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“From Inequality to Equality: Hypothesizing about the Possibilities”

Income inequality is an important topic this year. However, given sufficient effort on the part of Whites and Blacks, income inequality can be reduced. Generally, if Blacks obtain the right kinds of education and training and engage in more entrepreneurship, and if Whites open the lines of opportunity for hiring and promoting Blacks and begin to patronize Black businesses more vigorously, then the income gap can be narrowed.

What is, in my opinion, a more important and pernicious economic inequality, is wealth inequality. The Federal Reserve Board’s (FRB’s) 2010 Survey of Consumer Finances (SCF) revealed that median (half of households above and half below) White net worth (wealth) was \$130.6 thousand. For Nonwhites or Hispanics (including Blacks), it was just \$20.4 thousand. In other words, the median White household had more than 6 times more wealth than the median Black household.

This may seem like an insurmountable wealth gap. In fact, we have argued in earlier commentaries that for Blacks to achieve wealth equality with Whites, the former must receive a gift. We have also argued that Blacks have no workable plan for closing the White-Black wealth gap.

This commentary shines a different light on that thinking. Recently, we sat down with a computer and began to test certain hypotheses concerning the White-Black wealth gap. Here is what we did, how we hypothesized, and the related results.

First, in addition to the above cited net worth or wealth estimates from the SCF, we obtained information about median White (\$52.9 thousand) versus Nonwhite (\$34.6 thousand) household income and the median desired saving rate for households (about 10%). Second, we obtained information about long-term rates of return or earnings based on the Standard and Poor’s 500 Index, which is a broad measure of investment earnings from the US stock market. That rate was about 7.5% over the past nearly 60 years.

Third we hypothesized as follows:

- White and Nonwhite median incomes would grow at about a 2.0% rate into the future—this is consistent with the FRB’s policy of restraining inflation at about the 2.0% level. In other words, it is hypothesized that incomes will keep pace with inflation.
- Whites would continue to save at about a 10% rate going forward, but Nonwhites (Blacks) would save at a 15% rate. If Blacks want to catch up and achieve equality, then some sacrifice will be required. Consider that some Blacks gift 10% of their incomes to churches today. Therefore, it may be possible for Blacks to shift out of church saving and into personal saving plans that set aside 15% of their incomes for long-term future investment.

- Whites would earn the long-term S&P 500 average rate of return (7.5%); however, Nonwhites (Blacks) would average a slightly higher rate of return (9.0%). We will come back to this point in a moment.
- Both Whites and Blacks would be taxed on investment (capital gains) earnings at about a 20% rate—the current tax rate for long-term capital gains for many taxpayers.

A priori, each of these hypotheses seem fairly reasonable, except for the one concerning rates of return. Why would we expect Whites to receive a rate of return lower than that of Nonwhites or Blacks? The answer lies not so much in what is expected, but in what might be possible.

If Black entrepreneurs can gain access to Black savings and use their special kinship relationships with the world's people of color to invest those savings in a rising Africa or other emerging markets where the rates of return might be higher, then Blacks might be able to earn a slightly higher average rate of return than would be available to Whites in the US. In addition, if Black entrepreneurs could constitute the Black community as a type of emerging market and learn to squeeze higher rates of return out of businesses in that market, then a higher than “normal” rate of return might be possible for Black investment. For now, let's just assume that it is possible for Blacks to earn a rate of return that is slightly higher than that available to Whites.

In combination, the higher saving rate and higher average rate of return make it possible for Blacks to catch up with White median wealth.

Using a computer simulation, we found that at first the wealth gap grows, but within less than 60 years that gap begins to close.

In just over 70 years, the median wealth gap not only closes but switches to Black Americans' favor!

This and similar scenarios show that it is possible for Black Americans to achieve wealth equality with Whites over the long haul, if the former are willing to maintain a very aggressive saving and investment plan. The only questions left to answer are: (1) Are Blacks willing to wait so long? (2) Are Blacks willing to make the sacrifices? and (3) Are the hypotheses realistic?

On the first question, Blacks have historically shown a unique and high level of patience, so they may be willing to wait. On the second question, it seems that Blacks are willing to sacrifice when they are advised on the benefits of the sacrifice, and if they can see the return at the end of the line. As for the third question, it can only be answered by future Black entrepreneurs who are willing to venture out on behalf of their fellow Black Americans to seek higher rates of return in markets around the world and at home.

If the answers to the three questions are “yes,” then this hypothesizing about moving from wealth inequality to equality can become more than a possibility. It can become a reality!

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