RACIAL DISCRIMINATION: WHY WE SEE IT OR WHY WE DON'T

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Introduction

Racial discrimination is a polarizing topic. Experts argue about where, why, how, and to what extent it exists in any number of historical or contemporary situations. Despite the controversy, the fact remains that racial discrimination is the result of actions taken by individuals. Individuals choose whether or not to engage in racial discrimination the same way they choose whether or not to take any other action, by evaluating the expected costs and benefits as they are measured on their personal value scale and acting accordingly. If people possess no racial preference whatsoever, then a preference to discriminate will not even appear on their value scale. The purpose of this paper is to examine the extent to which and in what forms racial discrimination occurs under the prerequisite assumption that a preference to discriminate on the basis of race does exist. Economic agents will racially discriminate when they have a preference to do so and they perceive that the benefits of doing so outweigh the costs.

Many different types of costs and benefits of racial discrimination may exist within a person's mind. One benefit may be a type of psychic profit. If a person has a strong antipathy for a certain group, he may receive some kind of psychic benefit from discriminating against that group. A person may receive a social benefit from engaging in discrimination by protecting his own group against that of another. A third benefit could be that racial discrimination is one way to diminish search costs. In a world of scarcity, individuals do not have the time or resources available to always attain perfect information. At some point, search costs become inhibitive and people must act based on the information they currently possess. Because individuals typically possess more information about their own group, they may engage in racial discrimination to reduce the search costs that would be necessary to properly evaluate members of another group. Costs of racially discriminatory behavior may include social costs, such as if one is ostracized from society for being racist. If racial discrimination is illegal, one might face legal costs such as court or jail time for violating the law. Most relevant to economics are the monetary costs associated with racial discrimination which will be discussed at length later.

Under different types of institutional structures, different costs and benefits are at play. For example, in a free market all forms of racial discrimination are legal so legal costs of racial discrimination would not exist. In a market hampered by government intervention such that racial discrimination is illegal, legal costs could be quite prohibitive. This paper examines the costs associated with free market racial discrimination as well as how those costs are altered by government interventions. While many different types of interventions exist, those focused on in this paper are specific to housing markets and labor markets: namely, rent control, zoning, and redlining and minimum wage, unions, and occupational licensing. When these interventions are enacted, they change the incentive structures that economic actors face. Ultimately, the government alters institutions and imposes interventions that change the costs and thereby the prevalence of racial discrimination.

Important Definitions

In economics, institutions are the “rules of the game.” Douglass C. North defines institutions as “the humanly devised constraints that structure political, economic and social interaction” (North 1991, 97). He says institutions “determine transaction and production costs and hence the profitability and feasibility of engaging in economic activity" (North 1991, 97). Government interventions are the various laws, restrictions, and requirements that the government imposes on private individuals, entrepreneurs, and businesses in a hampered economy. Interventions change the institutions of an economy and can heavily influence the incentive structure that economic actors face. Since changes in institutions can drastically alter profit and loss incentives, government intervention affects the extent to which people engage in racial discrimination based on the costs and benefits associated therein.

It is important to define what is meant by racial discrimination and differentiate it from other terms such as racial prejudice or bias. Thomas Sowell differentiates between two types of bias: cognitive bias and favoritism. Under cognitive bias, a person may not intend to differentiate by racial attributes but may systematically undervalue certain groups due to cultural factors or circumstances. Favoritism is a preference for one's own group. Bias does not require an individual to believe that a certain group is inferior; yet, in each case the results of bias are that one group is consistently given preferential treatment over another (Sowell 214, 2009). Beverly Tatum defines prejudice as "a preconceived judgment or opinion, usually based on limited information" (Tatum 2017, 85). Oftentimes, people form prejudices unconsciously due to social and cultural factors that are absorbed over time. While prejudice itself is an opinion and not an action, it is often translated into prejudiced acts such as racial discrimination (Sowell 2009, 215).

Walter E. Williams writes that "Racial discrimination is an act of choice whereby racial attributes provide the criteria for choice" (Williams 1982, 24). Defining racial discrimination as "discrimination on the basis of race" is circular and unhelpful without first characterizing what race is. Defining "race" is a difficult task due to the large historical, scientific, and sociological debate surrounding the topic. Brendan O'Flaherty defines race by saying that "Races are labels that come from history. Races create a partition of people based (to a great extent) on ancestry, with some genetic correlations, and that partition affects how people think about themselves and how others think about them" (2015, 45). Races are groups that historically people ascribe themselves and others to based on factors such as cultural heritage, physical characteristics, and geographic location. These factors still hold great weight today in regards to the beliefs that people hold about one another and how those beliefs inform interactions.

Effects of Racial Discrimination

Racial discrimination affects different people to various degrees depending on the type of and extent of the discrimination. Obviously, in any case of discrimination, the person being discriminated against is economically impaired. If he is not hired for a position, if someone will not trade with him, or if someone will not offer him a loan, he is worse off, regardless of whether or not the discrimination is a result of racist prejudices. He is worse off because he is unable to engage in an exchange that he would otherwise prefer to engage in. He therefore does not receive the benefit from that exchange and is disadvantaged relative to the person who was chosen instead of him who does get to engage in the exchange.

In the case where, due to racial preferences, discrimination is pervasive to the point where no exchange is made at all, it is not only the person discriminated against who is worse off, but also everyone involved in the situation and ultimately society as a whole. Society benefits when the members of society benefit. When people refuse to engage in mutually beneficial exchange due to racial discrimination, the benefits of an exchange that otherwise would have taken place are lost. Mises discusses this idea in *Omnipotent Government* when he writes, “Autarky in one country may lower the standard of living in every other country. If a nation says: ‘Let us alone; we do not want to interfere with your affairs, and we will not permit you to mind our business,’ it may wrong every other people” (Mises 1994, 279). Refusal to engage in exchange harms everyone because voluntary exchange is mutually beneficial. Less exchange results in less benefit for society.

Racial discrimination can also disadvantage the very person who is doing the discriminating. Discrimination based on anything other than economic efficiency has an economic cost. Milton Friedman writes that “A businessman or an entrepreneur who expresses preferences in his business activities that are not related to productive efficiency is at a disadvantage compared to other individuals who do not. Such an individual is in effect imposing higher costs on himself than are other individuals who do not have such preferences.” (Friedman 2002, 109-110). For example, we could construct a thought experiment in which it is the case that an employer has the option of hiring one of two different employees. Both are willing to work for the same wage. However, one employee is slightly more productive than the other but from a racial group that the employer does not prefer. If the employer chooses to hire the less productive employee based on his being from the employer’s preferred racial group, then the employer has imposed the cost on himself of having a less productive worker than he otherwise could have had. In the case where the employer’s competitor does not have the same racist preferences and hires the more productive worker, he would be at an advantage economically since his business would enjoy greater economic productivity for the same cost. The employer with racist preferences must deal with lower productivity despite having to pay the same cost. This price paid for racial discrimination may be called "the racist premium" (Moran 2018).

The Racist Premium

The economic cost of racial discrimination is whatever monetary amount an individual must give up in order to discriminate on the basis of race rather than on economic efficiency or other relevant criteria. In a free market, some people may be willing to pay the racist premium and give up financial profit for psychic profit in the form of whatever satisfaction they receive by engaging in racial discrimination. At the same time, people without such racist preferences are free to take advantage of the economic profit opportunity provided to them by people willing to pay the racist premium.

A notable historical example of this economic principle in action can be found in a New *York Times* article from August 18th, 1900. Entitled "Negro Finds Way to Wealth," this article chronicles the story of J.D. Bowser, a successful African American school principal living in Kansas City who was accused of "systematically buying houses in aristocratic neighborhoods and moving into them in order that he might compel the white neighbors to buy him out at a profit to himself" (Negro 1900). Bowser was brought to court for buying houses in white neighborhoods, moving into them as a black man, and then refusing to sell the houses to the outraged neighbors except at "exorbitant profit." While the result of the lawsuit is not published in the article, *the Times* concludes by writing that "Bowser read a long paper in his own defense, standing on his right as a freeborn American citizen to live where he pleases and sell his property at whatever price he can find a purchaser willing to pay" (Negro 1900). J.D. Bowser provides an excellent example of how an enterprising individual in a free market can punish racial preferences through economic means.

In a free market, the racist premium provides some limit to the extent to which racial discrimination can prevail. The competitiveness of the market will contribute to determining the cost of discrimination and its effect on market participants. Milton Friedman discusses how in the case of a competitive free market, an entrepreneur who discriminates on the basis of anything other than economic efficiency may be forced to stop discriminating or close his doors. Friedman explains that "A businessman or an entrepreneur who expresses preferences in his business activities that are not related to productive efficiency is at a disadvantage compared to other individuals who do not. Such an individual is in effect imposing higher costs on himself than are other individuals who do not have such preferences. Hence, the free market will tend to drive him out" (Friedman 2002, 109-110). In a competitive environment, when a businessman chooses to engage in racial discrimination, the economic cost to his business can become inhibitive to his continued operation.

In emphasizing the economic power of the racist premium, one should not neglect to recognize that the cost of racial discrimination may not be enough to cause such discrimination to disappear entirely. As long as people are willing and able to pay the racist premium, they are free to continue engaging in discrimination if they determine, based on their own personal value judgments, that the benefits outweigh the costs. Daria Roithmayr notes that markets in the real world are rarely perfectly competitive and that "racial gaps might persist because people still have a taste for exclusion, and competitive forces can't drive out people's taste for discrimination for a number of reasons" (Roithmayr 2014, 16). An entrepreneur with racial preferences who makes enough income to cover both his operation costs and costs racial discrimination could continue to operate his business albeit at a lesser financial profit than he may otherwise enjoy.

When the government begins to hamper the market through institutional changes and regulations, the costs of racial discrimination begin to shift. Depending on the intervention, the racist premium may be raised or lowered. Because the degree to which discrimination can prevail depends upon the costs of doing so, governments can significantly alter how prevalent racial discrimination is within a society. Note that the amount of racial discrimination that occurs does not depend upon the amount of bias, prejudice, or hatred that is present in a society but rather depends upon the price of acting on those opinions and feelings. The costs and benefits weighed in people's minds determine whether or not they will engage in racial discrimination.

One of the most basic economic principles, the Law of Demand, explains that only at lower prices will quantity demanded be higher, *ceteris paribus*. Therefore, if all else is held equal, then people will engage in more racial discrimination when the cost to them is lower and will engage in less racial discrimination when the cost to them is higher. If the government alters the institutional structure such that the cost of racial discrimination in a particular industry decreases, then one would expect to see more evidence of racial discrimination in that industry. The discussions of the labor and housing markets in the following sections of this paper examine the ways in which government intervention alters economic incentive structures and the resulting changes in racial discrimination that are observed.

Housing Markets

In a free market, people are free to engage in racial discrimination and face no consequences from the government for indulging their racial preferences. There are no laws requiring people to or preventing people from discriminating on the basis of race. This fact may cause some to become concerned that a free market would experience rampant racial discrimination as everyone works to protect their own group, generating hostility and a breakdown of society as the more powerful groups exploit the less powerful. What such concerns neglect to recognize is that people can only discriminate as far as the costs allow. All economic agents face a cost-benefit analysis when making decisions. Depending on the preferences and institutions in play, the costs of discrimination could be so low relative to the benefits that racial discrimination could and would run rampant. Alternatively, the costs of discrimination could be so high relative to the benefits that racial discrimination virtually disappears.

Free market conditions would allow racial discrimination to arise spontaneously in the form of housing segregation. Segregation could be the result of antipathy between groups but could also be caused by factors that have nothing to do with animosity. For example, neighborhoods might voluntarily segregate because efficiency is increased when inhabitants speak a common language and share a common culture. This fact is why we observe various cultural districts that develop within cities. In such cases, the benefits of homogeneity outweigh the costs.

When trying to combat segregation, governments often accuse and legislate sellers as the actors engaging in racial discrimination by refusing to supply housing to certain groups. This focus overlooks the ways in which buyers engage in racial discrimination when choosing where to live. Buyers may refuse to purchase housing in a neighborhood where the racial demographics do not match their preferences. An exchange requires both a buyer and a seller. Buyers' preferences and resulting self-selecting into certain neighborhoods contributes to patterns of segregation just as much as sellers' preferences. The patterns of segregation in a free market will reflect the preferences of the people living in those communities as they evaluate the costs and benefits of homogeneity or integration and act accordingly. The interest of this paper is to examine how government intervention alters the cost structure associated with racial discrimination from what it would otherwise be on a free market and changes the ways that preferences are expressed. Rent control, zoning laws, and red lining are three (of the many) ways that the government hampers the market and alters the prevalence of racial discrimination.

Rent Control

When governments enact rent control, they prevent landlords from charging above a certain price for housing. Rent is "controlled." When the legislated price is below the market clearing price, a shortage of housing develops as there are more people who demand to purchase housing at that price than there are sellers willing to supply it. The result is a surplus of housing applicants. In an unhampered market, a landlord can discriminate based on price and offer the housing to the most eager buyer who is identified by his or her willingness to pay the most for the housing. Under rent control, the landlord must choose between several different applicants who are all willing to pay him the same price which cannot be bid up by the most eager buyer. In this case, the landlord must discriminate on the basis of something other than willingness to pay. If the landlord holds a racial preference, he may choose to engage in racial discrimination since he no longer has any financial incentive to act otherwise. Under rent control, as Thomas Sowell describes, “such discrimination may cost the landlord nothing” (Sowell 2009, 223). The presence of effective rent control in a housing market decreases the cost of and therefore increases the likelihood of housing suppliers engaging in racial discrimination. Interestingly, this effect is often the exact opposite of what legislators intend when they implement rent control as a way to provide more affordable housing for disadvantaged groups.

Zoning

Zoning laws can be used directly or indirectly to alter racial discrimination in housing. Some zoning laws explicitly mandate where certain people can live. For example, in 1910, the city of Baltimore created a zoning law that prohibited African Americans from buying homes in majority white blocks of the city and prohibited Whites from buying homes in majority black blocks (Rothstein 2017, 44). Because the city was mostly integrated before this ordinance was enacted, they faced significant difficulty in applying the law. Richard Rothstein describes one case in Baltimore where “A white homeowner moved out while his house was being repaired but then couldn’t move back because the block was 51 percent black” (Rothstein 2017, 44). This kind of zoning law obviously requires absolute and complete racial discrimination in housing. Incentives are shifted so significantly that virtually everyone discriminates on the basis of race to avoid the legal sanctions which would follow if they tried to violate the law.

Other types of zoning laws such as those that specify residential, industrial, and toxic waste zones impact racial discrimination indirectly. After blatant racial zoning laws were prohibited by the U.S. federal government, officials could and did use other types of zones to segregate in ways that disproportionally discriminated against African American communities and created urban slums. Zones that are assigned as “residential” must follow certain zoning requirements such as how far back a house must sit back from the curb or how big its lot must be. Roithmayr discusses how these residential zoning requirements drive up the cost and therefore price of residential housing. For example, the increased prices of relatively more expensive single-family homes in the suburbs means that many poorer families (which due to various historical and economic factors usually means minority families) are unable to afford to purchase a house in a suburban neighborhood (Roithmayr 2014, 104). High economic costs discouraged minority families from moving into suburban homes. This phenomenon intensifies segregation and discrimination along racial lines as disadvantaged groups are locked into urban living.

Industrial and waste zoning have caused similar effects. A 1983 study by the U.S. General Accounting Office concluded that “across the nation, commercial waste treatment facilities or uncontrolled waste dumps were more likely to be found near African American than white residential areas” (Rothstein 2017, 54). Rothstein argues that historically the decision to place such industrial and waste zones near African American neighborhoods was motivated by white legislators who wished to avoid the deterioration of white neighborhoods. While they did not intend to intensify slum conditions near black neighborhoods, this was the result “when African American sites were available as alternatives” (Rothstein 2017, 55).

Government intervention in the form of zoning can directly or indirectly change incentives that affect racial discrimination. In either case, legislators can engage in racial discrimination because the costs they may bear are low while the benefits to their own communities are high. The real costs are borne by the disadvantaged members of the communities whose lives are injured by the zoning laws and who under a free market would choose to live elsewhere or would at least not be subjected to the residential, industrial, and waste zoning laws that cause these discriminatory results. In a free market, housing, industry, and waste would be placed wherever people's preferences as expressed through prices in the market system dictate that they should be, rather than in certain areas to the advantage of some and at the expense of others.

Redlining and Interest Rate Ceilings

A third type of government intervention that affects the housing market is redlining and interest rate caps which result in both direct and indirect racial discrimination, respectively. John T. Metzger defines redlining as "the refusal of financial institutions to make loans in specific geographic areas" (Metzger 2000, 7). Redlining emerged in the U.S. in the 1930s and was exacerbated by the Federal Housing Administration (FHA). In an act of clear racial discrimination, the FHA refused to insure home mortgages in African American or integrated neighborhoods because they were deemed "too risky" as the presence of African Americans was associated with falling property values (Rothstein 2017, 65). This discrimination persisted as late as the 1960s (Metzger 2000, 8). The U.S. National Commission on Urban Problems published a report in 1969 explaining the phenomenon as it occurred in the U.S. saying, "There was a tacit agreement among all groups—lending institutions, fire insurance companies, and FHA—to block off certain areas of cities within 'red lines' and not to loan or insure within them" (National Commission on Urban Problems 1969, 101). The parts of cities that were blocked off or “redlined” were usually majority African American neighborhoods. The result was discrimination in housing loans and insurance along racial lines as African Americans could not secure home loans or insurance like their white counterparts.

The government intervention that exacerbated the racial discrimination was not simply redlining itself but the regulations that changed how redlining impacted minorities. Statutes that placed ceilings on interest rates that lending institutions could charge for mortgage loans changed the incentives for banks, making it less likely that they would extend loans to riskier (usually minority) populations. As Williams describes, “Given these ceilings, banks have an incentive to ration credit, namely to lend money to those whose perceived credit worthiness is appropriate to the permitted legal interest rate” (Williams 1982, 30). When banks cannot extend a loan at an interest rate high enough to cover the risk they are taking on, they are disincentivized from investing in that market. Redlining and the interest rate caps associated with it created sections of cities that were not profitable to lend to or insure. Consequently, the result was discrimination based upon profitability which was correlated with race. Had interest rates been allowed to rise, mortgage loans may have been extended to riskier borrowers in the inner city. Historically, government intervention in the form of interest rate ceilings and redlining resulted in increased racial discrimination both directly and indirectly—directly when government agencies specifically refused to insure African Americans and indirectly when interest rate ceilings made extending credit to African American communities unprofitable.

Labor Markets

Free labor markets would operate very similarly to free housing markets. Since no laws exist to prevent them from indulging their racial preferences, employers in a free market are free to discriminate in hiring on the basis of race. Employees are also free to choose where they want to work although the conversation about racial discrimination generally focuses heavily on employers. The prevalence of racial discrimination will depend upon the costs and benefits as assessed by the economic agents involved. Employers can only discriminate on the basis of race in as far as the costs will allow them to while remaining competitive in the market. As Williams discusses, "The market would penalize the employer who chooses employees on market-irrelevant criteria" (Williams 1982, 42).

Interestingly, the free market will naturally tend to equalize wage rates between different groups (Williams 1982, 42). For example, suppose some employers hold racial preferences such that they engage in racial discrimination by refusing to hire workers of a certain race. Suppose also that in order to secure employment, workers of this less-preferred race are willing to work at a lower wage than those of other races. Under these conditions, enterprising employers who do not hold racial preferences could hire the workers who are willing to work for less and enjoy lower costs of production than employers who refuse to hire such workers because of racial preferences. The employers who do not engage in racial discrimination could then undercut the prices of the discriminatory employers and gain a larger share of the market. As larger profits are reaped by non-discriminatory firms, these profits may incentivize new market entrants who (in an effort to secure workers) will offer slightly higher wages to employees of the non-preferred racial group. In this way, wages of the non-preferred group are bid up until they equal those of all other workers.

In a hampered market, the government imposes interventions and regulations that alter this wage equalization mechanism and the costs of racial discrimination. Of the many ways that governments interfere with wages and labor markets, three are minimum wage laws, unions, and licensing requirements. These interventions alter the incentives that economic agents face and can change the costs of racial discrimination both directly and indirectly.

Minimum Wage

Minimum wage laws do not require any racially motivated action on the part of legislators to have drastic effects on the prevalence of racial discrimination in a society. When a minimum wage law is enacted, firms must make adjustments to their labor force. To deal with the now relatively higher cost of labor, some firms may fire workers while others may reduce the number of hours that each laborer works. In either case, the workers who are affected first are those who are the least productive. When faced with the excess supply of labor that is generated when the minimum wage is above the market rate, employers have an incentive to hire the most productive employees. Typically, the least productive workers are youths because they lack education and experience. Williams explains that “firms are less willing to hire and/or train the least productive employee, which includes teenagers, particularly minority teenagers” due to various socioeconomic factors (1982, 40). Politicians who enact minimum wage laws for the purpose of “helping the poor and disadvantaged” may harm the very people whom they intend to help.

In addition, the surplus of labor generated by minimum wage laws increases the likelihood that employers will hire based on their racial preferences. When an employer has several prospective employees who are all willing to work for the same wage, the employer faces no economic cost to indulging his racial preferences and is free to discriminate on non-economic factors. Because the most eager employee cannot bid down the price, he is helpless against the employer's racial discrimination. In the absence of minimum wage laws on a free market, workers who are discriminated against would be free to undercut wages and impose economic costs on employers who engage in racial discrimination.

Besides the indirect ways that minimum wage alters the prevalence of racial discrimination, minimum wage laws have been used intentionally and directly to price disliked groups out of the labor market, such as during Apartheid in South Africa. White South Africans used the argument of "rate for the job" to advocate for minimum wages (Hutt 1964, 72). Standard wage-rate laws held wages artificially above market rates, pricing less-preferred black South Africans completely out of certain labor markets and allowing white South Africans to maintain control over avenues of economic advancement (Hutt 1964, 72).

Unions

As is the case with other forms of government intervention, the granting of special privilege to unions can alter the costs of racial discrimination both directly and indirectly. Like minimum wage laws, unions create artificially high, uniform wage rates that generate a surplus of job applicants and reduce the costs of racial discrimination. In this way, unionization can contribute unintentionally and indirectly to an increase in the prevalence of racial discrimination. In addition, when wage rates are raised artificially high, firms must cut jobs and hours. The result is that the least skilled workers are priced out of the market, meaning minorities (who are often less educated, skilled, or experienced) are disproportionately affected by the disemployment effects of unionization (Sowell 1984, 89).

Historically, unions have been a tool used pervasively by Whites to maintain power over minority groups. In 1935, the U.S. Congress enacted the National Labor Relations Act (NLRA), which granted workers the right to unionize. At the time, however, many unions were “whites-only” and denied membership to African Americans or segregated them into lower-paid jobs (Rothstein 2017, 158). For example, the 1925 Constitution of the Brotherhood of Locomotive Firemen and Enginemen reads in Article 12, Section 22, that to be a qualified applicant a person “shall be white born, of good moral character, sober and industrious, not less than eighteen years of age, and be able to read and write the English language and understand our Constitution” (Grant 1972, 97). The fact that a person must be white is the first qualification listed. Racial discrimination does not get much more direct.

Both white workers and employers agreed to the unionization setup because the institutional structures in place incentivized them to do so. Daria Roithmayr describes the incentive structure well in her book *Reproducing Racism* when she writes:

> By forming a union that excluded black workers and by pushing employers to hire whites only, white railroad workers could drive up wages relative to their black and brown counterparts. Employers also profited from discrimination in their fight against unions. By dividing the labor market in two, railroads maintained a ready-made stable of black strikebreakers perpetually on call to undercut the power of the white

> union. For railroad and workers alike, then, discrimination was win-win. And those benefits came at the expense of black workers. (2014, 27)

Even though union workers are commonly represented as competing with their employers, it is in fact workers who compete among themselves. In situations like those described by Roithmayr, people with racial preferences can use the government-granted privilege of unionization to benefit themselves at the expense of others. Whether directly through race-specific membership requirements or indirectly through artificially high wage rates, unions reduce the costs and increase the pervasiveness of racial discrimination in a market.

Occupational Licensing

The general justification for occupational licensing requirements is that they protect the public from "incompetent and dishonest practitioners" (Gellhorn 1976, 6). To gain a license to work in a protected occupation, laborers must pass an examination that usually contains both practical and written sections (Dorsey 1983, 173). Licensing, like other government interventions in the labor market, alters incentives that affect racial discrimination both directly and indirectly. In a free market where no licensing exists, anyone is free to work anywhere they can find employment. Occupational licensing laws restrict entry into regulated industries both by requiring certain qualifications that disqualify some workers from obtaining a license and by restricting the total number of licenses available. The increased cost associated with obtaining an occupational license decreases the supply of labor in regulated industries thereby increasing the wage rates in those markets. Firms that face higher costs of labor due to licensing costs must rearrange their factors in ways that create disemployment effects that, as in the case of minimum wage, are often disproportionately felt by minorities. In addition, artificially high wages generate a surplus of job applicants, decreasing employers' costs of racial discrimination.

Besides generating the possibility of discrimination by employers, occupational licensing tests themselves can be discriminatory. To the extent that a licensing test measures a factor that is irrelevant to a worker's ability to do a job, certain applicants may be systematically excluded from employment that they are otherwise qualified to perform. For example, in his study of examinations for cosmetology licenses in Missouri and Illinois, Stuart Dorsey found that black applicants were 30% less likely to pass the licensing exam than other applicants (Dorsey 1983, 175). Since factors like formal education, which may impact an applicant's ability to perform well on a written test but be irrelevant to their skill with a razor, are correlated along racial lines, some researchers question whether certain licensing exams are racially discriminatory and contribute to the disproportionate failure rate for black applicants.

Whether or not licensing tests themselves contribute to racial discrimination, licensing examiners who hold the power to pass or fail applicants may directly engage in racial discrimination. Thomas Sowell describes a historical example of this occurring in the United States when he writes, "In the South, around the turn of the century, licensing examinations for black plumbers were conducted by white examiners, who almost invariably 'failed' them, even though the same individual blacks 'have easily met the requirements elsewhere'" (1981, 110). Occupational licensing requirements create many possibilities that can increase the presence of racial discrimination that do not exist in a free market. In the unhampered market, laborers must compete with one another. People do not receive state-sanctioned special privileges with which to gratify their racial preferences at no cost to themselves. Firms must make employment decisions based upon economic productivity or face being driven out of the market.

Direct Government Involvement: Requiring and Prohibiting Racial Discrimination

Throughout this paper it has been taken as a given that some people may, for any number of reasons, prefer one race of people to another and discriminate accordingly. The morality of whether having a racial preference and acting on it is good or bad lies outside the bounds of economic discussion. From the standpoint of economics, suffice it to say that, if one person disagrees with another about whether racial discrimination is acceptable or something to be deplored, such a person should try to convince the other of their point of view in a way that does not violate the other's personal property rights. It is appropriate for persons who disagree to argue and discuss, trying to convince the other that his preferences are wrong. But if two people disagree about the morality of racial discrimination, using the government to impose one's views and actions on another is not appropriate. As Milton Friedman describes, "the appropriate recourse is … not to use coercive power to enforce my tastes and my attitudes on others" (2002, 111). In fact, giving the government the power to prohibit racial discrimination is a dangerous acquiescence. For, a government that can ban racial discrimination can just as easily require it. Most often, as seen through the many historical examples throughout this paper, "majorities can surely be counted on to use their power to give effect to their preferences … not to protect minorities from the prejudices of majorities" (Friedman 2002, 114). A government strong enough to enact and enforce prohibition of racial discrimination is equally strong enough to enact and enforce a requirement of it. What must be kept at the forefront, however, is the fact that compliance with enforcement will always depend upon the costs of doing so.

When the government bans racial discrimination, the costs of such discrimination skyrocket. Not only are economic costs involved, but people who wish to discriminate on the basis of race must also face legal costs such as the possibility of jail time for violating the law. Despite the increase in costs, people who possess a strong preference to discriminate may still choose to do so and will find every method possible to work around the law and continue to indulge their preferences. One example of these preferences at work occurred in the U.S. during the early 1900s in the form of restrictive covenants.

When the Supreme Court banned the practice of racial zoning in 1917, white homeowners went to great lengths to keep their neighborhoods segregated. Restrictive covenants became widely used as a form of private racial discrimination that evaded the prohibition of racial zoning. Restrictive covenants were part of the deed clauses for houses and generally included items such as what color a homeowner could paint their house or what kind of trees could be planted in the yard. When a buyer bought a house, they signed the covenant agreeing to the terms and restrictions. From the 1920s through the 1960s, restrictive covenants in white neighborhoods included promises never to sell or rent to an African American in an effort to keep the neighborhood segregated (Rothstein 2017, 78). When restrictive covenants began to break down because of the difficulty of enforcing them, people began creating neighborhood contracts and community associations which residents were required to join before purchasing a home. Such contracts and associations excluded African Americans from membership, thereby preventing any African American from purchasing a home in a white area covered by a contract or association (Rothstein 2017, 79). These types of evasions demonstrate how even at high costs people will engage in racial discrimination if the perceived benefits in satisfying their preferences are high enough. A government ban of racial discrimination does not perfectly and completely remove its presence.

In other cases, such as when individuals with strong racial preferences are in power, a government may require racial discrimination. Such was the case in Apartheid-era South Africa. Again, the extent to which people follow the law is dependent upon the costs presented to them. When the costs of racial discrimination are too high relative to the benefits, people will evade or outright break the law. Sowell describes the situation in South Africa saying, “White employers in competitive industries violated official government policy on a massive scale by hiring more black workers and in higher positions than the law allowed” (2009, 221). He continues, “There is no compelling evidence that these particular white employers had different racial predispositions than the white people who administered the apartheid government. What they had were very different costs of discrimination” (2009, 221). Even when the government began to increase enforcement of the racially discriminatory requirements, construction companies continued to violate the law and pay the fines when caught. The economic cost of the fines was less than that of the profits that would had been lost following the law. Whether or not individuals choose to engage in racial discrimination will always depend upon the costs relative to the benefits of doing so. The law imposed by the government can only change the incentives, not what people choose to do based upon them.

The Case of Government Itself

The discussion of racial discrimination up until this point has focused almost entirely on the incentives faced by economic actors within the private sectors of the economy. One must remember that the government, too, is comprised of individuals who make decisions based on cost and benefit evaluations. What makes the actions of the government, government agencies, and government-controlled industries different from the rest of the private sector is that the government faces no profit and loss restraints. Unlike private individuals and firms that are restrained to some extent by the racist premium and other financial costs associated with racial discrimination, the government is restrained by no such costs as they possess an unlimited budget funded by taxpayers (not to mention having the ability to print their own money). Thus, it is not surprising that some of the greatest prevalence of racial discrimination is found in governments, their agencies, and their industries. Without financial restraints, governments face virtually no hindering costs of racial discrimination.

In 1913, U.S. President Woodrow Wilson began segregating government offices, installing curtains to separate clerical workers by race and creating separate bathrooms and cafeterias (Rothstein 2017, 43). As of 1950, the highly government regulated monopolistic U.S. telephone industry employed only one black woman for every 100 white women working as telephone operators (Sowell 2009, 218). Stark acts of racial discrimination like these can only occur because the government removes financial profits as an incentive, allowing individuals to make actions based on their racial preferences rather than economic efficiency.

Conclusion

Contrary to the fears that a free market would allow for unregulated and rampant racial discrimination, many factors contribute to costs that constrain the actions of individuals and the extent to which they choose to act upon the racial preferences, not the least of which is the racist premium. It is the government that often changes these factors through intervention in ways that decrease the costs of discrimination, increasing its prevalence in society. Even when a government bans racial discrimination, it usually does not possess the power to ensure perfect enforcement and people whose benefits still outweigh the costs will continue to engage in discriminatory practices. In addition, the government is often the greatest offender in this area as it does not face the same financial constraints as actors on a free market. Ultimately, a simple evaluation of costs and benefits determines why we see racial discrimination or why we don't.

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