

April 24-30, 2006  
Vol. 10, No. 34

April 24, 2006

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## Economist deciphers racial disparities in business ownership

By Jennifer McNulty

Economist Robert Fairlie knows that business ownership can be an escape route out of poverty, so he is bothered by an African American self-employment rate that's less than half the national average.

Only 3.8 percent of blacks own their own business, compared with 6 percent of Latinos and 11.6 percent of whites and Asian Americans, according to the most recent data. Moreover, black-owned businesses generate dramatically lower annual sales than firms owned by whites and Asian Americans, and they are more likely to close.



Robert Fairlie

For years, Fairlie has pored over data to understand these disparities with an eye toward identifying policy recommendations that would close the gap. With Alicia Robb of the Foundation for Sustainable Development, Fairlie has uncovered the primary factors that account for the differences, including striking inequality in levels of startup capital, as well as differences in work experience and educational achievement.

"Business ownership is an alternative to unemployment and discrimination in the labor market, and political influence comes with success in small business," he said. "Historically in this country, we've seen rapid growth of business ownership among immigrants, including Chinese, Japanese, Jews, Italians, Greeks, and, most recently, Koreans."

Yet rates of business ownership have been stubbornly stable among African Americans, said Fairlie, who presented his research during a talk entitled "Race, Families, and Business Success: A Comparison of African American-, Asian- and White-Owned Businesses." His presentation was sponsored by the UCSC Equal Employment Opportunity/Affirmative Action Office as part of its diversity lecture series.

Black-owned businesses average annual sales of about \$60,000, compared with \$167,000 for Latino-owned businesses, \$219,000 for white-owned businesses, and \$245,000 for Asian-owned firms.

Business failure rates during the first four years are 27 percent for black-owned firms compared with 22.5 percent for white-owned businesses. Only 14 percent of black-owned businesses generate annual profits of \$10,000 or more, compared with 30 percent of white-owned firms, and black businesses are less likely to employ others (11 percent compared with 21 percent), according to Fairlie's analysis of Census data.

In their search for contributing factors, Fairlie and Robb considered variables such as parental ownership of a business, industry-specific work experience, managerial experience, and location (urban or rural).

They discovered that people who had a self-employed parent are two- to three-times more likely to be a business owner than people who didn't have a self-employed parent, creating a strong "intergenerational link in self-employment."

But startup capital, prior work experience in a family-owned business, and education emerged as the biggest differences in the success and survival of black- and white-owned businesses, accounting for 43 percent, 11 percent, and about 6 percent of the disparity in business outcomes, respectively.

Businesses launched with \$100,000 or more of startup capital were twice as likely to prosper, but only 1.7 percent of black-owned businesses start out with more than \$100,000, compared with 4.9 percent of white-owned firms, said Fairlie. Similarly, 6.5 percent of black-owned businesses have more than \$25,000, compared with 11.1 percent of white-owned firms.

Vast differences in the net worth of blacks and whites accounts for the disparity in startup capital, said Fairlie. Defined as total assets, including home equity, automobiles, and savings, net worth among blacks is about \$6,000; Latino net worth averages \$7,000; and white and Asian

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American net worth is about \$70,000.

"Wealth inequality leads to these low levels of capital, which is a huge factor in determining the outcome of a business," said Fairlie, adding that, "Economists tend to focus on wage and income inequality, but there really needs to be more attention paid to *wealth* inequality in this country."

By contrast, 12 percent of firms owned by Asian Americans are launched with more than \$100,000 in capital, and they generate sales that are 60 percent higher than white-owned firms, said Fairlie.

"Half of all Asian Americans in the labor market have a college education or higher," said Fairlie, underscoring the importance of education.

In light of their findings, Fairlie and Robb identify several avenues for policy review, including improving bank lending laws to further protect African Americans from discrimination, addressing wealth inequality, and creating apprenticeships that would help make up for the lack of work experience in family-owned businesses available to blacks.

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