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Harold A. Black academic conference: an introduction to the special issue

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Abstract

This special issue brings together the papers presented and discussed at the Harold A. Black Academic Conference hosted by the Probasco Distinguished Chair of Free Enterprise at the University of Tennessee, Chattanooga, the Haslam College of Business at the University of Tennessee, Knoxville, and the Political Economy Research Institute at Middle Tennessee State University. Dr. Black is an emeritus professor of finance at the Haslam College of Business at the University of Tennessee, Knoxville, and has had a distinguished career advancing our understanding of race and discrimination in banking and finance. More specifically, throughout his career, Dr. Black undertook in-depth empirical studies that examined the institutional details of statistically observed disparate outcomes in banking and finance to determine whether these outcomes were attributable to discrimination or could be explained by non-discriminatory factors. In some instances, Dr. Black found that addressing disparate outcomes with inappropriate policies could result in perverse consequences that harmed the intended beneficiaries. This introduction explores the relationship between Harold Black's work, the papers in this special issue examining, building on, and extending Harold Black's work, and public choice economics.

Keywords Discrimination · Lending · Public choice · Harold Black

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1 Introduction

In celebration of Dr. Harold A. Black's career achievements in advancing our understanding of race and discrimination in banking and finance, public choice scholars convened in Chattanooga, Tennessee, for a conference hosted by the Probasco Distinguished Chair of Free Enterprise at the University of Tennessee, Chattanooga, The Haslam College of Business at The University of Tennessee, Knoxville, and the Political Economy Research Institute at Middle Tennessee State University. The conference, organized by Claudia Williamson-Kramer, Ramon P. DeGennaro, and Daniel J. Smith, occurred September 8th – 10th at the Read House.

While Harold Black never formally contributed to public choice economics, his research complements the public choice literature on race and discrimination. Public choice economists examine the knowledge and incentive problems policymakers face in addressing discrimination with regulation. Black made several contributions demonstrating these epistemic and motivational constraints, and their perverse effects, in the banking and finance industry through in-depth analysis of financial institutions and practices. This perspective was enabled, in part, by Black's depth of industry and policy experience, which helped him to dig below the surface of broad statistical observations of disparate outcomes.

Section 2 details the connection between public choice and the study of race and discrimination. Section 3 reviews Harold Black's academic contributions and draws connections to the public choice literature. Section 4 presents the articles included in this special issue and draws connections to the public choice literature. Section 5 provides our many acknowledgements in hosting the conference and drawing together this special issue.

2 Public choice, race, and discrimination

There is a long-standing connection between public choice economics and the study of race and discrimination. For instance, anti-discrimination work within the public choice tradition applies the tools of public choice to advance our understanding of the causes and mechanisms of discrimination (Magness, 2020). Public choice economists primarily use regulatory capture to interpret discrimination as an economic efficiency and constitutional problem (Halcoussis & Lowenberg, 1998; Lewin, 1979, 2000; Magness, 2020; Roback, 1986, 1988, 1989).

An essential contribution of public choice economics is that policymakers often face knowledge and incentive problems when intervening in the economy (Leeson & Subrick, 2006; Levy, 2002; Pennington, 2011). The policies of even the most well-intended policymakers are vulnerable to knowledge problems, and the policies of the most well-informed policymakers are still vulnerable to incentive problems. In reality, no policymaker is benevolent or omniscient. Thus, effective policy proposals must consider the cognitive and motivational constraints of policymakers, voters, and bureaucrats to be robust to expected deviations away from idealized assumptions. When it comes to race and discrimination, adopting this public choice perspective can help us better understand the emergence and persistence of policies that have discriminatory impacts and the adoption and maintenance of policies that fail to address disparate outcomes or even cause harm to intended beneficiaries.

Knowledge problems, when it comes to race and discrimination policies, may involve the complexities in understanding the underlying causes of discrimination, correctly identifying the agents of discrimination (employer, customer, or employee), accurately understanding the limits of racial and ethnic classifications in statistical data (Bernstein, 2022; Bodenhorn, 2015), or interpreting whether observed statistical disparities are driven by discriminatory factors. Due to these knowledge problems, policy interventions may impose substantial costs while failing to achieve their objective. Providing false assurance that the issue has been adequately addressed, for instance, may also lead policymakers to turn their attention to other matters (Loury, 2002) or cause policymakers to look past more severe, identified causes of racial inequality, such as the criminal justice system (Loury, 2008) or zoning (Rothstein, 2017). Due to knowledge problems, policy interventions may even cause perverse outcomes that harm the very groups that policymakers sought to help (Bernstein, 2001; Coate & Loury, 1993; Ferguson 2022; Sowell, 2019; Williams, 2011).

Incentive problems can also emerge in policy interventions addressing race and discrimination (Fryer, Jr., 2010; Hutt, 1964; Leonard, 2005, 2016; Riley, 2014; Rothstein, 2017; Sowell, 2005; Williams, 1982, 2011). For instance, policymakers may be incentivized to adopt popular regulatory solutions to real or perceived discrimination problems despite severe knowledge problems or even when there is evidence that the electorally popular solution will be ineffective or detrimental. Incentive problems may also lead policymakers to use anti-discrimination rationales to advance partisan or special-interest agendas, particularly a concern when these agendas may undermine the market institutions that drive economic growth and foster racial tolerance (Agneman & Chevrot-Bianco, 2023; Berggren & Nilsson, 2013, 2016; Boettke & Smith, 2015; Easterly, 2000; Henrich et al., 2005; Roback, 1986). Policymakers might also be incentivized to falsely attribute undesirable outcomes to discrimination or blame the perverse discriminatory effects of previous policy interventions on the market, thereby reducing competition, one of the primary ways the market process aids in the elimination of discrimination (Becker 1957).

3 Harold Black's research and public choice economics

While Professor Black's research did not contribute directly to the public choice literature, his methodology and results complement those of public choice economics. The primary emphasis of much of Black's research is examining the prevalence and effects of discrimination in the financial industry. Black sought to look beyond measurements of statistical disparities in outcomes. Instead, his research drilled deeply into the details of financial institutions to examine the circumstances and the institutionally determined structure of incentives and the flow of information that produced the observed outcomes. Notably, his research also often examined how governmental policies affected the structure of incentives and the flow of information and, thus, the subsequent observed outcomes. His research, which often overturned or questioned some of the results from studies that found assumed discrimination was the cause of observed statistical disparate outcomes due to its failure to investigate institutional details, validated his methodological approach for measuring the presence and extent of discrimination.

The perception that racial discrimination is systemic in financial markets continues to motivate regulation. Black argued that, to be effective, such regulation needed to be well-designed and aimed at addressing disparate outcomes that could not be attributed to non-discriminatory factors. Black's seminal paper (Black et al., 1978) was one of the first econometric tests for bias in lending decisions and the first to employ logistic regression analysis in discrimination studies. Black uses careful empirical work to provide a deeper understanding of when and where discrimination occurs in the financial industry, finding that, at least in some cases, regulations intended to help minority groups by improperly diagnosing outcomes as discriminatory ended up causing harm to minority groups.

For instance, Black et al. (1997) and Black et al. (2001) find that Black-owned banks may discriminate against Blacks and low-income borrowers. Their results suggest that factors other than discrimination may drive statistical differences in outcomes between races. In another example, Black (1999) argues that lending regulations in the Community Reinvestment Act and the Home Mortgage Disclosure Act could lead to financial institutions extending loans to financially unqualified borrowers to reduce their rejection rates of minority groups. But this policy risks further damaging the credit histories of individuals with poor credit histories by exposing them to default risk. Separately, Black et al. (2003) find that banning mortgage overages may discourage banks from lending to financially riskier clientele and first-time customers, who are disproportionately members of minority groups because they often require additional time and thus impose additional costs during the loan approval process. They conclude that "Thus, policymakers and regulators should not strive to eliminate differential pricing but should concern themselves with those differences that are unrelated to market forces."

Black (1999) builds on the insights of Becker (1957) and Friedman (1962, p. 101), arguing that competition in the financial industry is a significant force in reducing the probability of discrimination and bias. This implies that regulation that substantially lessens competition, even if it overcomes knowledge and incentive problems, may still have offsetting effects that increase avenues for discrimination.

4 The contributions in this special issue

This special issue brings together a range of research using, building upon, and extending the work of Harold Black. In his contribution to this special issue, Black (2023) reviews the recent advances in the literature on discrimination in the financial industry. He examines the current literature to ask whether discrimination in lending still exists and, if so, whether it is intentional or not. He also provides biographical details, including how his time at the Office of the Comptroller of the Currency and industry consulting offered valuable inputs into producing relevant academic research. He recommends that young scholars take the time to understand the practical details and workings of financial transactions and markets. Blackboard theorizing uninformed by financial institutional detail is insufficient for making important determinations about discrimination in an industry or business.

Munger and Tilley (2023) assess the overarching themes in Black's scholarship and draw important connections to the public choice and institutional economics literature. They argue that the "reason to do careful empirical investigations is that some practices that appear racist have plausible profit-maximizing or risk-management explanations and that discrimination is a continuum, not a switch" (p. [to be determined in Special Issue]).

Williamson Kramer (2023) examines how cultural values associated with individualism and collectivism affect racial tolerance. Using data from the Integrated Values Survey, she finds that individualism is associated with more tolerant racial attitudes. Indeed, groups sometimes branded as intolerant are more tolerant than average, and individualism might be the key factor. Williamson Kramer argues that research examining discrimination must consider this cultural channel of influence via its individualism or collectivism. An implication is that policies that undermine or promote individualism can affect discrimination. This is particularly a concern given the potential cultural persistence of policies (Ariely et al., 2019; Jha, 2013). But, given that it is often difficult to impose foreign institutions on a culture that does not accept it (Boettke et al., 2008), it may mean that discriminatory cultures may persist de facto even under de jure changes (Acemoglu & Robinson, 2006).

Cyree and Winters (2023) use Home Mortgage Disclosure Act data from 2007 to 2016 to study banks rated "Outstanding" for Community Reinvestment Act purposes. Using models available to regulatory agencies, they find that despite being rated for outstanding compliance with the CRA, these banks statistically discriminate against Asian, Black, Hispanic, and women borrowers. But they also find statistical discrimination against white males lacking a co-applicant, a result, they argue, that is inconsistent with taste-based discrimination. The key is that even banks rated "outstanding" for compliance discriminate based on data and models available to regulators. This implies that either the models or data are flawed or at least not up to the task. This paper highlights the knowledge problems inherent in attempts by regulators to determine when discrimination exists. It provides additional support for Black's work demonstrating that statistical analyses of discrimination without investigation into institutional details often are insufficient for determining discrimination's existence.

Bolen et al. (2023) examine the effects of the payday lending interest rate cap in Illinois on subprime borrowers. They find that the cap substantially decreased lending and lending amounts to subprime borrowers. Using a survey of payday lending customers, they find that respondents said they were harmed by the interest rate cap, which left them with no options for borrowing money. This imposed other costs on them, such as late fees on missed payments and disconnected utilities. Survey respondents said they wished they could use their previous lender. This paper highlights the idea that perverse consequences can stem from the knowledge problems inherent in assessing and regulating the financial industry. Financial regulation pursued under public interest rationales can harm the very groups the regulation aims to help due to the lack of knowledge. Related to Black's work, they find that the unintended consequences may fall heaviest on low-income individuals, who are disproportionately minorities.

Reinarts and Melo (2023) examine the effect of the Americans with Disabilities Act of 1990 (ADA) on the educational attainment of disabled Americans using data from the Current Population Survey. Although the ADA was ostensibly intended to prevent discrimination against disabled individuals, Reinarts and Melo find that the Act negatively impacted post-secondary educational attainment for disabled Americans. Consistent with the theme of Black's work, in terms of educational achievement, but also in line with the literature on the Act's effect on employment, the ADA harmed the very disabled Americans the legislation was intended to help.

Richardson and Blizard (2023) examine the impact of the Dodd-Frank Act on low-income housing markets using data from Forsyth County, North Carolina. They find that the Act, which made small-dollar mortgages less profitable by imposing caps on points and fees, led to a measurable decline in property values for homes under $100,000. Absent these small mortgage loans, cash sales became the norm. Poor potential buyers, unable to raise the full purchase price, were driven out of the market; external investors took over much of the market. The Dodd-Frank Act, while driven by public interest rationales, suffered from not only public choice and regulatory capture factors (Ban & You, 2019; You, 2017) but also unintended consequences stemming from knowledge problems policymakers faced regulating complex and diverse financial markets.

Stringham (2023) builds on Black's (1979) work, finding that small financial institutions serving low-balance accounts are often disadvantaged compared to larger financial institutions that do not service the market for low-balance accounts. He argues that a fixed regulatory cost generates an Alchian-Allen effect that leads financial institutions to drop low-balance accounts. Regulators may prefer this outcome since it is easier to control and extract rent from large financial institutions (Stigler, 1971; Posner, 1974; McChesney, 1987). Given this effect, he argues that we should expect underbanking to be more prevalent in low-income countries with more regulation. Stringham examines how the market, through the expansion of the use of cryptointermediation, can help expand financial inclusion, using Nigeria as a case study. This research provides another example of an unintended consequence of financial regulation.

Melo and Neilson (2023) provide a novel index of rent-seeking using the industrial composition of state-capital MSAs against comparable synthetic matches. They find that industries traditionally associated with rent-seeking are over-represented near state capitals. This research provides an index that public choice scholars can use to advance our understanding of the causes and consequences of rent-seeking and aid future efforts to understand its effect on race and discrimination.

5 Conference and special issue acknowledgements

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Declarations

Competing interests The authors have no conflict of interest to report.

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