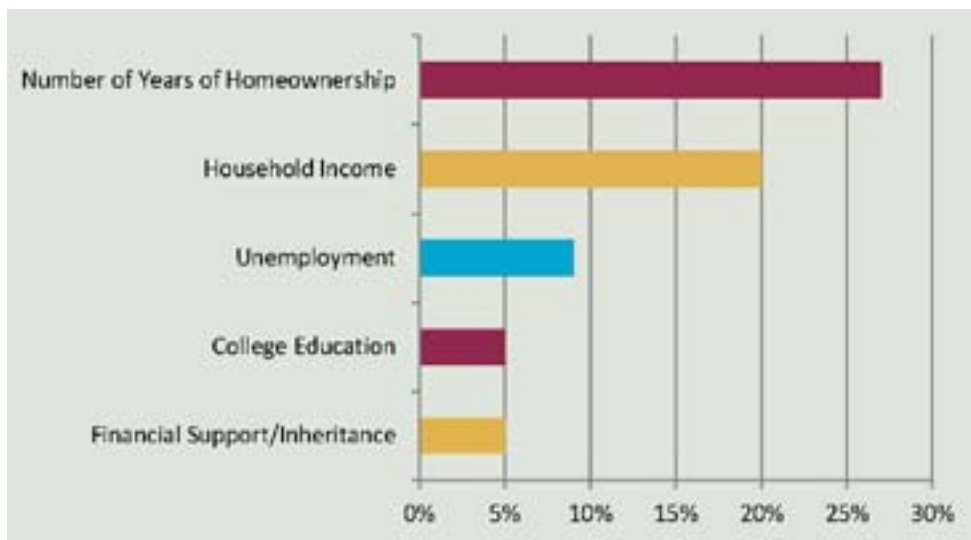
The Foundations of Inequality

We started our analysis with an overriding question: Why has economic inequality become so entrenched in our post-Civil Rights era of supposed legal equality? The first step was to identify the critical aspects of contemporary society that are driving this inequality (Figure 2).³ Next, we sought to determine whether equal accomplishments are producing equal wealth gains for whites and African-Americans (Figure 3).⁴ This approach allows for an evidence-based examination of whether the growing racial wealth gap is primarily the result of individual choices and cultural characteristics or policies and institutional practices that create different opportunities for increasing wealth in white and black families.

Among households with positive wealth growth⁵ during the 25-year study period, as shown in Figure 2, the number of years of homeownership accounts for 27 percent of the difference in relative wealth growth between white and African-American families, the largest portion of the growing wealth gap. The second largest share of the increase, accounting for 20 percent, is average family income. Highly educated households correlate strongly with larger wealth portfolios, but similar college degrees produce more wealth for whites, contributing 5 percent of the proportional increase in the racial wealth gap. Inheritance and financial support from family combine for another 5 percent of the increasing gap. How much wealth a family started out with in 1984 also predicts a portion (3 percent) of family wealth 25 years later.

Unemployment, the only significant factor that depleted wealth since it forced families to draw upon their nest eggs,

FIGURE 2: WHAT'S DRIVING THE INCREASING RACIAL WEALTH GAP



explains an additional 9 percent of the growing racial wealth gap. In addition to continuing discrimination, labor market instability affects African-Americans more negatively than whites.

The evidence we present to examine the racial wealth gap points to institutional and policy dynamics in important spheres of American life: homeownership, work and increased earnings, employment stability, college education, and family financial support and inheritance. Together, these fundamental factors account for nearly two-thirds (66 percent) of

the proportional increase in the wealth gap. In the social sciences, this is a very high level of explanatory power and provides a firm foundation for policy and reform aimed at closing the gap.

The \$152,000 Question: What Drove the Growing Gap?

Having identified the major drivers of the racial wealth gap, we now can dig deeper into each one—homeownership, income, college education, inheritance, and unemployment—to determine how similar accomplishments grow wealth *differentially by race*. Figure 3 provides a close look at how these factors, as well as marriage, which we will discuss later, translate into differences in wealth accumulation for black and white families. We know that wealth increases through accomplishments such as job promotions, pay increases, or the purchase of a home, as well as important life and family events including receiving an inheritance and getting married. Figure 3 highlights how similar accomplishments and life events lead to unequal wealth gains for white and African-American families. The result is that while wealth grew for African-Americans as they achieve life advances, that growth is at a considerably lower rate than it is for whites experiencing the same accomplishments. This leads to an increase in the wealth gap.

Homeownership

The number of years families owned their homes was the largest predictor of the gap in wealth growth by race (Figure 2). Residential segregation by government design has a long legacy in this country and underpins many of the challenges African-American families face in buying homes and increasing equity. There are several reasons why home equity rises so much more for whites than African-Americans:

- Because residential segregation artificially lowers demand, placing a forced ceiling on home equity for African-Americans who own homes in non-white neighborhoods⁶;
- Because whites are far more able to give inheritances or family assistance for down payments due to historical wealth accumulation, white families buy homes and start acquiring equity an average eight years earlier than black families⁷;
- Because whites are far more able to give family financial assistance, larger up-front payments by white homeowners lower interest rates and lending costs; and
- Due to historic differences in access to credit, typically lower incomes, and factors such as residential segregation, the homeownership rate for white families is 28.4 percent higher than the homeownership rate for black families⁸.

Homes are the largest investment that most American families make and by far the biggest item in their wealth portfolio. Homeownership is an even greater part of wealth composition for black families, amounting to 53 percent of wealth for blacks and 39 percent for whites⁹. Yet, for many years, redlining, discriminatory mortgage-lending

practices, lack of access to credit, and lower incomes have blocked the homeownership path for African-Americans while creating and reinforcing communities segregated by race. African-Americans, therefore, are more recent homeowners and more likely to have high-risk mortgages, hence they are more vulnerable to foreclosure and volatile housing prices.

Figure 1 shows households losing wealth between 2007 and 2009 (12 percent for white families, 21 percent for African-American families), which reflects the destruction of housing wealth resulting from the foreclosure crisis and imploded housing market. Overall, half the collective wealth of African-American families was stripped away during the Great Recession due to the dominant role of home equity in their wealth portfolios and the prevalence of predatory high-risk loans in communities of color. The Latino community lost an astounding 67 percent of its total wealth during the housing collapse¹⁰.

Unfortunately the end to this story has yet to be written. Since 2007, 10.9 million homes went into foreclosure. While the majority of the affected families are white, borrowers of color are more than twice as likely to lose their homes. These higher foreclosure rates reflect a disturbing reality: borrowers of color were consistently more likely to receive high-interest risky loan products, even after accounting for income and credit scores¹¹.

Foreclosures not only have a direct impact on families, they also result in severe collateral damage to surrounding neighborhoods. One report estimates that this collateral destruction led to nearly \$2 trillion in lost property wealth for communities across the country. More than half of this loss is associated with communities of color, reflecting concentrations of high-risk loans, subsequent higher foreclosure rates, and volatile housing prices¹².

While homeownership has played a critical role in the development of wealth for communities of color in this country, the return on investment is far greater for white households, significantly contributing to the expanding racial wealth gap shown in Figure 1. The paradox is that even as homeownership has been the main avenue to building wealth for African-Americans, it has also increased the wealth disparity between whites and blacks.

Income and Employment

Not surprisingly, increases in income are a major source of wealth accumulation for many US families. However, income gains for whites and African-Americans have a very different impact on wealth. At the respective wealth medians, every dollar increase in average income over the 25-year study period added \$5.19 wealth¹³ for white households (see Figure 3), while the same income gain only added 69 cents of wealth for African American households.

The dramatic difference in wealth accumulation from similar income gains has its roots in long-standing patterns of discrimination in hiring, training, promoting, and access to benefits that have made it much harder for African-Americans to save and build assets. Due to discriminatory factors, black workers predominate in fields that are

FIGURE 3: HOW WEALTH IS ACCUMULATED*

	White Wealth Growth**	Black Wealth Growth
Each \$1 in Income Increase Yields	\$5.19	.69
Each \$1 of Inheritance Yields	.91	.20
Each \$1 in Family Financial Support Yields	.35	.51
Years of Homeownership	No Significant Impact	Significant Impact
Marriage	Significant Impact	No Significant Impact

*This table shows how key life advances and events (an increase in income, inheritance, family financial support, homeownership and marriage) translate into the ability to increase wealth. Even with equal advances, wealth grows at far lower rates for black households, who typically need to use financial gains for everyday needs rather than long-term savings and assets.

**Regression estimates at the median change in wealth over the 25-year study period conducted separately for white and black households

least likely to have employer-based retirement plans and other benefits, such as administration and support and food services. As a result, wealth in black families tends to be close to what is needed to cover emergency savings while wealth in white families is well beyond the emergency threshold and can be saved or invested more readily.

The statistics cited above compare change in wealth over the 25 years at the median wealth for typical white and black households. Yet we already know that the average white family starts out with abundantly more wealth and significantly higher incomes than the average black family. When whites and blacks start off on an equal playing field with a similar wealth portfolio, their wealth returns from similar income gains narrow considerably.¹⁴ Black families under this scenario see a return of \$4.03 for each dollar increase in income – a considerable closing of the wealth breach.

This analysis also captured the devastation of unemployment on wealth accumulation. Unemployment affects all workers but due to the discriminatory factors listed above, black workers are hit harder, more often, and for longer periods of time. With much lower beginning wealth levels and unequal returns on income, it is a greater challenge for African-Americans to grow their family wealth holdings in the face of work instability.

Inheritance

Most Americans inherit very little or no money, but among the families followed for 25 years whites were five times more likely to inherit than African-Americans (36 percent to 7 percent, respectively). Among those receiving an inheritance, whites received about ten times more wealth than African-Americans. Our findings show that inheritances converted to wealth more readily for white than black families: each inherited dollar contributed to 91 cents of wealth for white families compared with 20 cents for African-American families. Inheritance is more likely to add wealth to the considerably larger portfolio whites start out with since blacks, as discussed above, typically need to reserve their wealth for emergency savings.

College Education

In the 21st century, obtaining a college degree is vital to economic success and translates into substantially greater lifetime income and wealth. Education is supposed to be the great equalizer, but current research tells a different story. The achievement and college completion gaps are growing, as family financial resources like income and wealth appear to be large predictors of educational success. While current research identifies a narrowing black-white achievement gap, race and class intersect to widen the educational opportunity deficit at a time when workers without higher-level skills are increasingly likely to languish in the job market.

College readiness is greatly dependent on quality K - 12 education. As a result of neighborhood segregation, lower-income students—especially students of color—are too often isolated and concentrated in lower-quality schools. Neighborhoods have grown more segregated, leaving lower-income students—especially students of color—isolated and concentrated in lower-quality schools, and less academically prepared both to enter and complete college. Further, costs at public universities have risen 60 percent in the past two decades, with many low-income and students of color forced to hold down jobs rather than attend college full time and graduating in deep debt. Average student debt for the class of 2011 was \$26,600. Student debt is an issue that affects most graduates, but black graduates are far more vulnerable: 80 percent of black students graduate with debt compared with 64 percent of white students.¹⁵ More blacks than whites do not finish their undergraduate studies because financial considerations force them to leave school and earn a steady income to support themselves and their families.¹⁶

The context of broad class and race educational inequity helps us better understand why a college education produces more wealth for white than black households, accounting for a 5 percent share of the widening racial wealth gap (see Figure 2). In the past 30 years, the gap between students from low- and high-income families who earn bachelor's degrees has grown from 31 percent to 45 percent.¹⁷ Although both groups are completing

college at higher rates today, affluent students (predominantly white) improved much more, widening their already sizable lead. In 1972, upper-income Americans spent five times as much per child on college as low-income families. By 2007, the difference in spending between the two groups had grown to nine to one; upper-income families more than doubled how much they spent on each child, while spending by low-income families grew by just 20 percent.¹⁸

Social and Cultural Factors

As part of this analysis we set out to test notions about the role social and cultural factors play in widening or closing the racial wealth gap. To determine how these factors might affect wealth, we zeroed in on the role of marriage in perpetuating the racial wealth gap. We find that getting married over the 25-year study period significantly increases the wealth holdings for white families by \$75,635 but have no statistically significant impact on African-Americans. Single whites are much more likely to possess positive net worth, most likely due to benefits from substantial family financial assistance, higher paying jobs, and homeownership. Hence, marriages that combine modest wealth profiles seem to move whites past emergency-level savings to opportunities to invest and build wealth.

By contrast, marriage among African-Americans typically combines two comparatively low-level wealth portfolios and, unlike white households, does not significantly elevate the family's wealth. While the number of household wage earners bringing in resources does correlate to higher wealth, the impact of marriage is not statistically significant for blacks and the reality is that most do not marry out of the racial wealth gap.

Closing the Racial Wealth Gap

Public policy can play a critical role in creating a more equitable society and helping all Americans build wealth. College loans, preferential homeownership, and retirement tax policies helped build opportunities and wealth for America's middle class. Medicare and Social Security have protected that wealth. While the bold vision of policymakers, advocates, and others interested in social and racial justice is needed to develop a precise policy agenda, we believe the following broad public policy and institutional changes are critical to closing the gap:

- **Homeownership** - The data in this report clearly target homeownership as the biggest driver of the racial wealth gap. We need to ensure that mortgage and lending policies and fair housing policies are enforced and strengthened so that the legacy of residential segregation no longer confers greater wealth opportunities to white homeowners than it does to black homeowners. As our nation moves towards a majority people of color population, increasingly diverse neighborhoods must deliver equitable opportunities for growing home equity.
- **Income** - This report identifies the importance of stable, family-supporting jobs and increasing incomes as a prime avenue for building wealth. To address the gap caused by income disparity, proven tools should be fully implemented at the national, state, and local levels, including raising the minimum wage, enforcing equal pay provisions, and strengthening employer-based retirement plans and other benefits.
- **Education** - It is clear that differential educational opportunities and rewards are further widening the racial wealth gap. We need to invest in affordable high-quality childcare and early childhood development so every child is healthy and prepared for school. We need to support policies that help more students from low-and moderate-income families and families of color attend college and graduate. And we need to value education as a public good and invest in policies that do not leave students strapped with huge debt or a reason to drop out.
- **Inheritance** - Due to the unearned advantages it transmits across generations, inheritance widens inequality and is a key driver of the racial wealth gap. If we truly value merit and not unearned preferences, then we need to diminish the advantages passed along to a small number of families. Preferential tax treatment for large estates costs taxpayers and provides huge benefits to less than 1 percent of the population while diverting vital resources from schools, housing, infrastructure, and jobs. Preferential tax treatment for

dividends and interests are weighted toward wealthy investors as is the home mortgage deduction and tax shielding benefits from retirement savings.

It is time for a portfolio shift in public investment to grow wealth for all, not just a tiny minority. Without that shift the wealth gap between white and black households has little prospect of significantly narrowing. A healthy, fair, and equitable society cannot continue to follow such an economically unsustainable trajectory.

Endnotes:

¹Rakesh, Kochhar, Richard Fry and Paul Taylor, *Wealth Gaps Rise to Record Highs Between Whites, Blacks, Hispanics*. Pew Research Center, July 2011. Data is from the Survey on Income and Program Participation.

²Figure 1 presents median wealth values for each year depicted in the graph. All dollar values are in 2009 dollars.

³Figure 2 presents the major factors yielded through Oaxaca decomposition analyses. The dependent variable, change in wealth over the 25 year study period, was transformed into its natural logarithm due to its skewed distribution. As such, these analyses were conducted only for households with positive wealth gain over 25 years. The variables in the analysis include change of marital status from married to single and vice versa, number of children, age, college degree, retired, unemployment (duration), average income over 25 years, inheritances and monetary supports, change from renting to owning and vice versa, homeownership (duration), and baseline wealth in 1984.

⁴Figure 3 summarizes findings for median regression analyses conducted separately for white and African-American households. Median regressions are the appropriate approach for highly skewed dependent variables, in this case change in wealth over 25 years. The variables in the median regression models include change of marital status from married to single and vice versa, number of children, age, college degree, retired, unemployment (duration), average income over 25 years, inheritances and monetary supports, change from renting to owning and vice versa, and homeownership (duration).

⁵These analyses could be only conducted for households with positive wealth due to the need to transform the dependent variable into its natural logarithm. In this sample, 87% of white and 70% of African-American households had positive wealth growth during the study period.

⁶Shapiro, Thomas, *The Hidden Cost of Being African American*, Oxford University Press, 2004.

⁷Joint Center for Housing Studies analysis of American Housing Survey, 2009, tabulations of 2009 AHS.

⁸Joint Center for Housing Studies, *State of the Nation's Housing 2012*.

⁹IASP tabulations of Survey on Income and Program Participation, SIPP 2008, Wave 7.

¹⁰Rakesh, Kochhar, Richard Fry, and Paul Taylor, *Wealth Gaps Rise to Record Highs Between Whites, Blacks, Hispanics*. Pew Research Center, July 2011.

¹¹Gruenstein Bocian, Debbie, Peter Smith, and Wei Li, *Collateral Damage: The Spillover Costs of Foreclosures*. Center For Responsible Lending, October 24, 2012.

¹²Gruenstein Bocian, Debbie, Peter Smith, and Wei Li, *ibid*.

¹³White and African-American wealth holdings are measured as the change of their wealth portfolios over the 25 year study period, comparing baseline wealth to wealth in 2009. The median 25 year change in wealth for white families in this group is \$211,400 and \$18,942 for African-Americans.

¹⁴In real terms this means comparing whites at the 50th percentile to African-Americans at the 76th percentile.

¹⁵The Project on Student Debt, *Student Debt and the Class of 2011*, October 2012.

¹⁶The Project on Student Debt, *ibid*.

¹⁷Martha J. Bailey and Susan M. Dynarski, "Inequality in Postsecondary Education" in *Whither Opportunity?* Edited by Greg J. Duncan and Richard J. Murnane, 2011.

¹⁸Kornrich, Sobino and Frank Furstenberg, Investing in Children: Changes in Parental Spending on Children, 1972 to 2007 Demography 2012 Sep 18.

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