Large and persistent gaps in income and wealth exist among major racial and ethnic groups in the United States. Society has long heralded that education is key to closing these economic disparities. This view is widely supported by economists.

For instance, William Emmons and Bryan Noeth (2015) at the Federal Reserve Bank of St. Louis find that a college degree explains the rising levels of wealth for White and Asian families, but falling levels of wealth for African-American (Black) and Hispanic families since 1992.

However, while college led to more wealth within all racial and ethnic groups, it failed to explain the changes in wealth over the past two decades. This perplexing issue motivated a series of studies sponsored by the St. Louis Fed, which released their findings in a recent issue of Review.

This newsletter summarizes the leading article of William Emmons and Lowell Ricketts (2017), who contribute to our understanding of diverging wealth outcomes among racial and ethnic groups in the past two decades.

Wealth Gaps

A family’s wealth, or net worth (the value of total assets minus total debts), is a measure of its financial strength. After adjusting for inflation, a typical family’s wealth is about the same today as it was 25 years ago.

Asian families are an exception as they accumulated about 50 percent more wealth during that period. As a result, the wealth gap with White families has narrowed for Asians, while the corresponding gaps for Black and Hispanic families have remained about the same.

Today, the wealth of a typical Black or Hispanic family is about one-tenth of the amount of a

SOURCE: Federal Reserve Survey of Consumer Finances, and Emmons and Ricketts (2017, Figure 2).
typical White family, and typical Asian wealth is about two-thirds of typical White wealth.

**Income Gaps**
Greater wealth is associated with higher income for various reasons. A higher income allows a family to save more because spending, such as food consumption and utilities, tends to rise less than proportionately with income.

Also, individuals earning higher incomes might also be better at making financial decisions that raise wealth accumulation. As shown in the chart above, the median family incomes among Black and Hispanic families have remained about 40 percent lower than that for White families since 1989. During that period, however, the median Asian family income has grown relatively faster than all other racial or ethnic groups, and it has exceeded the median income of White families for much of the last two decades.

**Education Boosts Income and Wealth**

The conventional wisdom attributes the observed wealth and income gaps to educational attainment. Indeed more than 60 percent of Asians born in 1980-84 had a college degree, compared with 33 percent of Whites, 25 percent of Blacks, and 16 percent of Hispanics. The patterns for postgraduate degree attainment are similar. The differences in educational attainment have also tended to widen among successive younger cohorts after World War II.

**Education Protects Only White and Asian Family Wealth**
While the positive effect of more education on income and wealth levels seems clear, this is not the case whether more educated families can better withstand major economic and financial shocks. Over the two decades between 1992 and 2013, White and Asian families headed by college graduates nearly doubled their wealth, while their less-educated counterparts accumulated less wealth.

**Divergent Trends**
The divergent trends in median wealth among college-educated families are associated with the negative long-term income trends among Black and Hispanic college graduates. Similar to the changes in wealth between 1992 and 2013, the median incomes of college-educated gained 18 percent and 31 percent, respectively, over that same period.

Their Black and Hispanic counterparts, however, earned at least 10 percent less. This suggests that, for Blacks and Hispanics, even closing the educational gap with Whites might not necessarily translate into wealth and income parity.

**College Is Not Enough**
Emmons and Ricketts (2017) analyze the observed changes in family financial conditions by first focusing on educational attainment. They find that differences in educational attainment alone explain less than half of the wealth gaps for Blacks, but nearly all (about 90%) of the wealth gaps for Hispanics and Asians.

College cannot level the playing field particularly for Blacks when the same degrees generate different returns. Janelle Jones and John Schmitt (2014) illustrate this point by comparing Black and White Harvard MBA graduates. They find a $5,000 pay differential at the beginning of their careers, and that gap widens to $100,000 per year within six to eight years of graduation.

**Observable Factors**
In addition to education, Emmons and Ricketts explore a large number of observable factors, including basic demographics, such as age; behavioral choices, such as education, family structure, and financial decisions; and some measures of luck, such as income windfalls and bequests.

Other than the age of the family head (life-cycle effects), the most important factors that explain the wealth gaps are measures of financial choices, such as
housing, the shares of financial assets in total assets, and the debt ratio. Along with educational attainment, these observable factors together explain about 70 percent of the Black-White wealth gap and virtually all of the Hispanic-White and Asian-White wealth gaps.

The above results, however, are based on the assumption that all families face the same choices and opportunities for education, successful family life, and solid balance sheets.

Emmons and Ricketts further relax this restrictive assumption with an alternative model, which allows different choices for different racial and ethnic groups. Compared to the previous model, the share of wealth gaps that can be explained by the same observable factors falls below 20 percent for Blacks and Hispanics and to about 75 percent for Asians.

Systemic or Unobservable Factors

In other words, the vast majority of the wealth gaps particularly for Blacks and Hispanics lie beyond the scope of their own choices and actions regarding educational attainment, family structure, and financial decisions.

Emmons and Ricketts conclude that “the gaps appear to be deeply rooted in unobservable factors that may include discrimination or other long-lasting disadvantages ... the [unexplained] portions of the gaps await more fundamental change in the nature of our society.”

References


Past Issues:

2017, No. 8: Demystifying the $10 Billion Impact
2017, No. 7: Recent Employment Dynamics
2017, No. 6: Economic Diversity Across South Texas
2007, No. 5: Local Business Dynamics
2017, No. 4: Housing Market Downswing?
2017, No. 3: Impacts of Rising Seas
2017, No. 2: Closing Income Gaps with Education
2017, No. 1: Seasonal Employment
2016, No. 12: A Tale of Two Oil Towns
2016, No. 11: Where You Live Matters
2016, No. 10: How Distressed is Our Community?
2016, No. 9: Disparities in Local Business
2016, No. 8: Understanding Local Unemployment
2016, No. 7: Corpus Christi by the Rankings
2016, No. 6: Local Divergence after the Fall
2016, No. 5: Advanced Manufacturing Drives Local Economy
2016, No. 4: Survival of the Fittest in Texas Oil
2016, No. 3: Local Health Care Dilemma
2016, No. 2: Economic Disparity Among Us
2016, No. 1: Small Business Climate

Economic Pulse

is a joint publication of the South Texas Economic Development Center, the College of Business, and the EDA University Center at Texas A&M University-Corpus Christi. Material may be reprinted if the source is properly credited.

Any opinions expressed or implied are solely those of the original authors and do not reflect the views of the College of Business or Texas A&M University-Corpus Christi. Send correspondence to Jim Lee, (361) 825-5831 or email jlee@tamucc.edu.

For past issues of this newsletter and other publications, visit us online at: SouthTexasEconomy.com