



Neighbor discrimination theory and evidence from the French rental market[☆]



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ARTICLE INFO

Keywords:

Customer discrimination
Matching frictions
Neighborhood externalities
Housing market

JEL classification:

R21
J71

ABSTRACT

This paper describes a novel concept of customer discrimination in the housing market, neighbor discrimination. We develop a matching model with ethnic externalities in which landlords differ in the number of apartments they own within the same building. Larger landlords are more likely to discriminate only if some tenants are prejudiced against the minority group. Observing that minority tenants are less likely than majority group tenants to live in a building with a single large landlord is thus evidence of neighbor discrimination. We show empirically that African immigrants in France are significantly less likely to live in a building owned by a single landlord. This increases the probability that African immigrants live in public housing in localities with more single-landlord private apartment blocks.

1. Introduction

The housing market and more precisely the rental market is the quintessential customer market (Lang, 2007). And yet, empirical research on housing market discrimination has not benefited as much as it could have from Becker's (1957) theoretical insights into the rationale for customer discrimination. This paper develops a search model predicting that a particular group of landlords are more inclined than others to care about tenants' prejudice. It derives an empirical strategy to test for the existence of a particular customer discrimination in the housing market: *neighbor discrimination*. We then implement the test on French data and quantify the effects of neighbor discrimination on segregation into the public housing sector.

The main intuition is that the implications of neighbor discrimination in the rental market depend on the ownership structure within buildings. Some buildings with several flats are entirely owned by a unique landlord (hereafter, *building landlord*), whereas in many

buildings, landlords own a single flat (hereafter, *dwelling landlords*). Suppose that among the majority group in the population of potential applicants, the “Whites”, some will turn down an offer in a building in which some of the other tenants are part of a “Black” minority. Such a neighbor discrimination should matter more for building landlords than for dwelling landlords. Unlike the former, the latter do not care that accepting a black tenant may make it more difficult for the other landlords in the building to find a tenant.

We develop this idea in a dynamic framework with ethnic heterogeneity, two-dwelling buildings, fixed rents and matching frictions (Section 2). Dwelling landlords sharing a building play a dynamic game whose (Markovian) equilibria are studied; building landlords maximize the value of the building. The model highlights two externalities due to the presence of prejudiced Whites. Accepting a Black tenant today generates a *static externality* whereby it becomes more difficult to fill in the other vacant lot today because prejudiced Whites refuse to rent. It also generates a *dynamic externality* whereby it becomes more difficult

[☆] This paper updates work registered as CEPR working paper 9160. Previous versions of this paper have circulated under the title “The Neighbor is King: Customer Discrimination in the Housing Market”. It has benefited from the comments of Jim Albrecht, Pierre Cahuc, Jan Eeckhout, Cecilia Garcia-Penalosa, Laurent Gobillon, Florence Goffette-Nagot, Morgane Laouénan, Thomas Piketty and Sébastien Roux, as well as two anonymous referees and the editor. We also thank seminar participants at GREQAM, CREST, INSEE, Sciences-Po, Paris School of Economics, Rennes University, Aix-Marseille University, INED and Georgetown University, as well as conference participants in Dijon, Aix-en-Provence, Glasgow, London, Shanghai, Uppsala and Ghent. Data was made available by the Centre Maurice Halbwachs and the Centre d'Accès Sécurisé à Distance. This research is supported by the Direction de l'Animation de la Recherche, des Etudes et des Statistiques (Dares) and a public grant overseen by the French National Research Agency (ANR) as part of the “Investissements d'Avenir” program (reference: ANR-10-EQPX-17 - Centre d'accès sécurisé aux données – CASD).

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<https://doi.org/10.1016/j.jue.2018.01.002>

Received 14 July 2015; Received in revised form 24 October 2017; Accepted 23 January 2018

Available online 31 January 2018

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to fill in the same flat in the future because the tenant in the other apartment will more likely be Black. Both externalities provide a rationale to discriminate because they reduce the value of the building. However, only the building landlords can internalize the static externality.

In equilibrium, all landlords have the same behavior when faced with unprejudiced White applicants. However, the static externality implies that building landlords tend to discriminate more often than dwelling landlords when there are prejudiced Whites. Discriminatory behavior requires that the arrival rate of applications and the share of prejudiced Whites are sufficiently large, whereas the share of Blacks is sufficiently small. Otherwise neighbor discrimination does not affect housing market outcomes. A related prediction is that black tenants rent less often from building landlords only if there are prejudiced Whites. This prediction provides a test of neighborhood discrimination that can be run on regular survey data, provided the landlord type is reported in the survey.

Sections 3 and 4 conduct empirical tests of the theory using data from the French National Housing Survey. The survey is conducted at dwelling level and reports whether there is a single building landlord or not. This provides a natural measure of the building landlords of our theory. The minority group supposedly exposed to neighbor discrimination is composed of African immigrants. These individuals are mostly confined to the rental sector and largely over-represented in the public housing sector. According to the 2002 French Housing Survey, only 22% owned their dwellings against 56% for the whole population, and 46% lived in public housing (HLMs) against 15% for the whole population.

Our empirical work aims at understanding whether African immigrants are exposed to neighbor discrimination and whether this contributes to their segregation into the public housing sector. Although the proportion of African immigrants is large in a few cities, making less likely the possibility of discrimination in the expectation of a white tenant, the mean proportion in the rental market is about 13% and varies across cities, which allows us to detect discriminatory behaviors.

In Section 3, we show that African immigrants living in privately-rented apartments are less likely to have a building landlord. In accordance with our theory, this result is suggestive of neighbor discrimination. According to our estimates, the marginal effect of being an African immigrant instead of a French-born citizen decreases the probability of matching with a building landlord by 3–6 percentage points. These figures represent between 7.5% and 15% of the unconditional probability of having a building landlord and at least 50% of the probability gap of having a building landlord. We obtain these results by means of a regression framework whereby we account for potential confounding factors and also by a test based on propensity score matching.

In Section 4, we compute the share of dwellings owned by building landlords in each local housing market. The probability that tenants of African origin will live in public housing is positively correlated with this variable, whereas the correlation does not stand for any other ethnic group. This second result suggests that neighbor discrimination constrains Africans to reside in public housing. The effect is economically significant: an increase by one-standard deviation of the share of dwellings owned by building landlords raises the African-specific probability of living in public housing by 7 percentage points, which amounts to nearly 30% of the unexplained differential between African immigrants and natives.

These findings are worrisome. Unlike taste-based discrimination, neighbor discrimination is rooted in profit maximization. It is therefore more likely to persist and probably more robust to anti-discrimination policies. Public housing is concentrated in deprived neighborhoods, characterized by lower-quality public goods and higher crime rates: in 2002, 28% of African immigrants lived in an area targeted by the *Zone Urbaine Sensible* program, against 6% for the whole population. The lack

of housing opportunities also impairs geographic mobility, thereby contributing to explain large residual disparities in unemployment rates as documented by [Decreuse and Schmutz \(2012\)](#), [Gobillon et al. \(2014\)](#) and [Combes et al. \(2016\)](#).

Our empirical approach belongs to the literature concerned with identifying intentional discrimination from statistical data. For example, [Knowles et al. \(2001\)](#) and [Anwar and Fang \(2006\)](#) (see also the review by [Persico, 2009](#)) attempt to distinguish racial prejudice from statistical discrimination. In a different perspective, [Charles and Guryan \(2008\)](#) focus on taste-based discrimination. We go back to the theory of discrimination and extract one specific rationale for discrimination out of the black box. The test relies on two assumptions. First, conditional on all observable characteristics of the dwelling, including location, tenants do not directly derive utility from whether the landlord owns several contiguous apartments or not. Second, building and dwelling landlords do not differ in racial prejudice. In Section 3, we describe the two kinds of landlords at length and argue that they are very similar. Although we cannot document their respective levels of prejudice, the variables usually associated with prejudice do not differ much between the two groups.

We emphasize quantity rationing in the rental market. This suits well the French rental market where there is little room for price discrimination.¹ In the US, price discrimination in the housing market has been studied since the 1960s, when the growing expansion of the African-American and Hispanic middle class was starting to modify the racial makeup of Suburbia ([Rapkin, 1966](#); [King and Mieszkowski, 1973](#)). Studies based on hedonic methodologies and geographical discontinuities show that Blacks often have to pay a premium to enter formerly all-White neighborhoods ([Yinger, 1997](#)). However, a number of audit studies and field experiments show that minority applicants also receive fewer opportunities to visit housing units. Pair-based audits highlight the role played by realtors. Using the results from an audit conducted in 1981 in Boston, [Yinger \(1986\)](#) shows that Black applicants are offered up to 30% fewer opportunities to visit housing units: two decades later, this gap narrowed but was far from having closed ([Zhao et al., 2006](#)), and it remains substantial on new media, such as websites, where agents use names as ethnic proxies. A pioneering experiment by [Ahmed and Hammarstedt \(2008\)](#) shows that Arabic-sounding Internet applicants in Sweden receive much less attention on the online rental market. [Hanson and Hawley \(2011\)](#) confirm this finding for African-Americans. The latter study also concludes that discrimination is more severe for units that are part of a larger building, a finding that resonates with our paper.

The notion of spatial externality is at the core of the paper and is related to the literature on residential segregation. For example, [Cutler and Glaeser \(1997\)](#), building upon [Schelling \(1969\)](#) tipping model, coined the term “decentralized racism” for Whites willing to pay for living in predominantly white neighborhoods. When living in dense areas, the closest neighbors are those next door and here the considered externality is limited to the building. This very local externality is what makes neighbor discrimination different from other contexts of customer discrimination.

Our model is derived from the theoretical literature on labor market discrimination in frictional environments. This literature is mostly focused on employer discrimination. While discrimination only affects wages in a frictionless environment, the combination of search frictions and hiring discrimination translates into higher unemployment probability ([Black, 1995](#); [Bowlus and Eckstein, 2002](#); [Rosen, 2003](#); [Lang et al., 2005](#)). We study a related type of quantity rationing in the

¹ The asked rent is generally posted on the ad and landlords are not allowed to increase it unilaterally before signing the lease. A set of laws and regulatory practices prevents them from fixing prices at will on many segments of the private rental market. Price discrimination must be covert: it may involve the amount of the security deposit (two or three months), or temporary discounts in exchange for improving the quality of the dwelling.

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