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The Structures that Bind: An Examination of Housing and Wealth Inequality in America and a Proposal for an Effective Economic Solution

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Introduction

What is owning a home for most families? For some, they buy a house as a stable place to spend their lives, so the financial benefits of homeownership are of secondary importance. For others, the financial benefits are the primary motivation for homeownership, but one thing remains constant across both scenarios; owning a home is an effective way to generate wealth and maintain financial stability. For most, if not all, middle and lower-income families, their home is their biggest asset and therefore often their biggest liability before their mortgage is paid in full. By understanding this, another question makes itself clear. Why do more white families own homes than Black families do? In other words, why does housing inequality persist and what can be done as a solution?

This paper intends to answer these questions by synthesizing existing literature to examine the intersection of housing inequality and wealth inequality as well as proposing a potential economic solution in the form of a public banking option for the United States. While it may not initially seem as such, housing and wealth inequality are in an incredibly complex, interdisciplinary relationship with each other that extends far past the scope of economics alone. The mechanisms which reinforce inequality have roots in law, education, sociology and community impact, which can't always be captured by a researcher. The list of mechanisms goes on, which makes it so that a single solution cannot resolve inequality by itself. In order to properly address this housing inequality, a myriad of interdisciplinary interventions must be employed to attack the root cause of housing inequality, which in essence, is wealth inequality.

With roaring wealth and housing inequality today, it's clear that current political solutions are not adequate. On both sides of the political arena, the solutions being proposed are 'Band-Aid' fixes, meaning that they may be addressing the most visible structures of inequality, but are not addressing the core problem: existing wealth differentials in the United States. Conservatives argue that freeing the housing market will address much of the inequality within it, whereas liberals advocate for affordable housing solutions and anti-discrimination legislation. While these may all be viable solutions and even an important part of a wider solution, as stated before, when used individually, they are 'Band-Aid' fixes and do not address broader wealth inequality. Therefore, they are unable to make a significant impact on inequality in the long-run.

Economically speaking, breaking the cycle of inequality is not an easy task. There are few effective methods of redistributing wealth in an effort to lessen racial inequality. Often, when thinking about ways to redistribute wealth, one of the first things that most people think of are paying reparations to descendents of enslaved Black Americans. The systemic racism which is pervasive in American history means that Black families today are still experiencing the long-term impacts of post-Civil War, anti-Black legislation, such as Jim Crow, which was a series of anti-back laws passed in the Southern United States between 1877 and the mid-1960s.[1] This was the era of 'separate but equal' even though public and private services for Black individuals were anything but equal. This included financial services, which left many Black residents unbanked and unable to generate wealth. Without saving accounts or investments of any kind, Black people did not have anything to leave their children in terms of generational wealth. The income inequality and discrimination experienced by Black communities after the passage of the Civil Rights Act further prevented Black people from generating wealth or purchasing homes. It's important to keep in mind that this is not ancient history. These events all took place in the last 200 years, but the mechanisms which enable inequality became so heavily

[1] David Pilgrim, "What Was Jim Crow?," September 2012, https://www.ferris.edu/jimcrow/what.htm.

ingrained in American social life and politics that current solutions are not capable of fully addressing the issue.

Our focus, then, should be on not applying Band-Aids to the most visible structures of inequality, it should be on transforming the U.S. financial system into a model that is accessible and works for all families, not just those that are profitable. One potential way to accomplish this is by employing a Public Banking option in the United States. One of the key barriers to generating wealth is a lack of access to basic financial services, so facilitating accessibility to financial services via public banks would make wealth building easier for many disenfranchised Black families. Financial inclusion is a crucial part of disassembling inequality since financial exclusion generally exacerbates existing wealth inequalities.[2] Public banks can offer affordable financial services and reinvest into the communities that they serve in order to redistribute wealth and transform the financial system so that all Americans have equal opportunities to build wealth.

If America treats banking as a universal public service, as it does for the USPS, it would be well positioned to address some of the systemic, economic problems that people of color face. At the risk of sounding like a broken record, one single solution cannot break the cycle of inequality. A public banking option may address the economic mechanisms which enable inequality, but do little to no good at addressing social concerns such as the ongoing racial conflict in cities across the United States. In order for a public banking system to be an effective solution, it would have to be supplemented with other legislation to tackle the mechanisms which public banks cannot. Political reforms in policing, the education of the oppression of Blacks and

[2] Thomas Herndon and Mark Paul, "A Public Banking Option as a Mode of Regulation for Household Financial Services in the US," *Journal of Post Keynesian Economics* 43, no. 4 (March 2020): 576–607.

reparations to descendents of enslaved Black Americans would all be effective supplemental practices with a public banking option.

It is, without a shadow of doubt, clear that housing inequality is a highly pervasive problem which has repercussions broader than just that of the housing market. For Black folks, housing inequality quite literally impacts their everyday life, socially and financially. This is not an issue that can be simply solved with the construction of additional affordable housing units. It's interdisciplinary nature makes it so that a solution would have to be equally complex and while public banks may only address the economic implications of inequality, they are uniquely positioned to address these implications quite well.

Chapter 1: The Cycle of Inequality

Overview of Housing Discrimination and it's Importance

The question of whether to rent or own property is one that essentially every household in America has to answer, and undoubtedly, the goal for many families is to eventually own a home. Generally speaking, many people think of owning a home as having a place to live, which is true, but it is also typically the largest asset that most families possess. A house is a vehicle for financial stability and generational wealth, yet, a remarkable amount of Americans don't own one. This is especially the case for people of color, who have disproportionately lower homeownership rates, implying that a meaningful racial differential in housing exists in the United States. The racial inequality in housing, in large part, stems from the residential segregation and housing discrimination which began around 1890, when the first sizable wave of Black Americans moved from the South to the Northern and Western regions of the United States.[3] It continued through 1990 and is sometimes still seen today. The impacts of residential segregation, however, still proliferate today's societies and many racial boundaries drawn in 20th century cities are still clearly visible in the 21st century.

It's important to first examine why owning a home is socially and financially important in today's society because it helps illustrate why racial housing inequality is so impactful on families of color. The process of purchasing a home drives households to save for expenditures such as down and mortgage payments. This saving, naturally, increases a household's net wealth. Once accumulated, these savings are invested in an appreciating asset (i.e. a home). Since houses generally increase in value over time, a homeowner's net wealth increases in unison with that of

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[3] David M. Cutler, Edward L. Glaeser, and Jacob L. Vidgor, "The Rise and Decline of the American Ghetto," *Journal of Political Economy* 107, no. 3 (1999): 455–506.

their home.[4] The opportunity of homeownership is unique since it gives families a chance to invest in a highly leveraged asset which generally grows over time at a rate faster than that of inflation. With this in mind, even a small percentage return on that asset leads to significant returns on invested capital.[5] Di et al. (2007) showed that, in a study conducted from 1989 to 2000, all homeowners, regardless of duration of ownership, had more wealth in 2001 than those who rented during that period, with all else equal.[6] For homeowners whose largest asset is their house, this effect is amplified since their home is proportionally larger in comparison to their other financial assets. This is the case for a large number of American households, especially those in lower income brackets. In 2001, home value constituted 42% of total household net wealth of all homeowners and 77% of total net wealth of lower income households.[7] Since 77% of total net wealth of low income households is constituted by their home value, it is natural that an increase in the value of their home has a larger impact on their net wealth as compared to a typical American household.

In terms of creating generational wealth, if parents buy a house to raise their children in and keep it for their lifetime, their house will appreciate and create wealth for their children once the parents are no longer around. Through generations, this highly impactful process is capable

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[4] Tracy M. Turner and Heather Luea, "Homeownership, Wealth Accumulation and Income Status," *Journal of Housing Economics* 18, no. 2 (June 1, 2009): 104–14, https://doi.org/10.1016/j.jhe.2009.04.005.

[5] Zhu Xiao Di, Eric Belsky, and Xiaodong Liu, "Do Homeowners Achieve More Household Wealth in the Long Run?," *Journal of Housing Economics* 16, no. 3 (November 1, 2007): 274–90, https://doi.org/10.1016/j.jhe.2007.08.001.

[6] Zhu Xiao Di, Eric Belsky, and Xiaodong Liu, "Do Homeowners Achieve More Household Wealth in the Long Run?," *Journal of Housing Economics* 16, no. 3 (November 1, 2007): 274–90, https://doi.org/10.1016/j.jhe.2007.08.001.

[7] Turner and Luea, "Homeownership, Wealth Accumulation and Income Status."

of shaping the future of a family. Turner and Luea (2009) show that in an average American household, when accounting for the skew of wealth distribution, an additional year of home ownership equated to an increase of $13,700 in total net wealth.[8]

Putting financial reasoning aside, owning a home in the U.S. is something of a status symbol within society. Part of the picture of the "American Dream" during the 20th century was home ownership, and while not as blatant, that idea certainly hasn't been abandoned in recent years. A home is a symbol of success and stability in American society and people are willing to save for a lifetime in order to eventually buy one. Other than personal relationships, there are not many things deemed more central to life than a house, so it makes sense why people are willing to go to great lengths for them.

According to the United States Census Bureau's 2021 data, the home ownership rate for White, Non-Hispanic householders is 74.2%, whereas that rate for Black householders is much lower at 44.6%.[9] This, in itself, shows how disproportionate racial home ownership rates are, even in today's society. Keeping in mind the societal and financial importance of home ownership, this disparity becomes even more meaningful. Since the homeownership rate is much lower for Black householders, there is a much greater portion of families that aren't gaining the societal benefits that come with owning property.

Families that are considered housing insecure are those that have difficulty paying rent and affording other month-to-month expenses. With that in mind, in 2018, there were 38.1 million people living below the poverty line, making up roughly 12% of the U.S. population. It's reasonable to assume that many of these people are considered housing insecure, which shows

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[8] Turner and Luea.

[9] "Quarterly Residential Vacancies and Homeownershpi, Second Quarter 2021" (FRED Economic Data, n.d.).

just one level of the problem. When lawmakers create policies that restrict housing supply, housing becomes inaccessible for low income families. As a result, housing prices rise and wealth inequality worsens.[10]

It's crucial that one looks at the historical context that put America in this predicament. American history is riddled with housing discrimination, and the resulting residential segregation remains one of the primary, underlying causes of today's housing inequality. The Great Migration of Southern Black families to the Northern United States in the 19th and 20th century is the prime example of this process. Before moving on, it's important to note that housing discrimination was not the sole driver for many Black families to relocate and there were many other social pressures including worsening racial violence and escaping the oppression of Jim Crow that lead families to look for alternative solutions.[11] The Great Migration saw over 6 million African Americans move from the American South to the Northern, Midwestern and Western regions of the country from roughly 1910 to 1970. Both World War I and World War II played an influential role in shaping The Great Migration because able-bodied, white men were being drafted into the armed forces and therefore being removed from industrial positions in the North. This created a wealth of opportunities in non-agricultural industries that Black Americans were eager to capitalize on by moving North. Since both World Wars facilitated this Great Migration, there were essentially two Great Migrations. The first facilitated by World War I and the second facilitated by World War II. There was still a certain amount of movement by Black Americans in between and after the wars, but the periods of greatest movement were dominated by these wras. For perspective, from 1940-1949 there were 1,450,000 Black Americans that

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[10] Mary Cleveland, "Homelessness and Inequality," *American Journal of Economics and Sociology* 79, no. 2 (March 2020): 559–90.
[11] "The Great Migration (1910-1970)," National Archives, May 20, 2021, https://www.archives.gov/research/african-americans/migrations/great-migration.

moved from the South. Ten years earlier, from 1930-1939, there were only about 390,000 people of color that moved.[12]

This is by no means an insignificant number of people, but it was much less than the amount during World War II. Unfortunately, those that moved during the Second Great Migration were met with increasing housing discrimination in the American North and West, which helped create the racial wealth inequalty which exists today.[13] Redlining, racially restrictive covenants, implicit and explicit threats of violence and general social tensions kept Black people out of white neighborhoods. Black neighborhoods, meanwhile, were blighted and crowded and African-Americans paid more than whites for equivalent housing and neighborhoods.[14] In the mid-twentieth century, these practices were commonplace. Before the 1970's when centralized racism was replaced with a more decentralized model and started to decline altogether, housing discrimination was essentially legal in the way it was handled by the United States Government. With the support of the law, housing discrimination was allowed to thrive in most regions of the US.

It's important to note that housing discrimination and residential segregation are not the same. Housing discrimination describes a process which creates residential segregation as a byproduct. It starts with community members, local officials and realtors creating barriers to entry in housing markets in order to prevent certain 'types' of people from entering a particular area or neighborhood. The most referred-to example of this is known as redlining, and was prolific throughout the mid-to-late 20th century. Influential legislation, including zoning laws

[12] "Great Migration," accessed October 12, 2021, https://depts.washington.edu/moving1/black_migration.shtml.

[13] "The Great Migration (1910-1970)."

[14] Cutler, Glaeser, and Vidgor, "The Rise and Decline of the American Ghetto."

and building capacity laws, enabled housing discimination to thrive in the 20th century.[15] This social and economic exchange, however, was not strictly limited to only the buyer and seller. As previously mentioned, community members or neighbors are a crucial, additional party involved. The voices of existing homeowners tend to be heard much louder than those looking to move into established communities by those who directly influence the house-buying process. Community preferences in regards to who resides in certain areas are by and large motivated by racism and home value. These two motivations are much more connected to each other than is immediately obvious. Concerns over home value are driven by the racist misconception that people of color reduce neighbourhood housing prices. White homeowners were concerned that their own house would decrease in value if a Black neighbor moved in. At their core, community preferences are driven solely by racism, which can manifest itself through different concerns about a community. One can clearly observe this in regards to home value. Cutler et al. (1997) argue that "segregation was enforced by collective actions on the part of whites to limit the access of blacks to white neighborhoods".[16] White residents absolutely did not want Black residents to move in, and they would act collectively to ensure that they didn't. As more and more people of color get turned away from white communities, new housing accommodations are pursued which Black families can afford to live in. On a large scale, as was the case in the United States, many of these people end up gravitating towards the same, more accessible areas.

Over time, the process of housing discrimination produces residential segregation by slowly moving people of color away from white neighborhoods and into neighboorhoods populated by people of color, which creates distinct racial lines between communities.

[15] Cleveland, "Homelessness and Inequality."

[16] Cutler, Glaeser, and Vidgor, "The Rise and Decline of the American Ghetto."

Non-white residents disproportionately live in low-income communities which are geographically and socially far from economic opportunities.[17] These lower income neighborhoods are often older, blighted areas which can contribute to low public morale, reducing motivation to attain such opportunities. Since these opportunities are generally far from affordable neighborhoods, increases in transportation costs can also inhibit residents' ability to pursue them. Many high paying jobs are located in expensive communities, which are usually distanced from the lower income areas where many people of color live. These increases in costs inhibit financial growth because families would have to reduce spending in another area of their budget, which often isn't possible.

It's also important to think about the implications of the relationship between housing and education. Many schools in low-income neighborhoods often do not perform as well as schools in wealthier, white communities. As a result, children are not given the tools that they need to increase long term economic opportunities when that time comes. It goes without saying that there are, of course, outliers to this and education is not always correlated with economic success. Due to the range of opportunities that are limited in low income communities, families are often "stuck" in these areas.

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[17] George Mason et al., "Residential Segregation and Desegregation: Is Housing Discrimination a Relevant Sociological Issue in the Twenty-First Century?," in *Conference Papers -- American Sociological Association* (Conference Papers -- American Sociological Association, American Sociological Association, 2006), http://ezprox.bard.edu/login?url=http://search.ebscohost.com/login.aspx?direct=true&db=sih&AN=26643196&site=ehost-live.

Redlining in 20th Century America

As previously mentioned, redlining was arguably the most proliferated form of housing discrimination in America. Redlining is a practice that involves the systematic denial of loans or other financial services to people of color that are attempting to buy property in white-dominated communities. The Federal Housing Administration which was established in 1934, essentially started the practice of redlining by refusing to insure mortgages in and around Black neighborhoods.[18] Redlining is traditionally motivated in one of two ways. It's based around the fallacy that black borrowers are poor financial risks and are a detriment to their communities, which is obviously based in racism. Aside from false ideals surrounding financial risks, it's likely that there was also the denial of loans simply because applicants were Black, with no consideration of finances. In other words, redlining was both rooted in racism *and* a perceived inability to pay back loans, which is not as overtly racist. In reality, when African Americans tried to buy homes in traditionally white communities, home value generally rose because African-American families were willing to pay more for properties than white families were. Black families were willing to spend more because their housing supply was so restricted that they were much more desperate for a home.[19] The practice of redlining effectively isolated Black people in neighborhoods that received much less investment than similar white neighborhoods.

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[18] Terry Gross, "A 'Forgotten History' Of How The U.S. Government Segregated America," NPR, May 3, 2017, https://www.npr.org/2017/05/03/526655831/a-forgotten-history-of-how-the-u-s-government-segregated-america.

[19] Gross.

This prevented generations of Black people from gaining equity in homeownership for greater long-term financial stability. [20]

In addition to the discriminatory and predatory lending involved with redlining, privately adopted, racially restrictive housing covenants started popping up around the country and many of them had government support.[21] Racial deed restrictions meant owners were contractually prohibited from selling their property to a person of color, which is housing discrimination in its most explicit form. By 1968 when the Fair Housing Act was passed, it was still illegal for the state to act on many of the racially restrictive deeds, because the legal contract had not expired.[22] Essentially, this was a legal loophole for realtors and homeowners which allowed them to legally discriminate against people of color. In certain cases during the early-to-mid 1900's, the US Government was even in support of some of these covenants. The Supreme Court of Louisiana supported a covenant prohibiting the sale of land to African Americans in the 1915 case *Queensborough Land Co. vs Cazeaux*[23] and in the 1927 case of *Schulte Vs Stark,* the Michigan Supreme Court supported racially restrictive covenants[24] [25]. This support was not concealed or

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[20] David Harshbarger and Andre Perry, "America's Formerly Redlined Neighborhoods Have Changed, and so Must Solutions to Rectify Them," *Brookings* (blog), October 14, 2019, https://www.brookings.edu/research/americas-formerly-redlines-areas-changed-so-must-solutions/.

[21] Mason et al., "Residential Segregation and Desegregation."

[22] "Racial Restrictive Covenants - Seattle Civil Rights and Labor History Project," accessed May 12, 2021, https://depts.washington.edu/civilr/covenants.htm.

[23] Case Law Access Project, "Queensborough Land Co. v. Cazeaux, 136 La. 724, 67 So. 641 (1915)," accessed October 21, 2021, https://cite.case.law/la/136/724/.

[24] "Schulte v. Starks, 238 Mich. 102," accessed October 21, 2021, https://casetext.com/case/schulte-v-starks.

[25] Mason et al., "Residential Segregation and Desegregation."

hidden either. They were actually quite blatant, determining that "It is settled by former decisions of this court that a restraint upon occupancy of the lots of a subdivision by colored persons is valid and enforceable" While redlining may still exist to some degree, it has mostly been sidelined by aunty-discrimination legislation. With that said, however, the long term effects of redlining are still ones that many people of color have to cope with in their day-to-day lives. While there might not be active redlining happening at scale, the racial boundaries that redlining set in the 20th century still exist in American cities today.

For the next 30 years, Black families continued to be denied loans or were turned away from white neighborhoods and therefore were unable to buy a house, but with the 1960's and the Civil Rights movement gaining momentum, change seemed near. A particularly influential piece of legislation introduced during the Civil Rights era was Title VIII of the Civil Rights Act, also known as the Fair Housing Act of 1968. Title VIII made it illegal to discriminate based on race, color, religion, sex, familial status, or national origin in the housing market.[26]

How are Inequality and Discrimination Perpetuated?

As is the case with most of the Civil Rights Act, the Fair Housing Act had a positive impact on race inequality, but did not solve the problem entirely. In the years following the Fair Housing Act, housing inequality and discrimination were beginning to decline. This is likely predominantly due to the impact of the Fair Housing Act. The Civil Rights movement as well as rising Black income and education helped diminish segregation, but the Fair Housing Act only addressed instances of discrimination if they were reported by the victim to the Department of Housing and Urban Development (HUD), which is problematic for several reasons. First, since

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[26] "The Fair Housing Act," August 6, 2015, https://www.justice.gov/crt/fair-housing-act-1.

the victim must report the incident to the HUD, they must be aware that they were discriminated against. In instances of redlining, it can be impossible to know that one was discriminated against. A bank does not have to provide a reasonable explanation as to why a borrower was denied a loan, so there isn't a way for that borrower to know they have been a victim of redlining. Discrimination would have to be very blatant, and the victim would have to be very aware of discriminatory practices generally in order for this model to function even mildly effectively. Additionally, the reach of the Fair Housing Act stopped at federally owned, operated, or funded properties, which did little to no good in addressing discrimination in the private housing market.[27] Additionally, in many racially restrictive covenants, the length of the contractual obligations of white homeowners to not sell their home to a Black family extended past the date of passage of the Fair Housing Act. Since the covenants were bound by contract, there was very little that legislation could do to break those contracts. The result was a number of restrictive covenants that continued to exist in the years following the passing of the Fair Housing Act.

Cutler et. al. (1997) present three theories which are meant to explain how segregation is created and perpetuated. They call their first theory the "Port of Entry", and it is particularly applicable to migrants such as those who moved during the Great Migration. Recent migrants tend to cluster amongst their own group in an effort to recreate familiar social environments. They describe this process as a typical depiction of "immigrant ghettos"[28]. It seems that recent immigrants often have a tendency to settle with people like themselves, either racially or culturally. It's important to note that this by no means claims that people of color caused their

[27] Mason et al., "Residential Segregation and Desegregation."

[28] Cutler, Glaeser, and Vidgor, "The Rise and Decline of the American Ghetto."

own segregation, but rather it is a means of describing the tendencies of recent migrants. The theory of "Collective Action Racism" is the most widely-recognized cause of segregation in America. Collective action can take several forms, the first of which being policy and legislation allowing and even promoting housing discrimination. Both redlining and racially-restrictive covenants are examples of Collective Action Racism. This also includes organized community activities such as "threatened lynchings or fire bombings that discourage blacks from moving into white neighborhoods"[29]. Efforts made on the part of both legislators and community members barred black families from white communities, forcing them to cluster in mostly Black neighborhoods. Cutler's third and final theory is that of "Decentralized Racism". Rather than collective action taken against Black people, decentralized racism describes white peoples' preference and decision to live with other white people. Because white people that are looking for a home are willing to pay more than blacks to live in predominantly white neighborhoods, housing could eventually become completely segregated.[30] While these are some of the mechanisms that create segregation, they are mostly a thing of the past. The underlying racial preferences, however, have not changed in many cases and segregation persists even without the collective action that created it.

At this point, it's obvious that housing inequality has been constructed through social processes, but those are not the only means in which it can thrive. Economically speaking, there are many contributing factors to the inequality seen today. Most basically, increases in housing prices continue to make it difficult for low-income households to invest in their future by purchasing a home. In 2000, the average home cost $167,500 and when adjusted for inflation it

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[29] Cutler, Glaeser, and Vidgor.

[30] Cutler, Glaeser, and Vidgor.

cost $268,567.10. In 2020, the average home cost $336,950[31] [32]. This is a $68,383 increase in the inflation-adjusted price within just two decades which is very significant, especially for families with little extra savings or income. For perspective, this is roughly a 25% increase in housing price in a 20 year time period, which is astonishing. Within the same time period, however, the median household income for Black families increased from $44,166 in 2000 to $45,438 in 2019. This is only about a 2% increase, which proportionally only represents about 10% of the increases in income for white earners in the same period. Black households are disproportionately affected by recent jumps in housing prices, which white people are more capable of responding to since they are making more money to begin with. Using the 2019 Survey of Consumer Finances, one can see that mean and median net wealth for Black Families are only about 15% of that for white families.[33] This racial wealth gap is exceedingly large and shows the sad truth of wealth disparities in the United States. This small size of the increase in median income, and more specifically, the wage gap facing people of color across the country is entirely socially constructed through many of the mechanisms discussed in this paper. Things like collective action racism, redlining and racially restrictive housing covenants were all created through social mechanisms by white people to keep Black people out of white communities.

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[31] U.S. Bureau of Labor Statistics, "Consumer Price Index for All Urban Consumers: Housing in U.S. City Average," FRED, Federal Reserve Bank of St. Louis (FRED, Federal Reserve Bank of St. Louis, January 1, 1967), https://fred.stlouisfed.org/series/CPIHOSNS.

[32] U.S. Census Bureau and U.S. Department of Housing and Urban Development, "Median Sales Price of Houses Sold for the United States," FRED, Federal Reserve Bank of St. Louis (FRED, Federal Reserve Bank of St. Louis, January 1, 1963), https://fred.stlouisfed.org/series/MSPUS.

[33] Neil Bhutta et al., "Disparities in Wealth by Race and Ethnicity in the 2019 Survey of Consumer Finances," accessed December 2, 2021, https://www.federalreserve.gov/econres/notes/feds-notes/disparities-in-wealth-by-race-and-ethnicity-in-the-2019-survey-of-consumer-finances-20200928.htm.

One might say that income inequality has a direct impact on housing inequality, and another might say that housing inequality is a contributing factor to income inequality. They'd both be correct in the sense that the two intrinsically have a connection, but they would both be wrong because it is not a one-sided impact. These issues are both mechanisms that enable systemic racism and have the ability to impact each other, both positively and negatively. With this in mind, it's important to examine some of the reasons that income inequality exists so that we can better understand its relationship with housing inequality.

On the Intersection of Disrimination in Housing and Labor Markets

While the field of economics of discrimination is proliferated with potential theories to expain income inequality, there are several that are particularly notable. One of those is the Theory of Statistical Discrimination put forth by Edmund S. Phelps. The core of this theory is the idea that the employer who seeks to maximize profits will discriminate against people of color if the employer thinks that those people are less qualified, reliable or long term on average than white applicants or employees[34]. This effect is compounded if obtaining applicant information is particularly difficult because without sufficient information, employers are more likely to resort to using skin color as a proxy for actual qualifications. If, at one point in time, an employer has an unreliable employee that arbitrarily has dark skin, that worker's skin color becomes a replacement for poor reliability in the employer's mind when making hiring and firing decisions in the future. The employer will then assume that the next Black applicant is unreliable and therefore biases enter employers' decision making process. The belief that white workers are

[34] Edmund S. Phelps, "The Statistical Theory of Racism and Sexism," *American Economic Review* 62, no. 4 (September 1972): 659–61.

more desirable may stem from the false assumption that people of color generally grow up in disadvantaged circumstances or have had a poor background. Unfortunately, this manifests in society in a way that is self-perpetuating. The perception that people of color collectively have a poor upbringing has an impact on employment in those communities, which contributes to even poorer conditions, which again impacts employment and so forth. I think that it is fair to say that there is a lower reward for people of color to invest in their own human capital because, in the employer's mind, the consideration of better employment is not one of qualifications, but of skin color.

Considered the pioneer of the economics of discrimination, Gary Becker and his theory of Taste-Based Discrimnation was essentially the first attempt to explain racial income inequality and discrimination. This theory was introduced in 1957 as the Civil Right Movement was building momentum, and the broader conversation of racism and discrimination were brought to the forefront. In Becker's model, an actor must act *as if* they are willing to pay something, either directly or in the form of reduced income, in order to interact with some people, but not with others. Becker considered this as having a taste for discrimination. In order for discrimination to occur, the actor must actually pay or forfeit some of his income for the 'privilege' of interacting only with the people that they choose to. In the case of racial discrimination, white employers with a taste for discrimination are willing to pay a premium for white labor in order to avoid hiring black employees. Becker argues that the amount of discrimination by an actor against a group, depends on physical and social distance as well as their relative socioeconomic status.[35] This again, leads to a cycle of inequality because people tend to discriminate against lower income groups of people, which never allows those people to gain financial stability.

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[35] Gary S. Becker, *The Economics of Discrimination* (University of Chicago Press, 2010).

There are obviously many more theories regarding dicrimination in the labor market, but these two represent some of the more notable examples. The question is, however, which model is accurate? It's hard to say either is accurate when they have both been somewhat widely criticized, but they both provide valuable insight into what drives discrimination in the labor market. One of the larger flaws in Becker's framework is that he argues that in a free market economy, discrimination will eventually disappear because it is not *economically rational* to discriminate, so eventually employers will cease those practices. This has been criticized because it seemingly takes social circumstances out of the equation. While it may not be economically rational to discriminate, that will not change the generational prejudices that are the root cause of disrimination to begin with. With that said, the idea that some employers have a taste for discrimination is very plausible. Statistical discrimination, on the other hand, is significantly more 'solid' in terms of flaws. The model has faced some criticism for being insensitive to the racial struggle of people of color because there is no account for prejudice or racism in the model, which is highly reductive to the experiences of Black folks. With the recent uptick in research being done in this field, we are likely to learn more about the economics of discrimination soon, but even a pioneer in statistical discrimination, Edmund S. Phelps, states that he doesn't know if most discrimination is of a statistical nature, it is just a potential explanation.

All things considered, the discrimination witnessed in the U.S. labor market is most likely some conglomerate of the two models. I think it's safe to assume that there are still racist employers in the workforce, and therefore some level of taste-based discrimination occuring in the market. Similarly, it's safe to assume that there are employers who still use race as a proxy for real human capital investments on the part of people of color.

Given the plethora of concerns regarding early models of labor discrimination, it is natural that many new models begn to emerge. One of the most notable of these models is Michael Reich's (1978), and his argument can be expressed succinctly as: "racial inequality exacerbates racial antagonisms and divisions between black and white workers"[36] As racial divisions are inflamed by inequality, working class solidarity diminishes, lessening the collective bargaining power of the workforce. White workers have a tendency to develop racist attitudes towards black workers because of perceived conceptions that black co-workers decrease their own income, further deepening the division between Black and white workers. Reich argues that the size of the racial income gap is directly correlated with the division of Blacks and whites in the workplace. In other words, the greater the income gap, the deeper the racial divisions. These racial divisions impact both white and black workers because the conflict between them weakens their collective strength against the capitalists. So, for instance, if the workforce for a certain company wanted a raise and if there was income inequality at that company, those workers would have much less power to demand a raise than if they were all receiving equal pay. Generally speaking, Black and white working-class individuals often share many of the same goals, but the ongoing conflict that discrimination causes makes it difficult for them to ally towards these goals. Higher pay, better benefits and better working conditions are just a few examples of common goals shared by Black and white workers, but without their collective bargaining strength, it is very difficult to achieve them. The bartering strength held by the workforce is weakened by discrimination, therefore the workforce holds less power to bargain for increases in wage when the cost of living rises. This means that as time goes on, workers and families will be less able to afford basic living costs, let alone afford large purchases such as a

[36] Michael Reich, "Who Benefits from Racism? The Distribution among Whites of Gains and Losses from Racial Inequality," *The Journal of Human Resources* 13, no. 4 (1978): 524–44, https://doi.org/10.2307/145261.

house or other financial securities. Unfortunately, this exacerbates existing wealth differentials within companies and most extra profit is usually distributed to the higher-ups in those companies, rather than to their workers

Becker and other early economists studying discrimination often argue that racial discrimination hurts capitalists and benefits white workers but Reich argues the opposite. He asserts that capitalists are the only party to benefit from discrimination. Both Black and white workers suffer from the implications of inequality due to their weakened collective solidarity. Both parties suffer because the racial divisions that discrimination created directly inhibits the collective strength within the workplace. If the collective power of an entire workforce were united towards a certain goal, say ending income inequality, they would likely see some level of success; however, since discrimination weakens solidarity, the collective power of a workforce is much weaker and unable to address large concerns such as income inequality. While both Black and white workers may feel the impacts of discrimination, it goes without saying that Black workers are the most highly affected party in this scenario. They are most impacted by weakened workplace solidarity, but are also often being actively discriminated against or facing active racial income inequality, compounding the negative effects of the discrimination that Black workers face.

The impacts of income inequality are generally compounded by discrimination and inequality in housing and credit markets for Black famlies. At first glance, it may seem that housing and income inequality are mildly connected at best; however, upon further examination it becomes clear that they are not separate phenomena. Rather, they are highly interconnected social and economic concerns with many mechanisms that allow them to perpetuate each other. As Gary Dymski (2006) argues, racial wealth differentials represent two things. First, they are representative of a historical legacy of racism and discrimination in financial markets. Second, they represent a constraint on Black families' future economic activity, including purchasing a home.[37] In fact, Dymski makes the claim that active discrimination in labor, housing and credit markets are not as influential to overall wealth inequality since the "existing structural divides in resources and wealth do most of the damage".[38] In essence, he is arguing that active discrimination and income inequality do contribute to overall wealth differentials, but the impact of the resource and monetary constraints faced by Black communities is much greater. In other words, the systemic problems that Black households face when generating wealth are more impactful than the discrimination they experience in their day to day lives. This, however, is not to undermine the impacts of active race-based discrimination. The social, economic and emotional toll that discrimination takes on people of color is very significant and cannot necessarily be expressed through an economic model.

Housing and wealth inequality are involved in a self-perpetuating cycle in which they contribute to each other endlessly, keeping many families 'stuck' in their poor financial situations, while it's very easy for wealthy families to increase their financial standings. This cycle may not have a formal have a starting point; however, it is most logical to examine it starting at discrimination in the labor market because it is easiest to see the connections between mechanisms beginning from labor discrimination. Race-based discrimination in the labor market results in a lower ability to pay off loans and accumulate wealth, which tends to reinforce racial wealth inequality. This resulting inequality, for reasons we've already discussed, inhibits many Black families from purchasing a home, while similarly situated white families *are* able to build

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[37] Gary Dymski, "Discrimination in the Credit and Housing Markets: Findings and Challenges," in *Handbook on the Economics of Discrimination*, 2006, 215–59.

[38] Dymski, "Discrimination in the Credit and Housing Markets: Findings and Challenges."

enough savings to do so. This disparity in home-buying capability contributes to the creation of housing inequality. Meanwhile, housing inequality is being perpetuated by other mechanisms as well, such as discrimination and misinformation, exacerbating existing inequality. Given the importance of owning a home for generating wealth, when Black families are not able to buy homes, they are also not able to build wealth as effectively as white families, which contributes to the creation and continuation of racial wealth inequality. All of these mechanisms that create racial inequality reinforce each other in a vicious cycle which creates poverty and keeps many people in that situation. The interconnected nature of these mechanisms helps shed some light on why inequality is so persistent and economic outcomes for Black families continue to be inadequate as compared to white economic outcomes.

For context, using data from the American Community survey, from 2001 to 2016, the white homeownership rate decreased by only 1% to 71.3% in 2016. In comparison, the Black homeownership rate dropped nearly 5% to 41% in 2016, which is a staggering 30% lower than that for white households.[39] Similarly, median Black income increased from $41,081.50 in 2001 to $41,293.50 in 2016 whereas white income in 2001 was $49,783 and increased to $50,248 in 2016. Black families make, on average, $10,000 less than white families, and that gap is highlighted by the homeownership rate for the same time period. [40]

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[39] Laurie Goodman, Alanna McCargo, and Jun Zhu, "A Closer Look at the Fifteen-Year Drop in Black Homeownership," Urban Institute, February 12, 2018, https://www.urban.org/urban-wire/closer-look-fifteen-year-drop-black-homeownership.

[40] "Median Annual Earnings by Sex, Race, Ethnicity 2019," Tableau Software, accessed December 4, 2021, https://public.tableau.com/views/Mediannannualearningsbysexraceethnicity2019/Earningsbysexraceethnicity?:embed=y&:showVizHome=no&:host_url=https%3A%2F%2Fpublic.tableau.com%2F&:embed_code_version=3&:tabs=no&:toolbar=yes&:animate_transition=yes&:display_static_image=no&:display_spinner=no&:display_overlay=yes&:display_count=yes&:language=en&:loadOrderID=0.

We have already established a few mechanisms which perpetuate this cycle, but Dymski (2006) puts forth a list of restrictions that Black people face which allows inequality to persist. Dymski argues that when market entry is not free, when Blacks or whites have racial preferences, or an informational barrier exists, discrimination costs will continue to placed on Black people, and therefore inequality will persist.[41] It could be argued that entry to housing markets is not free for many black families because of the racial wealth gap, informational barriers and discrimination in housing markets. Because Black households generally cannot afford to buy a home or lack the financial services to do so due to a historical legacy of systemic racism, they are not free to enter the housing market. Whether Black families face discrimination, redlining, a lack of financial services or a lack of capital, they are facing barriers to entry in the housing market. Additionally, it's likely that an informational barrier exists between Black communities and financial institutions, which discourages those institutions from serving marginalized communities. Dymski asserts that if it is expensive to gather accurate information on borrowers, and if, on some level, borrowers' race and economic fundamentals can be correlated, lenders can use the racial composition of a neighborhood as a proxy for expensive information gathering[42], similar to Phelps' model of statistical discrimination in the labor market. Rationally, inequality and discrimination will linger as long as those mechanisms which perpetuate it are free to reinforce each other.

It is quite clear that housing and wealth inequality are highly pervasive in American society, and that there are a number of mechanisms which allow inequality to persist in the long run. Furthermore, it is also clear that they are highly interconnected, and one cannot address one

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[41] Dymski, "Discrimination in the Credit and Housing Markets: Findings and Challenges."

[42] Dymski.

issue without addressing the other. Given the state of racial inequality today, it's safe to assume that any of the measures that the United States have implemented to combat inequality are not performing as expected since it is still prevalent in today's society. Many 'solutions' that the government have devised are equivalent to putting a small Band-Aid on a much larger cut. They employ solutions which may help the most topical issue, but do little to no good solving the much larger, underlying issue. As Mary Cleaveland (2020) puts it, "Conservatives emphasize freeing local housing markets from stifling regulation. Liberals emphasize coercing markets to increase the supply of "affordable" housing by various means, including rent control and obstacles to "gentrification."[43] Neither of these solutions, however, address the larger problem of growing wealth inequality, which creates a substantial amount of housing insecure Black residents. A solution for housing inequality needs to be one that orients itself towards solving wealth inequality, and a public banking option in the United States may do just that.

[43] Cleveland, "Homelessness and Inequality."

Chapter 2: An Appropriate Economic Solution for Racial Inequality

The Importance of Banks and Financial Inclusion in Housing

At this point, it's well established that housing inequality is a vicious, cyclical problem which is somewhat self-perpetuating and therefore won't naturally trend towards equality without external influences. While there are a plethora of potential solutions to this problem, from a financial and economic standpoint, a public banking option would make great strides in reducing the racial housing differential.

Using the 2017 FDIC National Survey of Unbanked and Underbanked Households, Herndon and Paul (2020) determine that 47.3% of Black households lack access to basic financial services and Black households are nearly six times more likely to lack any kind of financial institution than white households.[44] These are striking results as they show the sheer amount of Black families that are unable to use any affordable financial services. Additionally, it's reasonable to assume that many, if not all, of those financially excluded households are not homeowners since it is not feasible to buy a home without basic financial services.

It goes without saying that it is next to impossible for one to engage in any type of financial market without being involved with a financial institution. This is especially the case for mortgages because of the large amount being lent as compared to other types of loans. For smaller loans, such as auto lending solutions or loans to cover emergency expenses, people without access to traditional financial services usually attempt to obtain that credit in other ways such as through pawn shops, and payday or auto-title loans. Mortgages, on the other hand, are

[44] Herndon and Paul, "A Public Banking Option as a Mode of Regulation for Household Financial Services in the US."

often well above $100,000, making non-traditional financial services become all but obsolete. These loans often tend towards usury, which makes it very difficult for borrowers to build savings. Usury law generally prohibits lending at exceptionally high interest rates on loans[45], but many financial services, both traditional and non-traditional, still tend to charge staggeringly high interest rates. Gary Dymski (2006) even goes as far as to say that "usury has been a fine art in credit since the dawn of modern commerce"[46] and while there are laws that outlaw usury, it still persists.

It is becoming clear how important financial inclusion is in the housing market and for building wealth. As d'Alcantara and Gautier (2013) assert, "A lack of access to basic financial services such as credit or saving accounts forms a recognized and critical mechanism in generating persistent income inequality, poverty, as well as slower growth".[47] Without the necessary resources to build credit or save money over time, it's difficult to build wealth or even financial stability in the same way one could through a financial institution. The plethora of services that banks offer, from compounding savings accounts, financial advising and investment accounts enable their clients to build wealth much more effectively than one could without the use of a bank. The wealth-building that can come with banking at an established institution directly helps those people become homeowners, whereas unbanked people lack the tools they need to generate the necessary wealth to purchase a home.

In order to understand the relevance of banks in the housing market moving forward, we first need to understand the needs that aren't being met by current solutions. Financial exclusion

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[45] "Usury," *National Consumer Law Center* (blog), March 7, 2010, https://www.nclc.org/issues/high-cost-small-loans/usury.html.

[46] Dymski, "Discrimination in the Credit and Housing Markets: Findings and Challenges."

[47] G. d'Alcantara and A. Gautier, "The Postal Sector as a Vector of Financial Inclusion," *Annals of Public and Cooperative Economics* 84, no. 2 (June 2013): 119–37.

is, most generally, a lack of access to financial services at a reasonable cost. Thinking about the previous example of payday loans, they tend to be exclusionary because of their unreasonably high interest rates. While payday loans are short-term cash loans ranging from $100 to $1,000, loans typically cost 400% annual interest. In addition, large finance charges of 15-30% of loan amount can drive annual interest rates up to an astounding 780%.[48] Since the average loan term is about two weeks, a borrower who just uses one payday loan will not experience a full year of compounding interest. With that said, families which rely on these loans for many paychecks are borrowing with consecutive payday loans, which would aggregate to nearly a full year of interest. This staunchly contrasts those who are involved with a traditional banking institution, who can simply apply for a credit card and receive the same amount of credit, but at interest rates between 15% and 22%. High interest rates such as those in payday loans are highly detrimental to wealth-building among low-income communities. Mortgages also have a tendency to be exclusionary for similar reasons as well as the large down payment required on most home loans.

Herndon and Paul (2020) define financial exclusion as those that are unbanked or underbanked. Unbanked households are those that simply lack access to any type of bank account or traditional financial services. Underbanked households are those that have access to a bank account but still depend on high cost transactional services and credit services such as the previously discussed payday loans. [49] Generally speaking, if individuals do not have a means of accessing financial services over time, or if there are very few lenders that are guided by capable and inclusive internal management systems and providing affordable services, they could be considered financially excluded.

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[48] "How Payday Loans Work," *Payday Loan Information for Consumers* (blog), accessed November 21, 2021, https://paydayloaninfo.org/how-payday-loans-work/.

[49] Herndon and Paul, "A Public Banking Option as a Mode of Regulation for Household Financial Services in the US."

For unbanked or underbanked households, the reality of saving enough for a down payment, or even getting a loan is very grim. Within the current financial system, owning property is all but impossible without the use of a bank. Given the large term, amount and down payment of mortgages, they tend to be out of reach for many families, especially those which have been historically underserved in finance. Financial institutions are almost always necessary for any kind of large debt arrangement, excluding of course, the alternative financial solutions mentioned earlier. Unless one was to purchase a house in cash, which is unrealistic for a plethora of reasons, they would be unable to buy that house without the services which financial institutions provide. With this in mind, if 47% of Black households are unbanked or underbanked[50], then that 47% is, generally speaking, excluded from most mainstream financial services, including savings accounts, credit cards, and mortgages, most of which are crucial to owning a home. For those low-income families which do have access to basic financial services, they often face egregious fee structures from their banks, such as stacking overdraft fees, debit card swipe fees and withdrawal fees which can get quite costly, especially for those on a budget.[51] This is usually due to the relatively small balance and deposits of low income households, which does not incentivize banks to provide them with quality, affordable financial solutions. Across major private banks in America, 25 to 40% of checking accounts are not profitable, so banks try to recoup that profit through predatory fee structures for low-balance accounts.[52] Low income households, generally, receive quite limited utility from existing banking

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[50] Herndon and Paul.

[51] Vassilisa Rubstova, "Banking and Poverty: Why the Poor Turn to Alternative Financial Services," *Berkeley Economic Review* (blog), accessed December 5, 2021, https://econreview.berkeley.edu/banking-and-poverty-why-the-poor-turn-to-alternative-financial-services/.

[52] Herndon and Paul, "A Public Banking Option as a Mode of Regulation for Household Financial Services in the US."

options. The key takeaway here is that, whether banked or underbanked, low-income Black families do not have access to the viable, affordable financial services. It's also worth noting that discrimination is also often involved in the quality and cost of financial services. Yes, private banks are concerned with profit maximization, but some forms of discrimination which do not maximize profit still persist when racial biases enter the decision making process.

The only option most people have when financing a home right now is through a privately owned bank, which poses several problems. Private banks operate for the same reason as any other private business operates, to make profit. While it could be argued that this inherently does not pose any problems, upon closer inspection it's easy to see why profitability in finance is somewhat problematic. Since private banks are profit-driven, they're not interested in ensuring that every family can own a home, rather, they're interested in lending to those families from which they can make as much money, with as little risk as possible. Because of the United States' history of undeserving Black people in finance, the 'better' borrowers in the eyes of the bank are usually wealthier, white families.

Banks will usually perform a credit analysis on potential borrowers when issuing loans to determine their credit worthiness, so people or families with little to no credit history will either get denied for a loan or, occasionally, they will get approved, but with unrealistic terms in an effort to reduce the issuer's risk while also making the loan less accessible. Additionally, people without extensive credit history have credit scores that are more sensitive to change than someone who has had good credit for the majority of their life. To contextualize, if someone misses a payment on their very first credit card, that mistake is likely to drive their credit score down significantly. Meanwhile, a similar missed payment from someone who has extensive credit history may only see their score drop by a couple of points.

This goes to show how our current banking system does not encourage personal financial growth unless it is profitable for the banks. Dymski (2006) describes that private banks have steadily begun catering to 'uparket' depositors and either shedding lower-income customers and segmenting their customer markets by charging high marginal rates.[53] It helps keep the wealthy rich, but does very little to help impoverished communities achieve basic financial literacy and stability. Instead of ensuring that everyone has relative financial stability, banks currently seek to help only those which they can profit from. Given the importance of money in a capitalistic society, it seems natural that everyone residing in that society should have access to basic services to help them manage their money. Aside from the issues that Black communities face discussed in Chapter 1, Black communities are perpetually barred from housing markets because of a lack of accessible banking for those communities

Defining a Public Banking Option

While the U.S. has, on several occasions, attempted to implement various models of public finance, there are virtually no large-scale, public options for banking. There are three public banks operating in America today which have seen success, but only on a state scale or smaller. Meanwhile, there are a number of other countries with powerful public banking institutions that have been quite successful. This leads us to a question, however. What could a public bank look like in America?

The key feature that defines public banks is just that; they are public institutions which are community-driven. This means that public banks' interest and profit is owned by the public and returned back to the public. These institutions are naturally driven by public interest, so any

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[53] Dymski, "Discrimination in the Credit and Housing Markets: Findings and Challenges."

profits that the bank makes from the credit it issues gets reinvested into public projects, relief aid, and other infrastructure to help financially fortify low-income neighborhoods. In the case of private banks, profit generally goes into the pockets of their shareholders and executives. This poses a stark contrast to a public banking option, which instead redistributes profit among the community that it serves. The redistribution of funds throughout a community, however, isn't strictly facilitated by public projects and relief aid. Lending to individuals or households which would typically be considered high-risk borrowers is another method in which public banks could address wealth redistribution. In conjunction with the other forms of investment into a community, public banks will be an effective tool to begin redistributing funds more equitably.

Furthermore, without the constraint of profitability faced by private institutions, public banks are able to provide access to affordable banking services and credit to those who otherwise would not be able to engage with such services. Public banks can offer services and fund projects that have public benefit greater than the monetary cost to the bank, even if that benefit is not financial in nature. This will allow public banks to promote financial security through affordable financial services. In terms of consumer finance, public banks could offer mortgages, student loans and credit cards while also providing small business loans to promote financial growth in developing communities. This is, essentially, investing in communities across the country and redistributing wealth to help narrow the wealth gap along historically drawn racial lines in United States neighborhoods. The idea of public interest is central to public banks, so it makes sense that they would invest in public projects such as renewable energy, affordable housing and infrastructure projects, all of which can make significant quality of life improvements in a given neighborhood or community.

Herndon and Paul (2020) propose a more specific model of a public banking option for their analysis. They definitively define a public option as "the government using the direct provision of services to households and intermediaries as a tool to regulate in the public interest."[54] In other words, by providing services directly to the public without the involvement of a private institution, the government would be able to regulate household financial services in conjunction with public interests. The key mechanism at play here is that imposing regulation on private banks in order to redistribute wealth is not as effective as the government directly redistributing wealth through public banks. In other words, rather than telling private banks what to do, the government can just do what they need to directly through public banks. without the use of a middleman (i.e. private institutions). As the name of their paper implies, they consider the viability of public banking as a mode of regulation for household financial services. In their model, a public banking option would primarily provide two services. First, public banks would directly provide households with universal access to consumer credit and other basic financial services such as checking and savings accounts and financial advising. The second responsibility of public banks would be managing an online marketplace where public and private financial services would compete against each other. [55]

These services would serve as a mode of regulating household financial markets as well as shielding households from financial risk that disproportionately affects lower income households. A public option would be able to structure loans that decentralize risk away from consumers since banks that are publicly funded are capable of absorbing risk and financial loss. This cannot be said about private banks which either cannot or choose not to engage with loans

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[54] Herndon and Paul, "A Public Banking Option as a Mode of Regulation for Household Financial Services in the US."

[55] Herndon and Paul.

that centralize risk on themselves. In some cases this is justified, since private banks are able to go bankrupt, which public public banks could not do due to the origin of their capital.The government is much more capable of absorbing risk and loss than a private institution, so they're able to engage with more risky lines of credit or loans. History has shown that household financial markets need some type of regulation mechanism, with loans like bullet mortgages dominating the early 1900's. These mortgages concentrated risk on the borrower which discouraged and prevented families from buying homes. Bullet mortgages were typically short loans (3-5 years) and were not fully amortizing, meaning borrowers had to pay off the full balance by the end of the term, often resulting in a large 'bullet' payment at the end, which gave the loans their namesake and was very risky for homeowners.[56] When we compare these to mortgages today, which range from 20-50 years with relatively low risk put on the borrower, we can see how regulation has reduced consumer risk and therefore made mortgages more accessible. This is not to say that today's home finance solutions are perfect, they obviously aren't, but they have made significant progress from solutions of the past.

Herndon and Paul also reference New Deal financial reforms as a successful attempt at using a public banking option in the United States. New Deal reforms were aimed at providing access to financial services in all communities through increasing the amount of financial intermediaries. The government essentially used restrictions in bank charters to reshape depository institutions into public utilities which could provide stable, affordable credit to their communities. These restrictions included:

> "restrictions on lines of business, branching, types of assets that could be held and in what amounts, lending beyond a specified distance from the institution, the

[56] Herndon and Paul.

amount of loan that could be lent to a single entity, and prohibited adjustable rate lending."[57]

While seemingly extreme, Herndon and Paul argue that the charter restrictions imposed on depository institutions could be considered universal service requirements, which is a standard practice in infrastructure regulation. As is the case with other public services, it is often not profitable to serve low-income areas, so universal service requirements ensure that a public service is able to effectively serve the community in which it is located. In the case of financial services, the charters imposed by the U.S. government attempted to ensure that financial solutions were accessible to all communities. It's worth noting that "all communities" isn't actually representative of every community because the New Deal was passed in the mid-1930s, when racial violence and discrimination were still quite prevelent in many parts of the country. In reality, "all *white* communities" is a more accurate representation of the impact of New Deal reforms.

Considering the lack of affordable financial services for low income communities in the 21st century and the generational impacts that has had on low-income households, it's almost without question that financial services are essential services in the same way the Postal Service is. The USPS serves low income communities, even though it may not be profitable and a public bank should operate in the same way. While the reforms of the New Deal era have since been dismantled, they do provide clear, valuable insight into what a public banking option for the 21st century could look like.

Since it is clear that the Postal Service is a proven model of a public service, a more developed model for a public banking option is to integrate public banks into Post Offices. The United States Postal Service is one of relatively few universal services in the United States and is

[57] Herndon and Paul.

often referred to as a relatively successful model. It has been able to provide nearly uninterrupted, universal postal service for well over 200 years, with very few notable postal crises. Originally founded as a private institution in 1771, but when faced with stiff competition in the early 19th century, the Postal Service became a public service in 1845.[58] One of the factors that has defined its success since then is that it is, in most cases, universal. The Postal Service continues to deliver to unprofitable areas because as a public service, it's obligated to serve all communities.

This success that the Postal Service has achieved serves to highlight a major problem in the U.S. financial system. If it is not profitable or if it is overly risky to provide financial services in a certain low-income area, there is no incentive for private banks to serve that area. This leaves many low-income communities without any financial services and without those services, it's very difficult to build wealth. A public bank, however, does not face as severe of a profit or revenue constraint. In fact, it doesn't even need to break even and is therefore able to serve the 'unprofitable' communities which need their services the most. Since the postal service operates in every neighborhood in America, regardless of profitability, it is logical that this is a point in the system where public banks could be implemented relatively easily and financial inclusion could be facilitated more effectively, especially in places where post offices aren't operating at full capacity. Partnering with the Postal Service would provide public banks with much of the infrastructure required to provide universal service.

d'Alcatara and Gautier (2013) show that a postal banking model can be a vehicle for financial inclusion and can be, generally speaking, done profitably. They argue that "post offices

[58] Smithsonian Magazine and Winifred Gallagher, "A Brief History of the United States Postal Service," Smithsonian Magazine, accessed November 23, 2021, https://www.smithsonianmag.com/smithsonian-institution/brief-history-united-states-postal-service-180975627/.

are well placed to cheaply deliver financial services to financially excluded citizens".[59] Geographically, post offices are strategically designed and placed to provide postal services to all residents of a given city which, in turn, would make postal banks geographically accessible to the same group of residents. Post Offices which aren't operating at full capacity often have spare building space, which would be replaced with technological tools and resources to offer financial services. In a postal service/bank partnership (i.e. a postal bank), the post office is able to collect extra revenue to help reduce the financial restrictions of accessibility. [60] In other words, the postal bank is able to create affordable financial solutions because the post office can help financially cover the financial restrictions of accessibility. The authors do note, however, that a postal bank may not be a lasting solution to financial exclusion. Postal market competition and technological advances such as email and text platforms have dramatically enhanced competition in postal markets, potentially leading to a decline in the viability of a postal bank.

Public Banking in 21st Century America: Occasio-Cortez and Tlaib's Public Banking Act

While there are several small public banks in the United States, such as the Bank of North Dakota, there is no large-scale legislation which supports a system of public banks. In October of 2020, Congresswomen Rashida Tlaib and Alexandria Ocasio-Cortez introduced the Public Banking Act (H.R. 8721), which according to Congresswomen Tlaib's October 30, 2020 press release:

> "Allows for the creation of state and locally administered public banks by establishing the Public Bank Grant program administered by the Secretary of the

[59] d'Alcantara and Gautier, "The Postal Sector as a Vector of Financial Inclusion."
[60] d'Alcantara and Gautier.

> Treasury and the Federal Reserve Board which would provide grants for the formation, chartering and capitalization of public banks. It also codifies that public banks may be members of the Federal Reserve."[61]

Occasio-Cortez and Tlaib were motivated to introduce this bill because they believe the government should provide an alternative to Wall Street Banking by creating a financial system that works for lower-income families. The bill, in totality, would essentially pave the way for the formation of public banks across the country. More specifically, it allows the Secretary of the Treasury and the Federal Reserve Board to support public bank's formation, capitalization, financial market infrastructure development, supporter operations, and unexpected losses through public bank grants.[62] Because of public banks' robust government support, they will be able to effectively serve underbanked communities without the risk faced by private banks. The Public Banking Act essentially uses public banks as a method of directing capital towards neighborhoods traditionally underserved by private finance.

The Public Banking Act would enable the Federal Reserve to charter and grant membership to public banks, as well as working with other required institutions to establish a regulatory scheme for those banks. A regulatory scheme for an American public bank would be composed of guidelines to ensure that banks are equitably serving their communities and working towards a long-term decline in inequality. The bill also created a public banking incubator program, which provides member banks with the resources and technical assistance to "develop technologies, practices, and data that promote public welfare."[63] The incubator program

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[61] "Tlaib, Ocasio-Cortez Introduce Legislation Enabling Creation of Public Banks," Representative Rashida Tlaib, October 30, 2020, https://tlaib.house.gov/tlaib-aoc-public-banking-act.

[62] "Tlaib, Ocasio-Cortez Introduce Legislation Enabling Creation of Public Banks."

[63] "Tlaib, Ocasio-Cortez Introduce Legislation Enabling Creation of Public Banks."

would be of great use in creating more points of contact between financial institutions and low-income communities, strengthening the financial stability of those who live there. Additionally, the Federal Reserve will establish new liquidity and credit facilities, allowing it to provide direct federal support to local and state public banks.

Tlaib and Occasio-Cortez argue that the bill, in the short term, will be a fast and effective system to distribute relief funds in times of need. In the long term, they argue the bill will remedy systemic problems inside the U.S. banking system which historically have disproportionately impacted low-income, marginalized communities. Ultimately, through the creation of a public banking option, Tlaib and Occasio-Cortez seek to revolutionize the United States financial system into a model accessible for all. The Public Banking Act is uniquely positioned to address wealth inequality as well as systemic racism within the U.S. banking system. By creating an accessible banking model that serves all income levels and reinvests in the community through affordable credit and the creation of "a myriad of public goods" such as affordable housing and renewable energy projects, the Public Banking Act will be able to open doors for low income households to become homeowners. [64]

How does a Public Option Address Housing Inequality?

A public banking option does not directly address the specific issue of housing inequality. Rather, it addresses a part of the foundation of housing inequality which is underlying wealth inequality. By making access to credit more affordable and enabling households of all income levels to receive financial services, public banks would be able to facilitate low-income Black families to buy a home and begin building generation wealth and long-term stability. Public

[64] "Tlaib, Ocasio-Cortez Introduce Legislation Enabling Creation of Public Banks."

banks can promote community welfare and reduce wealth inequality by lending small business loans and reinvesting into local projects, which helps ensure that building wealth is more accessible. As was established in Chapter 1, wealth inequality is directly, negatively correlated with housing inequality. Changes in wealth inequality directly impact changes in housing inequality and vis-a-vis. As public banks contribute to the decline in wealth inequality, they will be indirectly affecting housing inequality as well.

Geoff gilbert (2019) articulates three primary failures of the current U.S. banking system: “1) it works to concentrate society’s wealth; 2) it is two tiered , wherein poor and working class people, who are disproportionately people of color, do not have access or only have access on relatively expensive terms; 3) is inherently unstable”.[65] Public banks, rationally, are well positioned to address these concerns and there are a number of mechanisms which position public banks to effectively address wealth inequality and therefore housing inequality. Most broadly, the mechanism which regulates the public banks (i.e. a regulatory scheme) allows the government to regulate public banks to ensure that they are working towards non-profit-driven, community-based goals. An example of this type of regulation is salary caps on public bank staff, unlike private sector executives, who make more than their employees by several magnitudes. Regulation such as this ensures that public banks are redistributing as many funds as possible. As is the case with many other universal public services, public banks will not always be profitable, so a regulation mechanism will ensure that public banks remain sturdy financial institutions which are able to serve their communities, even in the face of monetary loss.

Public banks create avenues of wealth building by making checking accounts, savings accounts, and credit accessible to underbanked Black communities. These types of basic

[65] Geoff Gilbert, “Who Plans Our Political Economy? A Solidarity Economy Vision for Democratic Political Economy Planning,” *Harvard Unbound* 12, no. 101 (2019): 101–57.

financial services are absolutely crucial to wealth building and home purchasing, so when these services become accessible via public banks, many Black families will have the tools necessary to purchase a home and begin to build household wealth. In order to facilitate financial inclusion with these accounts, they should be provided at no cost to their holders. Income from lending services should sufficiently cover the operating expenses of these basic services.[66] Those who don't have access to these services are not even able to engage with the most basic form of wealth-building: formally saving a portion of one's income. While shoving cash under a mattress is *technically* considered savings, formally owning a compounding savings account and depositing into it regularly is a simple, yet efficient method of building wealth. Saving is the first step towards building enough capital to make a large purchase or apply for financing. Those who do not have savings accounts are not able to engage with this step, and therefore cannot work towards making a large purchase, such as a home.

The logical next step in wealth-building is building a robust credit portfolio, which public banks can also facilitate for low-income individuals. A public banking option would include a full range of 'plain-vanilla' consumer finance options, which include loans such as mortgages and auto loans. These loans would include transparent policy without the predatory fine text and affordable terms that shield borrowers from risk.[67] If lenders view Black borrowers as riskier in terms of loan default, a credit or mortgage relief fund though a public banking option would reduce the risk of nonpayment on many loans in Black communities. For instance, if a Black family experiences large, unforeseen medical bills due to a lack of affordable healthcare in the United States, they may be unable to meet their financial obligations in terms of loan repayment.

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[66] Herndon and Paul, "A Public Banking Option as a Mode of Regulation for Household Financial Services in the US."

[67] Herndon and Paul.

A credit relief fund created through public banks would enable that family to flexibly meet their obligations and get back on budget. This fund enables Black families to more easily purchase homes because public banks are able to issue loans that private banks would consider to be too risky, since a credit relief fund would reduce the risk of default. Private banks are unwilling to take on a certain amount of risk, so 'risky' families are excluded from financial lending. Because public banks can reduce the risk of loan default, they are able to serve risky families better than the private sector. Additionally, once a borrower successfully pays back one of these 'plain vanilla' loans, they will have access to a small, revolving line of credit which would further enhance their financial security.[68]

In terms of mechanisms which don't directly impact individual households, but rather communities more broadly and all of their residents, public bank 'profits' can be redistributed throughout the community through infrastructure investments and public projects. Through investments in sustainable energy and other public projects, neighborhood values rise, but not in the same way that gentrification increases value. Gentrification has historically displaced low-income Black families due to large rent and cost of living increases, whereas public banks would be increasing community value, which makes communities more valuable for their sustainability, accessibility, aesthetics and safety. Underbanked communities typically receive little to no financial support from the private or public sectors, so public banks would be an efficient way to direct capital towards underbanked, Black communities. Generally when we look at Black versus white communities, we see that white communities receive more government support in the form of policing, sustainable energy, and infrastructure, all of which increase quality of life in a given neighborhood. This, however, is not a fast process, and the infrastructure improvements facilitated by public banks will not be possible immediately. Rather,

[68] Herndon and Paul.

it's an ongoing process that has long term impacts, whereas the accessibility of financial services has an immediate impact on underbanked, Black communities by allowing them to start generating wealth immediately.

Generating wealth is futile, however, if households are not resilient to economic shocks and crises such as the 2008 Financial Crisis or the COVID-19 pandemic. As previously mentioned, public banks provide an efficient method of distributing relief funds in times of crisis, shielding residents from disasters and crises, which tend to disproportionately affect Black families. According to an analysis of the U.S. Census Bureau's Household Pulse Survey (HPS) found that during the COVID-19 pandemic, Black households in which someone had lost employment were more likely to report housing insecurity than White households in a similar situation.[69] In other words, pandemic related job loss disproportionately affected Black households housing security. This analysis also established that Black families were more likely to take on debt to cover household-related costs than white families.[70] This is notable because Black families' increased pandemic debt has the potential to increase the likelihood of housing insecurity in the future because of increased stress that debt would put on their household finances.

Because relief funds in times of need will be able to be distributed more easily through public banks, the impact of crises like COVID-19 will be lessened for low-income, Black communities, who suffered greatly from the pandemic. With more readily available capital and credit offered by public banks, in the face of a crisis, funds will be able to be distributed quickly

[69] U.S. Census Bureau, "COVID-19 Pandemic Hit Black Households Harder Than White Households, Even When Pre-Pandemic Socio-Economic Disparities Are Taken Into Account," Census.gov, accessed December 1, 2021, https://www.census.gov/library/stories/2021/07/how-pandemic-affected-black-and-white-households.html.

[70] U.S. Census Bureau.

and efficiently. In addition to the effectiveness of the delivery of relief funds, aid provided by state or local public banks will be stacked on top of federal aid, providing residents with a larger cushion from economic crises. In other words, recipients will get federally and locally administered aid, making them that much more resilient to financial shocks. Additionally, those who own a home or other financial securities are able to draw equity on those securities to recover faster from financial crises. People without these assets, however, do not have this ability and therefore suffer more from crises.

Aside from the services provided and projects funded by public banks, their presence in financial markets could change how private banks approach low-income communities. Public banks outclass private banks in several ways, so they will introduce competition into financial and credit markets which those markets have not seen before. Because of this new competition, private banks may be more incentivized to service low-income communities. As previously established, having more financial intermediaries in a given area is shown to promote financial inclusion, so the introduction of private banks in low-income areas may additionally increase accessibility. It's worth noting, however, that this could also have the opposite effect, with private banks incentivized to only serve wealthy individuals and public banks relegated to serving low-income communities. Either way, public banks will still provide low-income neighborhoods with affordable financial services.

The main, underlying motivation for a public banking option is to promote a solidarity economy, and to make space for everyone to participate in that economy.[71] A solidarity economy is a system that prioritizes social profit over monetary profit and would allow the banking system to be controlled by communities through proposals submitted by the users of the funds. Many

[71] Gilbert, "Who Plans Our Political Economy? A Solidarity Economy Vision for Democratic Political Economy Planning."

public banking institutions would therefore be controlled by those who have been historically marginalized.[72]

Housing inequality and insecurity cannot be thought of in isolation. Housing is directly correlated with wealth, so we can't think of public banks as suddenly enabling non-home owning families to buy houses. Rather, public banks promote home ownership by facilitating the ability to purchase a home. A public banking option addresses housing inequality indirectly such that it gives families financial tools for wealth-building and eventually home ownership.

Public Banking isn't the Entire Solution: Next Steps

The vicious, self-perpetuating cycle that connects housing and wealth inequality is not one that is easily broken. There are many economic, political and social mechanisms which enable this cycle to persist. A public banking option is an intervention that would help weaken this cycle, but would have very little impact on the context in which it occurs. Housing and wealth inequality are incredibly complex, interdisciplinary concerns, so it makes sense that their solutions would be equally complex. While public banks do economically address housing inequality, they do not address the broader social concerns involved, such as general racism, racial boundaries in United States cities, or ongoing racial conflict in neighborhoods in the U.S. today. Public banks are more so a tool to financially help those who have been historically underserved in finance, which is predominantly Black families. They are an effective tool in providing Black households with affordable financial services, but can do very little to address the systemic racism which perpetuates their financial inequality.

[72] Gilbert.

The grim reality of racial inequality in America is that the financial and political system encourages wealthy individuals to benefit from the structures of racial oppression. Unfortunately, if some people still benefit from the structures of oppression, they have no incentive to work to dismantle them.

Given that public banks are not an effective way to address the context in which housing inequality occurs, there are certain supplementary policies which could do more to address social concerns that public banks cannot. It goes without saying that reparations for descendents of enslaved Black Americans are a major step, both financially and socially, towards ending racial inequality. Geoff Gilbert (2019) puts it best when he states " People made vulnerable by current status quo institutions must be made materially whole through reparations before any new system can claim to be just and equitable".[73] Reparations can take many forms, but a few specific packages that would make a large impact are individual payment to descendants of enslaved Black Americans, college tuition payments for descendants of enslaved Black Americans, student loan forgiveness for descendants of enslaved Black Americans, and most importantly for the issue at hand, down payment grants and housing revitalization grants for descendants of enslaved Black Americans.[74] As gentrification occurs, as is the case in cities across the country, Black households are priced out of and displaced from neighborhoods that they helped establish and maintain.[75] Reparations in the form of housing grants would be highly effective in helping Black households keep up with the egregious home prices in the market today.[76] Ensuring that

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[73] Gilbert.

[74] Rashawn Ray and Perry M. Andre, "Why We Need Reparations for Black Americans," *Brookings* (blog), April 15, 2020, https://www.brookings.edu/policy2020/bigideas/why-we-need-reparations-for-black-americans/.

[75] Ray and Andre.

[76] A brief snapshot of housing prices can be found in Chapter 1.

Black households can afford to keep up in the market further weakens the structures which maintain housing inequality.

Thinking from a more social perspective, promoting awareness of the structures of systemic racism and how deeply ingrained they are in American history would allow for more open political conversations regarding dismantling those structures entirely. Contrary to what the contemporary political climate seems to suggest, the oppression of Black Americans is not a political debate, it is an ongoing struggle for Black people across the U.S.. The first step towards dismantling these structures of oppression is understanding them. Widespread public education of how oppression persists, such as teaching Critical Race Theory in schools, will help the public understand and combat racism. Racism and racial injustice tend to be hidden from public consciousness until a major racial conflict begins the conversation once again. This issue shouldn’t be stratified by a string of racial injustices, it should be an ongoing process of education and steps toward lasting change in the systems that perpetuate racism.

Conclusion

There should be no question in our minds that housing inequality is not an independent phenomena. In actuality, the causes and implications of housing inequality extend far past the boundaries of the housing market. Using existing literature, this paper examines these broader economic roots and uses the resulting context to formulate a public banking option as an economic tool to dismantle the structures of inequality. Public banks are oriented in such a way that they are able to successfully transform the United States financial system into a universal public service.

A public banking option is positioned as well as it is because it addresses the larger underlying mechanism which creates housing disparities: wealth inequality. By redistributing wealth via accessible financial services, public projects, and timely relief aid in times of crisis, public banks can steadily chip away at the structures which enable inequality. For low-income Black families, one of the main barriers that prevents them from building wealth is having access to avenues to do so. Public banks, as a universal public service, will be able to provide these families with the tools necessary to accumulate wealth. Public banks indirectly reduce housing inequality by giving families the same opportunities to generate income and wealth that white families have. They are also able to help households build resilience to financial shock, which tend to disproportionately affect Black families. Aside from this resiliency, public banks can provide additional local relief aid much more quickly than it is possible now through Federal channels.

In terms of future research and next steps, there is still a significant amount of work to be done in order to comprehensively understand housing and wealth inequality as well as the intervention of public banks in that relationship. One of the most crucial steps in regards to future research is an empirical analysis examining the cycle of inequality. While we can hypothesize a number of things regarding inequality such as questions like will an increased number of financial intermediaries decrease the amount of underbanked residents in a certain area, it is hard for us to know if this is the case in the real world and if outcomes will be as we expect without statistically significant evidence of such.

Outside of academics, politics and economics, what steps can Americans take on a community or individual level to fight inequality? While this is completely up for debate, educating oneself on America's violently racist history and the systems of oppression set in place for Black individuals is an effective way for the public to contribute to ending inequality. As trite as it may sound, understanding a problem is always the first step to solving it. If the structures of oppression are more widely understood, then the American public is more well-positioned to begin combating racial inequality. As mentioned in regards to Michael Reich's (1978) model of discrimination, the collective power of a workforce is diminished by weakened solidarity[77], and the public at large is no different. If there was a larger force of people who understood the systems of inequality, they would be more well equipped to address it. A collective voice is always heard more clearly than individual ones. It's worth playing devil's advocate here though. If capitalists are educated on the structures of oppression and discrimination is still prevalent in the economy, they will be able to more easily exploit people of color and the structures that oppress them.

Academics and politicians alike need to stop addressing different forms or structures of inequality as separate issues. Policymakers and economists have a tendency to look at individual forms of inequality through a telescope. In other words, they tend to think of wealth, income and housing inequality independently while not addressing the structures that bind them all together.

[77] Reich, "Who Benefits from Racism?"

Moving forward, we need to zoom out and examine what binds it all together. While this paper examines a few mechanisms which enable inequality, there are many, many more that were not addressed. Understanding the connections and basic mechanisms which connect different types of inequality is essential to understanding and combating broader racial inequality.

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