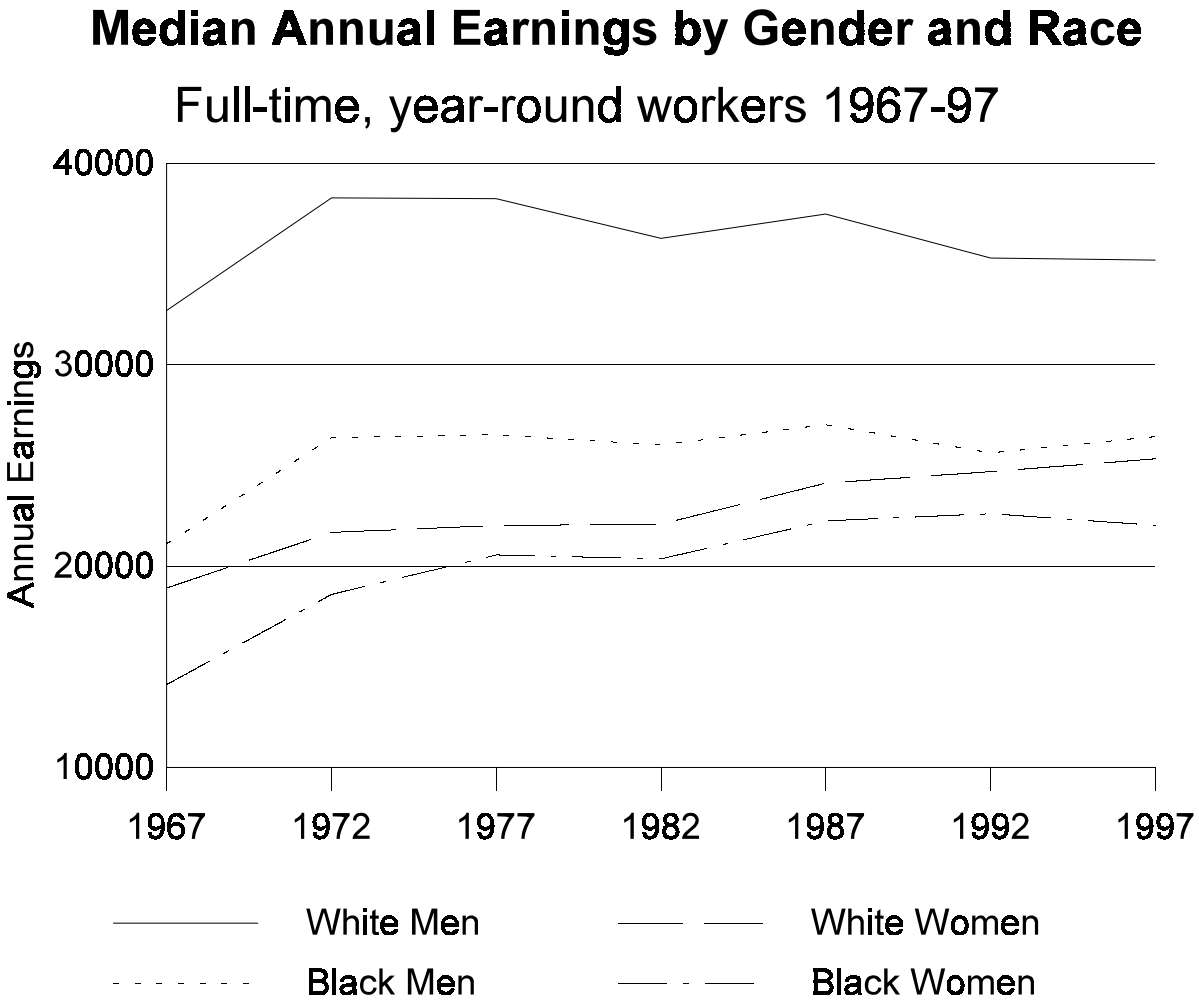
Discrimination in Labor Markets

A. Introduction

1. Disparities in earnings across groups



a. annual earnings of black men and women and white women are less than those of white men

b. some convergence in recent years (due mostly to drop in earnings for white men)

c. pre-1967 differences were even more pronounced

2. How do we account for these differences? To what extent do they reflect discrimination?
3. Concepts (Cain 1986)
    a. Discrimination – unequal *treatment* for members of groups who differ on some observable characteristic such as gender or ethnicity but do not vary in their underlying productivity; unequal treatment of otherwise equal individuals
    b. Individual discrimination – unequal treatment of an individual or by an individual firm
    c. Market discrimination – unequal outcomes for all members of a particular group; in labor markets, we typically focus on wage outcomes
    d. Prejudice – psychic disutility associated with a worker's demographic or other characteristics which are unrelated to the worker's productivity (motivation for individual discrimination)
    e. Segregation – unequal representation of different groups with equal productivity and motivation in different markets or occupations

B. Theoretical Models of Discrimination (Cain 1986)
    2. Discrimination by consumers
        a. price of discrimination
            1. assume that consumers are prejudiced (have tastes for discrimination) and are willing to pay a different price to associate only majority workers
            2. price of a majority worker, p

3. price of a minority worker, $p - d$
4. d captures the value of the taste for discrimination

b. advantages of measure: continuous, potentially measurable, cost interpretation

c. disadvantages: does not measure stigma felt by victim, requires interaction between minority workers and consumers

d. leads to segregation but not necessarily wage differentials; hence, market level of discrimination might well be zero

e. provides an insight into the difference between individual- and market-level discrimination

f. more intriguing insight: segregation eliminates wage discrimination

2. Discrimination by workers

a. majority worker's wage demand with other majority workers, w

b. demand with minority workers, $w + d$

c. again leads to segregation but not necessarily market discrimination; if there are equal skills across workers, competition among employers, and mobility across markets, minority workers can still earn w elsewhere

3. Discrimination by employers

a. assume all employers discriminate and set wages for minority workers at $w - D$; this does lead to a sustainable equilibrium

b. if instead employers discriminate to varying degrees ($w - d_i$), market differential will (if there are few

enough minority workers) simply be the lowest level of d_i (0 if some employers do not discriminate)

c. again, the model leads to segregation but not necessarily wage discrimination

4. Product monopoly
   a. two advantages of assuming a monopoly:
      1) definitional uniformity in tastes
      2) above-competitive profits to support d_i
   b. disadvantage: does not necessarily translate to monopoly power in labor market
   c. thus, the firm would still have to pay w to minority workers, though it could segregate workers or pay higher wages to majority workers
5. Monopsony – single buyer of labor
   a. in this case the firm has power in the labor market
   b. permits exploitation ([VMP − w] / w); greater exploitation allowed for group with more inelastic labor supply curve
   c. genuine monopsonies (e.g., one company towns) are rare; although its not hard to imagine that some firms at some times have a limited amount of market power
   d. need to consider the elasticity of labor supply carefully; for instance, the model does not explain discrimination against women (who presumably have more elastic labor supply curves than men)
6. Labor unions as monopolies
   a. to secure monopoly rents, some method of restricting

entry is a necessary first step

b. if discrimination is consistent with members' tastes, could help to prevent members from defecting

c. not clear that union story matches up with time series evidence on discrimination

d. also is not consistent with recent trends in union membership

7. Statistical discrimination

a. let q be worker's true innate productivity

b. employer observes $y = q + u$; y provides employers with a signal of q

c. employers pay $w = \mathrm{E}(q \mid y)$

d. leads to individual discrimination but not group discrimination (in fact some minority workers are made better off)

C. Empirical tests

2. Regression methods

a. Standard model, regress earnings on a set of observed productivity characteristics, $\boldsymbol{X}$, and a group (minority = 1) identifier, Z

$$W = \boldsymbol{X}'\mathbf{B} + AZ + e$$

estimates that $A < 0$ are taken to indicate that discrimination is present

b. first issue is whether the productivity characteristics are exogenous or reflect past or pre-market discrimination

1) e.g., previous employers could have discriminated in deciding whether to provide training
2) there may be segregation or discrimination in access to quality schooling
3) no simple rules as to what variables to include

c. second issue is the possibility that a productivity characteristic that is correlated with group status is omitted
1) leads to omitted variable bias
2) effects of productivity and group status will be confounded

d. findings
1) using "standard" controls for productivity such as level of schooling and potential work experience typically reduces but does not eliminate the differences in wages
2) including more elaborate productivity/ability controls such as AFQT (see, e.g., O'Neill 1990) can eliminate the difference in wages

3. Audit methods
a. methodology
1) send two equally (or artificially) matched job candidates to apply for jobs
2) record the reactions that each encounters
3) look for systematic differences in treatment

b. advantages:
1) presumably controls for productivity differences

2) can examine reactions at all stages of the application process
3) is useful in detecting subtle differences in behavior

c. disadvantages:
1) hard to truly control for all relevant differences; Heckman (1998) shows how particular distributions of relevant differences can lead to false conclusions of discrimination
2) relatively expensive (have to train and compensate testers)
3) informed testers may look too hard for differences (more generally, there may be differences in perceptions between majority and minority testers)
4) possibly unethical (people are applying for jobs they don't intend to fill and taking up firms' interviewing resources)
5) only indicates individual discrimination, not market discrimination

d. results from Urban Institute study in Washington (from Heckman 1998)
1) both get job 16.6%
2) neither gets job 58.5%
3) white gets job, black doesn't 19.1%
4) black gets job, white doesn't 5.8%
5) does this indicate discrimination?
6) Heckman (p.105) argues: "Only a zealot can see evidence in these data of pervasive discrimination

in the U.S. labor market" (basis of this argument is that whites are treated favorably only 19.1% of time)

7) viewed another way, the chances for employment are substantially higher for whites vs. blacks (35.7% vs. 22.4%)

References

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