

Growth and Inequality: Identifying the Tradeoffs

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Abstract

This paper reviews recent research analyzing the growth-inequality relationship among heterogeneous agents. The primary source of heterogeneity is due to the initial endowments of physical capital, although extensions to include human capital and ability are also briefly considered. The models considered fall into three structural categories. The first is the one-sector endogenous growth model, which abstracts from distributional, as well as aggregate, dynamics. The second assumes neoclassical production and is characterized by transitional dynamics in both aggregates and inequality, enabling us to discuss both *intratemporal* and *intertemporal* tradeoffs. It introduces only one source of heterogeneity and cannot address issues pertaining to wealth and income mobility. To achieve that, requires at least two sources of heterogeneity, such as capital and ability or skills, which are introduced in a third model. An important characteristic of the framework is that the effects of any changes on the measures of inequality are path-dependent, a characteristic that has important policy implications.