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ETHNIC DISCRIMINATION AND THE INCOME OF MAJORITY-GROUP WORKERS*

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Neo-classical economics suggest that workers belonging to a superordinate ethnic group gain from economic discrimination against members of a subordinate ethnic group. The Marxist perspective disagrees, contending that superordinate workers actually lose. When income differentials between Jews and Arabs across local labor markets in Israel are decomposed into "legitimate" and "discriminatory" components, the data lend support for the neo-classical perspective. However, the relationship between market discrimination and the income of superordinates is more complex than perceived by previous work on the topic. On the average, Jewish workers gain from economic discrimination against Arabs. But they do not gain equally. Such discrimination results in increased income inequality among Jewish workers, increasing the income share received by Jewish workers at the upper tail of the income distribution and decreasing the income share received by workers at the lower tail.

Students of social stratification agree that discrimination has detrimental consequences for the income of subordinate racial and ethnic groups. For example, blacks and Hispanics in the U.S. earn less than comparable whites, and Arabs in Israel earn less than Jews with similar characteristics. Although most of the discrimination literature is concerned with the costs of discrimination for minorities, a substantial literature focuses on its impact on members of the *super*ordinate group. For example, in the U.S., a long-standing question has been whether whites gain or lose financially from racial discrimination against black workers.

The two main theoretical positions on this issue are seemingly incompatible. One is derived from neo-classical economics, the other from Marxist class analysis. Neo-classical economics contends that discrimination is economically irrational — while employers underpay minority workers, they overpay majority workers. Thus, discriminatory employers lose from discrimination. The beneficiaries of such discrimination are employees from the superordinate group (Arrow 1973; Becker 1957). Marxists take issue with this position. Viewing discrimination as one strategy of the capitalist class to divide and conquer the working class, they claim that only employers gain from discrimination. Workers, including those who belong to the superordinate group, actually lose (Reich 1971, 1978).

Previous empirical research that attempts to resolve this theoretical controversy has so far produced inconsistent and even conflicting findings (cf. Beck 1980). While several researchers have lent empirical support to the neo-classical position (e.g., Villemez 1978), others have provided findings congruent with Marxist arguments (Reich 1971, 1978; Bonacich 1972; Szymanski 1976, 1978). This paper contributes to the ongoing debate by analyzing the impact of labor market discrimination against Arabs in Israel on the economic well-being of Jewish workers.

PREVIOUS RESEARCH

As part of his path-breaking Marxist analysis, Reich (1971) examined the effect of discrimination on income inequality among whites across the 48 largest U.S. SMSAs in 1960. His measures of inequality were the Gini coefficient and the share of income received by the top one percent of white families. His measure of discrimination ("racism") was the ratio of black to

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white median family income. The lower the numerical value of this ratio, argued Reich, the higher the combined effect of direct labor market discrimination, as well as indirect discrimination (e.g., discrimination in education and housing) against blacks in the community. The data analysis revealed that as discrimination increases so does inequality among whites, thus supporting the Marxist contention that discrimination reduces both black and white workers' income.

Using 1970 census data, Szymanski (1976) measured discrimination as the ratio of black to white male median earnings (rather than Reich's family income), thus focusing more closely on labor market processes (cf. Villemez 1978). Szymanski also substituted the median earnings of white males for one of Reich's measures of income inequality (income share of top 1 percent), arguing that it captures more directly the notion of white economic gain or loss. Controlling for several key variables, Szymanski's empirical analysis yielded results similar to Reich's, again supporting the Marxist analysis.

Villemez (1978) questioned the validity of both Reich's and Szymanski's findings on the grounds of a series of "severe conceptual and methodological problems" (p. 772). First, he pointed out a problem of multicollinearity among key variables. Second, he maintained that median income and the Gini coefficient are inadequate indicies of white economic well-being. Better measures are the proportion of white workers earning over $15,000 and less than $5,000 in 1970. However, far more troublesome in Reich's and Szymanski's analyses, according to Villemez, were their measures of discrimination ("racism"). He argues that the Index of Net Differences (Lieberson 1976) is a better proxy for black/white income inequality than the ratio of black to white earnings or income. By reanalyzing the 1970 census data (utilizing different measures for both discrimination and economic well-being) Villemez demonstrated that whites appear to gain from both the presence of blacks and from black subordination.

The confusion between these two bodies of research was recently captured in a comprehensive analysis by Beck (1980). Using longitudinal data and the multitude of measures suggested by previous research, Beck failed to support the Marxist view, but provided only weak support for the neo-classical position. Beck's conclusion is equivocal: "While this study does not invalidate Reich's and Szymanski's work, it at least calls their findings into serious question" (p. 164).

It is not clear whether the confusion surrounding the findings is a function of different measures, different methodologies, or both. What seems clear, however, is that previous research used measures of discrimination that are inadequate for testing the two theories. All have employed measures based on some aggregate ratio of black/white income and assumed that this ratio is determined solely by pre-market and market discrimination. This is not necessarily so. The ratio could reflect, for example, different preferences for work and leisure between the races that have nothing to do with pre-market discrimination, let alone market discrimination. Even if these ratios capture overall discrimination (market and premarket), they cannot distinguish between the two components. Yet neo-classical economics confines its theoretical focus to the effects of *market* discrimination (i.e., income differentials between the races that are *not* a function of their different levels of human capital) on the economic well-being of the superordinate group. It is *not* concerned with the effects of *pre*-market discrimination.

A more conventional measure of market discrimination that takes into account the relevant characteristics (e.g., education) of the two groups is necessary for testing the neo-classical prediction. In the analysis that follows we use individual-level data to estimate such measures in order to properly address the neo-classical thesis.

DATA SOURCE

Israel provides an especially illuminating setting to examine the impact of market discrimination on the income of a superordinate group. The most meaningful ethnic split in Israeli society is between the Jewish majority and the Arab minority. Previous research has repeatedly demonstrated that Jews in Israel are superordinate to Arabs in every aspect of social and economic status (Peres 1971; Simon 1971; Semyonov 1988). Israeli Arabs comprise about 17 percent of the population. They have fewer years of schooling than Jews, hold lower status occupations, and earn less than Jews with comparable characteristics. While the degree of residential segregation in Israel is extreme, most Arabs find employment in Jewish communities (Semyonov 1988).

The 1983 Israeli census of population provides detailed demographic and socioeconomic information on individuals as well as identification of community of employment. It is thus possible to construct data files on communities in which both Jews and Arabs are employed in order to examine the effect of market discrimination against Arabs on the economic well-being of Jews. There are 33 Jewish communities (or aggregates of adjacent communities) that we view as local labor markets with a substantial number of Arab workers.[1] The availability of data on individuals at the community level makes it possible to estimate both mean characteristics and regression equations predicting income for Jewish and Arab workers employed in each community, in order to arrive at indicators of market discrimination and economic well-being.

MEASURING MARKET DISCRIMINATION

Market discrimination is defined as the portion of the income gap between the superordinate and the subordinate groups that does not stem from differences in human resources or human capital characteristics (the "legitimate" gap), but rather from group membership and differential returns on relevant human capital resources. In order to estimate market discrimination, the total income gap between groups is decomposed into "discriminatory" and "legitimate" portions. There are several parallel models for decomposing mean differences between groups via the use of regression equations (e.g., Duncan 1968; Oaxaca 1973; Iams and Thornton 1975). In the present analysis, we applied the decomposition technique of regression equations suggested by Jones and Kelly (1984). The decomposition model is written:

$$Y_J - Y_A = [(a_J - a_A) + \sum (b_J - b_A) X_A] + \sum b_A (X_J - X_A) + \sum (b_J - b_A)(X_J - X_A) \quad (1)$$

where Y is the mean income of the J (Jewish) and A (Arab) groups, X is the mean value of the human resources antecedent variables included in the equation, b's are regression coefficients, and a's are the respective intercepts.

The model identifies three components. The first is the unexplained difference between the groups that reflects both group membership and differential returns on human resources. The second component is the portion of the gap due to differences in human resources, and the third is the interaction effect of jointly changing both mean resources and coefficients over the effect of changing them one at a time. Only the first component represents market discrimination while the other two capture the "legitimate" income gap between the groups. Market discrimination (MD) is thus defined as:

$$MD = [(a_J - a_A) + \sum (b_J - b_A) X_A] \quad (2)$$

Two regression equations, one for Jews and one for Arabs, were estimated in each of the 33 communities to calculate the coefficient of market discrimination. In each equation, monthly income was taken as a function of years of formal education (EDUC), age in years (AGE), age squared (AGESQ), and weekly work hours (HOURS).[2] For each community, the equations were decomposed to obtain the estimate of market discrimination as defined in equation 2. Thus, MD measures the portion of the income gap between Jews and Arabs employed in the same community that is attributable to group membership and differential returns on hours of work, education, and age. Each community was then assigned a value of market discrimination that was used in the analysis as a characteristic of the local labor market. The magnitude of MD was measured in Israeli shekels, and as a percentage of the total income gap between the two groups.[3]

[1] The 20/100 Israeli Census is a systematic random sample of households stratified within region of residence. The present analysis focuses on 144,043 employed males in the labor force between 25 and 64 years of age. The target population is Jews and Arabs who are employed in Jewish (or mixed) communities. There are 33 communities (or aggregates of adjacent communities), each of which forms a local labor market. In each market there are at least 30 Arab employees. Women are excluded from the analysis because very few Arab women commute to work in Jewish communities (Semyonov 1988). Six communities were excluded from the analysis because the number of Arabs employed was too small.

[2] Age, education, hours, and occupation are the only relevant individual characteristics available in the Israeli census.

[3] To test reliability, we also estimated market discrimination using the procedure suggested by Duncan (1968). Using this measure of market discrimination, we obtained virtually the same results.

Table 1. Means, Standard Deviations, and Correlations Among Variables Included in the Analysis: 33 Local Labor Markets, Israeli Labor Force, 1983

Variable	Mean (S.D.)	Variable 1	2	3	4	5	6	7	8	9	10	11
1. Mean Income (Jews)	38656 (3730)	----										
2. Mean Income (Arabs)	22834 (3479)	.079	----									
3. Income Gain (Jews)	811 (3167)	.894	.080	----								
4. Market Discrimination (in Israeli shekels)	6565 (4524)	.461	-.611	.523	----							
5. Market Discrimination (% of total gap)	39.19 (17.36)	.200	-.410	.282	.858	----						
6. NEWMD (in Israeli shekels)	6467 (4245)	.477	-.551	.527	.980	.862	----					
7. NEWMD (% of total gap)	39.37 (18.28)	.183	-.198	.249	.705	.916	.783	----				
8. TOP5	16.4 (2.4)	.424	-.258	.387	.552	.409	.560	.359	----			
9. BOTTOM20	7.3 (.8)	-.511	.131	-.382	-.447	-.420	-.489	-.443	-.629	----		
10. % Arab	7.14 (5.79)	-.184	-.073	-.201	-.044	.161	.142	.363	-.092	.056	----	
11. % manufacturing	27.82 (13.0)	-.140	-.091	-.086	.012	.076	.054	.155	-.200	.262	.374	----
12. Size	6303 (8029)	.403	-.167	.172	.126	-.005	.095	-.074	.326	-.527	-.215	-.272

Note: See text for definition of variables.

ESTIMATING ECONOMIC WELL-BEING

The economic well-being of Jewish workers in each community was estimated by two indicators — income level and income gain. The first indicator, mean income of Jewish workers in the community, is straightforward and similar to those used in previous studies. The second indicator focuses on income of Jewish workers in the community, net of their human resources. It represents the component of income that appears to be determined by community and will be referred to as a measure of income gain. The two indicators are not mutually exclusive — the correlation between them exceeds .9.

The indicator of income gain was obtained using Duncan's (1968) model of indirect standardization. By forcing the mean socioeconomic characteristics of Jewish employed men (i.e., education, age, age squared, and weekly hours of work) of each community through the regression equation predicting income for the total Jewish male labor force, it is possible to estimate the expected income of workers in the community had their income been determined exactly like the total Jewish labor force. The deviation of observed mean income from expected mean income represents the amount of income workers "gain" or "lose" in the community relative to the total labor force, net of their human resources. The computation of the indicator of income gain was performed according to the following equation:[4]

$$\text{GAIN} = \bar{Y}_i - \hat{Y}_i = \bar{Y}_i - [-80801 + 3298\ \text{AGE}_i - 33\ \text{AGESQ}_i + 2740\ \text{EDUC}_i + 263\ \text{HOURS}_i] \quad (3)$$

where $\bar{Y}$ and $\hat{Y}$ are observed and expected mean

[4] The equation according to which the computation was performed is that estimated for the total Jewish male labor force age 25 - 64.

incomes of workers in the i^{th} community and AGE, AGESQ, EDUC and HOURS are the mean value of those variables in the i-th community. We refer to this measure as income "gain," keeping its operational definition in mind. Positive values represent relative net "gain" of income while negative values indicate net "loss."

THE RELATIONS BETWEEN MARKET DISCRIMINATION AND INCOME GAIN

Table 1 contains the means, standard deviations, and correlations among the 12 variables used in this analysis of 33 communities. The mean income of Jewish workers is substantially higher than that of Arab workers, and there is a considerable variation in the income level of each of the two groups across local labor markets. Furthermore, on the average, nearly forty percent (39.19) of the income gap between the groups can be attributed to *differential* returns on human resources and group menbership (i.e., market discrimination).

The zero-order correlation coefficients in the top five rows of Table 1 lend support to theoretical expectations derived from the neo-classical model. Market discrimination (in Israeli shekels) is positively related to both mean income (.461) and income gain of Jewish workers (.523). Similar results are obtained defining market discrimination as percentage of the total gap — the correlation with income gain is .282, and with mean income is .200. Apparently, Jewish workers tend to gain income in places where market discrimination against Arab workers is more pronounced.

From a theoretical viewpoint, market discrimination is the key independent variable explaining the income gain of Jewish workers. Nevertheless, the sociological literature underscores several other community characteristics that are central for understanding both income level of residents and socioeconomic differentials between ethnic groups, most notably size of the labor market, ethnic composition, and industrial structure (e.g., Frisbie and Niedert 1977; Semyonov, Hoyt and Scott 1984; Villemez 1978). Thus, it is important to control for these community attributes when examining the effect of market discrimination against Arabs on the economic gain of Jewish workers. In the present research, ethnic composition is measured by the percentage of Arab workers (*% Arab*) in the community work force; size of the labor market is the number of persons employed in the community; and industrial structure is defined as the percentage of the work force employed in manufacturing industries (*% manufacturing*).[5]

Table 2. Regressions Predicting Two Measures of Economic Well-Being of Jewish Workers in 33 Israeli Communities (Standard Errors in Parentheses)

	Mean Income		Income Gain	
Variable	(1)	(2)	(3)	(4)
Market Discrimination (in Israeli shekels)	.352*** (.127)		.367*** (.110)	
Market Discrimination (% of total gap)		48.2 (36.3)		58.1* (32.1)
% Arab	-85.9 (107)	-91 (118)	-116 (92)	-125 (104)
Size	.148* (.075)	.173** (.081)	.048 (.064)	.050 (.072)
% manufacturing	-2.5 (48)	-.88 (53)	.80 (42)	2.2 (47)
Constant	36095	36349	-946	-952
R^2	.352	.222	.327	.157

*$p<.10$ **$p<.05$ ***$p<.01$

In the following analysis, a series of regression equations incorporating community characteristics is estimated. In equations 1 and 2, mean income of Jewish men is taken first as a function of market discrimination measured in Israeli shekels (equation 1) then as a function of market discrimination as percent of the total gap (equation 2). In equations 3 and 4, income gain is the dependent variable measuring well-being while market discrimination in Israeli shekels and in percentage terms, respectively, are included in the set of the independent variables.

The findings revealed by the regression analysis (see Table 2) are consistent with the previous correlation analysis. The selected community characteristics do little to reduce the benefit to Jewish men of market discrimination against Arabs. These findings provide support for the neo-classical view. In all equations, the effect of the market discrimination variables when expressed in Israeli shekels is positive and substantial. When expressed as percentage of

[5] The sample size of the community male work force ranges between 455 and 33,440. Note also that income of Jewish workers is related positively to size and negatively to manufacturing employment in the community (see Table 1).

the income gap it remains positive and is sometimes significant. Apparently, in labor markets where Arabs "pay" increasing costs of economic discrimination, Jewish workers enjoy higher income in both absolute and relative terms.

THE ROLE OF OCCUPATIONAL DIFFERENTIATION

The positive effect of market discrimination against Arabs on the economic gain of Jewish workers may result from the extreme occupational segregation between the groups.[6] Arab workers, especially those employed in Jewish places, are heavily concentrated in low-status manual and service occupations. They are not competing with Jews for high-status, rewarding jobs (Semyonov 1988). According to the "overflow thesis," their presence in the labor market may enable Jews to abandon the least-desirable occupations and to "flow" in disproportionate numbers to prestigious and rewarding jobs (e.g., Glenn 1966; Frisbie and Niedert 1977; Spilerman and Miller 1977; Semyonov et al. 1984).

To examine the role of occupational segregation, we re-estimated market discrimination, taking into account the difference in occupational status between Jews and Arabs. The new estimates were obtained by applying Jones and Kelly's (1984) decomposition procedure to regression equations predicting income of Jews and Arabs as a function of age, age-squared, education, hours of work *plus* occupational status[7] for each of the 33 local labor markets. These estimates of market discrimination (NEWMD) represent the portion of the income gap between Jews and Arabs attributable to group membership and differential returns on education, age, hours of work, as well as on *occupational status*.

Whether measured in Israeli shekels or as percentage of the income gap, these new estimates of market discrimination were positively correlated with both average income and income gain of Jewish workers. The zero-order correlations between the variables range between .527 and .183 (see Table 1). Thus, even when considering the variation in occupational status between Jews and Arabs, the income of Jewish workers tends to be higher in labor markets characterized by higher levels of market discrimination against Arabs.

Table 3. Regressions Predicting Two Measures of Economic Well-Being of Jewish Workers in 33 Israeli Communities, Using NEWMD[a] (Standard Errors in Parentheses)

	Mean Income		Income Gain	
Variable	(1)	(2)	(3)	(4)
NEWMD (in Israeli shekels)	.416*** (.132)		.417*** (.115)	
NEWMD (% of total gap)		58.5 (36.0)		64.0* (31.9)
% Arab	-117 (105)	-134 (122)	-146 (91)	-169 (108)
Size	.147* (.072)	.176** (.080)	.024 (.063)	.053 (.071)
% manufacturing	-3.42 (47)	-1.12 (52)	.42 (42)	2.16 (46)
Constant	35967	36230	-996	-895
R^2	.389	.244	.358	.176

*$p<.10$ **$p<.05$ ***$p<.01$

[a] NEWMD (market discrimination) incorporates differences in occupational status between Arabs and Jews. See text for details.

Table 3 displays a series of regression equations predicting average income (equations 1 and 2) and income gain (equations 3 and 4) of Jewish workers using NEWMD and community characteristics. In equations 1 and 3, NEWMD is expressed in terms of Israeli shekels. In equations 2 and 4, NEWMD is measured as the percent of the income gap between Jews and Arabs. The results lend further support to the neo-classical model. In all equations, the effect of market discrimination on the income level of Jewish workers is positive (and significant in all but equation 2) — the income of Jewish workers tends to be higher in communities where market discrimination is high and this cannot be explained by the occupational segregation between Jews and Arabs.

MARKET DISCRIMINATION AND INCOME INEQUALITY

The findings presented thus far demonstrate that, on average, Jewish workers gain income in communities where economic discrimination against Arabs is more pronounced. These find-

[6] The index of dissimilarity across 323 occupational categories is 50. That is 50 percent of either group must change occupations in order to reach equality in the occupational distributions.

[7] Occupational status was measured on Tyree's (1981) index for occupations in Israel.

ings, however, do not tell us whether Jewish workers gain equally from such discrimination. Theoretical models such as those of the split labor market (Bonacich, 1972) or the competition hypothesis (Hodge and Hodge, 1965; Snyder and Hudis, 1976) lead us to expect a differential effect of discrimination on the income of the superordinate group. These models suggest that because of discrimination, members of subordinate groups have to supply their labor at a lower cost. This may lead to the deterioration of working conditions of those majority members who compete with minorities in the same labor market for the same jobs (mostly low-status, low-paying jobs). In a similar vein, the overflow thesis implies that the presence of minority members in the labor market benefits mainly members of the majority group at the top of the social system.

To examine these hypotheses we computed two measures of income inequality among Jewish workers. The first measure is defined by the share of all Jewish income received by the top 5 percent of Jewish workers in each local market (TOP5). The second measure represents the share of income received by the bottom 20 percent of Jewish workers in the locality (BOTTOM20).[8] If high-paid workers gain disproportionately from economic discrimination against minorities, MD (market discrimination) should exert a positive effect on TOP5 and a negative effect on BOTTOM20.

Table 4 contains the results of this analysis. In equations 1 and 2, TOP5 is taken as a function of market discrimination with other community characteristics entered as controls. In equation 3 and 4, BOTTOM20 is taken as a function of market discrimination with the same controls present.[9]

The regression analysis firmly supports the hypothesis that high-paid workers gain disproportionately from market discrimination against minority workers. The impact of market discrimination on TOP5 is positive, significant, and stronger than any other term in equations 1 and 2. The effect of market discrimination on BOTTOM20 is negative and significant. Indeed, in all four equations the effect of market discrimination on income inequality is over twice the size of its standard error. Apparently, in labor markets where discrimination against Arabs is more pronounced, the income share of Jewish employees at the top of the income distribution is larger while the income share of Jews at the bottom of the distribution is smaller.[10]

Table 4. Regressions Predicting Share of Income Received by Jewish Workers at the Top 5% and the Bottom 20% of the Income Distribution in 33 Israeli Communities (Standard Errors in Parentheses)

	TOP 5%		BOTTOM 20%	
Variable	(1)	(2)	(3)	(4)
NEWMD (in Israeli shekels)	.310*** (.082)		-8.34*** (2.52)	
NEWMD (% of total gap)		58.8** (22)		-23.0*** (5.8)
% Arab	-28.8 (65)	-58.4 (75)	-5.81 (20)	10.2 (20)
Size	.065 (.045)	.086* (.049)	-4.34*** (1.38)	-4.90*** (1.3)
% manufacturing	-26.1 (29)	-24.9 (32)	10.9 (8.92)	10.9 (8.43)
Constant	14954	14690	7854	8142
R^2	.418	.299	.500	.553

*$p<.10$ **$p<.05$ ***$p<.01$

Note: Coefficients were multiplied by 10^5.

CONCLUSION

The main purpose of the research reported here was to examine whether members of superordinate ethnic groups gain or lose from labor market discrimination against workers of a subordinate ethnic group. The data analysis lends support to a neo-classical model, which suggests that majority workers benefit from such economic discrimination. However, it also demonstrates that the relationship is complex, because discrimination against Arab workers enlarges

[8] Since the data are confined to employed men and exclude the self-employed and unemployed, the top 5 percent are mostly salaried professionals and managers, and the bottom 20 percent are mostly unskilled workers.

[9] Although market discrimination is viewed here as a determinant of inequality, the possibility that inequality may influence market discrimination cannot be rejected. Since our main interest, however, is explaining inequality, it is treated here as the dependent variable. The determination of the causal order between these two variables is beyond the scope of this analysis.

[10] This finding is consistent with other studies suggesting that income gains are not equally distributed; workers at the top are likely to gain more than workers at the bottom (Villemez and Wiswell 1978; Freeman 1973).

the income inequality of Jewish workers. It increases the income share of Jewish workers in the upper tail of the income distribution and decreases the income share of workers in the lower tail of this distribution. Ironically, those who benefit most from economic discrimination against minorities are the workers who are least likely to compete with them. Our findings suggest that when more than one group of workers stands to benefit from economic discrimination against minorities, those at the top of the social system benefit more than those at the bottom.

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