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Commentary

Title:

"The Economist's Approach to Thinking about Discrimination (and Other Issues)"

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The analysis of discrimination that I have presented in previous Commentary articles reveals a way of thinking unique to economics. In those articles I argued against the prevailing view that the wage differentials that we see between white males and women or minorities is primarily due to discrimination.[1] Obviously, there are many who take the opposite view. Using economic analysis we can more readily see the foundational flaw in thinking that leads many to reach untenable conclusions on matters dealing with discrimination.

Economic analysis makes one particular fundamental assumption about human behavior that sets it apart from Marxian influenced analysis prevalent in most of other social sciences and humanities. An economist starts with the assumption of Methodological Individualism, which states that individuals are the fundamental building block of the analysis of social action. All social actions, good or bad, are the results of people thinking and acting as individuals. This is not to say that the end result of all these individual actions will aggregate to what any particular individual desires. In a complex society of many people, millions of individual actions will often be in conflict, so the end result will not be what is most desired by any particular person. Social states, therefore, will be the "result of individual human action, but not of human design."[2]

In contrast, a non-economist will usually assume that groups are the basic building blocks of society and, therefore, the appropriate unit of analysis of social action. Influenced by Karl Marx (who claimed that the primary struggle in society was based on the conflict between the bourgeoisie and the proletariat), they see social conflict as propelled by the actions of groups, not individuals.[3] Under this model, people act as part of a class – rich/poor, white/black, Hindu/Muslim. Of course, the possible number of groupings is limited only by the imagination of the analyst. For instance, analysts who study young people in high school can break the student body down into goths, geeks, jocks, and others. People who study voting patterns break the population down into Boomers, Millennials, and others along generational lines, or between urban, suburban, and rural. Feminists will analyze a wage differential between men and women as the result of the conflict of two large blocks based upon gender. Any large group of people can be broken down into different blocks, especially if the groups are seemingly antagonistic in some way due to conflicting interests.

The problem with this kind of analysis is that it does not take into account that, while many people support the overall goals of their group or class, as individuals they also may have an interest separate from, and in conflict with, their own group. This is most easily seen in the behavior of cartels, which are organizations of producers that conspire to reduce the total output of their good in order to raise the market price and reap a share of monopoly profits. Once we understand the logic of individual cartel member behavior, we can draw a direct line to how firms behave when they enter the labor market to hire workers. For the rest of this paper we will use "cartel" to refer to any form of group conspiracy to monopolize a market where the goal is to extract unearned profit, whether a business combination, a racist sports league, a discriminatory hiring system, etc.

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[1] Minorities is something of a misnomer in wage differentials analysis. Both South Asians, East Asians, and Jews earn more than whites on average. When people talk about low minority wages they are primarily referring to a subset of minorities including African Americans, Southeast Asians, or Hispanics.

[2] For an in-depth exploration of how social outcomes are the result of spontaneous individual action, see: Law, Legislation, and Liberty, by Friedrich Hayek, University of Chicago Press, 1973, 1976

[3] The bourgeoisie are the property owning business class, also known as capitalists. The proletariat are the working class, who do not own capital (i.e., the means of production).

While most of us can readily see why a group of producers would want to conspire to charge a monopoly price, economic analysis helps us see that there is more going on than simple group interest. While the group as a whole can clearly benefit from a successful conspiracy to raise prices, any individual firm within the group can do even better (make a larger profit) if they alone defect from the group, lowering their own price below the cartel's price, and thereby increasing their individual quantity sold.[4] Once an individual firm breaks rank with the others, it is very difficult for the cartel to maintain the discipline necessary to maintain the monopoly price. This is due to the fact that the defecting firm will start to take away the customers of those firms sticking to the cartel price. If this continues, the remaining cartel members risk losing enough customers that their profits will actually be lower than if they abandon the high cartel price and start competing with the defector to win back customers.[5] Thus, a cartel member's individual interest undermines the group's interest. In order for the group to overcome this desire on the part of every individual within it to defect, it must have some kind of enforcement mechanism to maintain group cohesion.

A classic example of the collapse of group cohesion is explored in a Commentary article which I co-authored on the voluntary racial integration of professional sports.[6] In that paper we described how segregated, all-white teams voluntarily integrated during the 1940's and 1950's, long before it was required by law.[7] Clearly, the group (or cartel) interest of the white players and owners was to maintain the color barrier so that they would not have to accept and compete against black players. All it took was for one team, acting in its own self-interest, to break that barrier to bring the entire edifice of segregated sports to its knees. This is due to the fact that any individual team can increase its winning percentage if it accepts quality black players when the other teams do not. Once black players started helping their team win more games than the teams that remained all white, the ability of the all-white teams to remain so became untenable. It turned out that most white players, team owners, and fans would rather win with black players than lose without them.

Once you have internalized this kind of analysis, you realize that most theories of discrimination or oppression by one group over another are badly flawed. Economic analysis does not claim that group oppression of others is impossible, only that it requires an enforcement mechanism to restrain the defectors who pursue their own individual self-interest at the expense of their group's interest. Without this enforcement mechanism, the group strategy will fall apart.

This analysis makes the claim that a group strategy of paying white males more than equally qualified women or minorities will fail of its own accord, even *without* anti-discrimination laws. Any individual firm will find itself in the same position as that of the all-white professional sports teams mentioned earlier. Even if all firms are sexist and racist, and would therefore prefer to have a workplace consisting of only white males, this situation would be self-liquidating in the face of defector firms. Defector firms are those firms who cheat on the "agreement" (explicit or implicit) to hire only white males for a position. Initial defectors will be those firms that are less sexist/racist than their rivals, so that they choose to defect in order to get the large profit available

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[4] For a fuller treatment of the analysis of cartels see any standard introductory economics textbook, such as N. Gregory Mankiw, "Principles of Economics," Cengage, 8th edition.

[5] The recent dispute between Russia and Saudi Arabia, the lead country of the OPEC oil cartel, illustrates this analysis. See: https://foreignpolicy.com/2020/03/14/oil-price-war-russia-saudi-arabia-no-end-production/.

[6] "Competitive Markets Eliminate Discrimination: the Example of Professional Sports" by Burt Folsom and Michael Patrono (https://coles.kennesaw.edu/econopp/docs/August-2020-commentary.pdf).

[7] The Civil Rights Act of 1964 made discrimination in employment illegal whereas before that time it was not.

from hiring highly productive women or minorities (as we saw in the example of professional sports).[8]

The argument that individual self-interest will undermine any large-scale discrimination by one group against another relies on the absence of a "cartel" enforcement mechanism. True Free-Market Capitalism makes cartel enforcement impossible. When markets are truly free, any firm may enter or exit any industry, firms can negotiate with any worker they want, and firms and workers can agree to any wage they choose. There is no "official" wage for white males, females, or minority that is legally enforceable. The same is true of the prices that firms charge. Any attempt by any group to exploit others by paying women and minorities less than equally productive white males will collapse as other firms defect and profit from dealing with exploited workers until there is no difference between workers of equal productivity.

Economists who support Free-Markets see this as one of the tremendous benefits of Capitalism. Instead of having government second guess every hiring or pricing decision in the country, we can rely on the self-interest of market participants to break down discriminatory cartels on their own, or prevent them from forming in the first place. Discrimination can only flourish when government changes the rules to permit non-competitive behavior.[9]

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[8] For an examination of the scale of profits that can be accrued by defecting from a group see: "Why Competitive Markets Discourage Discrimination" by Michael Patrono (https://coles.kennesaw.edu/econopp/docs/February-2020-Commentary.pdf).

[9] For an excellent treatment of state sanctioned discrimination, see: C. Vann Woodward, "The Strange Career of Jim Crow," Oxford University Press, 1955, 1957, 1966, 1974.