

Inequality and growth: What does the transition economy data say?

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Despite an extensive literature on inequality and growth, there remains considerable disagreement on the effect of inequality on subsequent growth. This paper attempts to empirically evaluate that relationship with data from the transition economies of Central and Eastern Europe and the Commonwealth of Independent States. One attractive feature of this group of countries is that their starting points were remarkably similar. Yet, they subsequently have experienced substantial divergence in growth rates and income inequality. Hence, this data set offers considerable advantages for investigating the inequality and growth relationship. Since the existing literature has virtually ignored transition economies, the paper fills an important gap on the theme. Our estimations indicate that the effect of inequality on growth is negative, strong, and rather robust. *Journal of Comparative Economics* 35 (1) (2007) 35–56. California State University, Fullerton, USA; University of Southern California, USA.

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7. Concluding remarks

In this paper we have reexamined various dimensions of the growth-inequality debate in the specific context of countries undergoing transition from centrally planned to market systems. While at the beginning of the transition these countries shared many similar characteristics and specifically, had low levels of income inequality, over time they diverged considerably. Hence, the transition economies provide a potentially rich experience for examining the relation between income inequality and growth.

We apply the several different specifications and estimation methods that had been employed in the literature on inequality and growth in arriving at very different conclusions even with the same data sets. In contrast to the conflicting results obtained in the earlier studies, that had included at most only three transition economies, our empirical findings for transition countries indicate a strong, negative contemporaneous growth-inequality relationship for all these specifications, estimation methods, and different inequality data sets in the short to medium run.

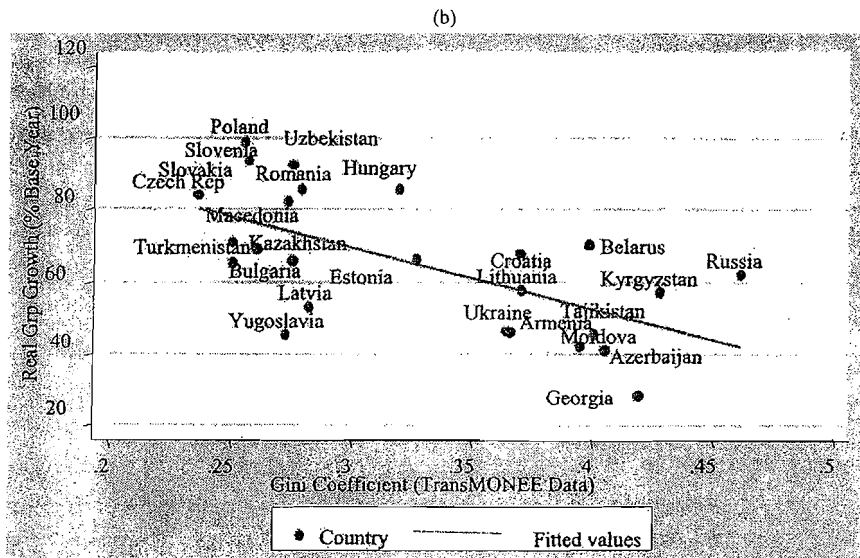
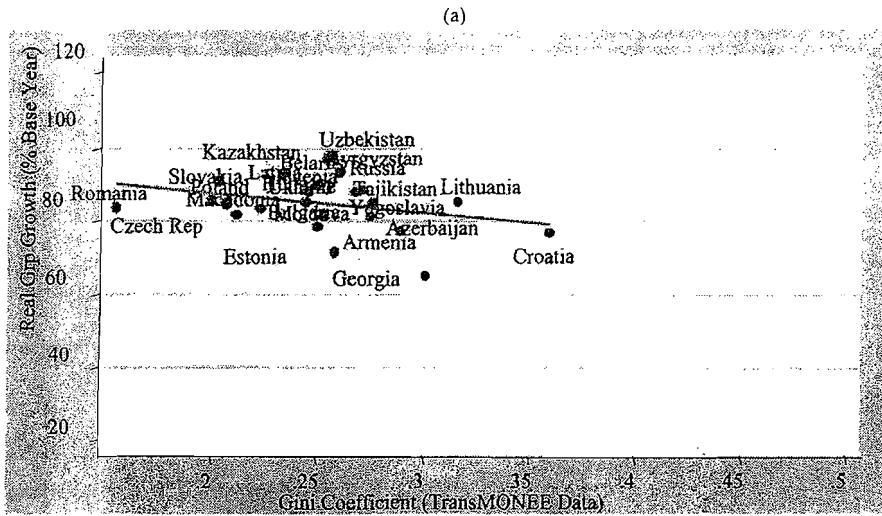


Fig. 3. Cross-country scatter plot of inequality, Gini coefficient, and growth by transitional phase. Panel (a) 1988–1992, initial phase; Panel (b), 1993–1997, stabilization; and Panel (c), 1998–2002, recovery phase of transition.

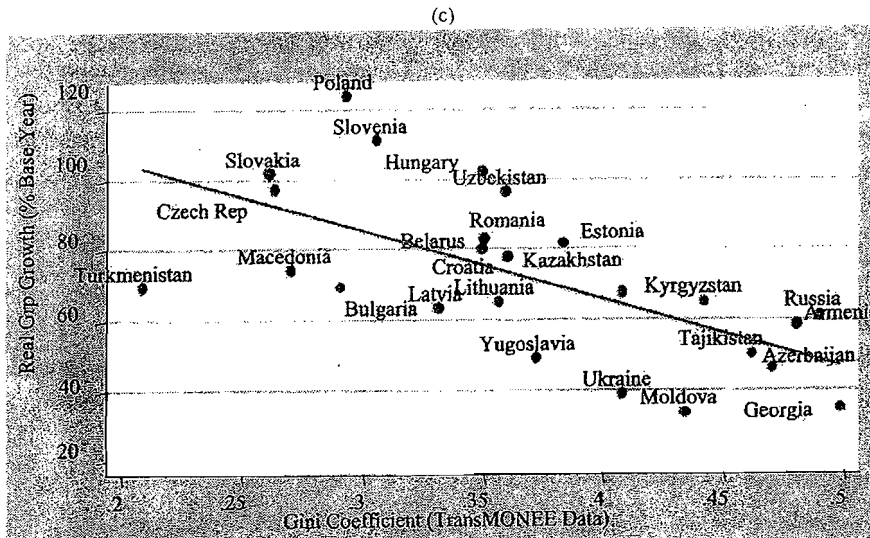


Table 1
Summary review of the empirical literature

Author	Data source	Estimation method	Specification/ Model	Inequality effect on growth	Coverage of transition economies	Accounting for nonlinearities
Persson and Tabellini (1994)	Heston and Summers (1991), Maddison (1982), World Bank (1984), other sources	OLS	Political Economy Model	Negative	None	No
Perotti (1996)	Various sources as listed in Perotti (1996)	OLS	Perotti	Negative	None	No
Alesina and Perotti (1996)	Various sources as listed in Alesina and Perotti (1996)	2SLS, 3SLS	Sociopolitical Stability Model	Negative	None	No
Li and Zou (1998)	Deininger and Squire (1996), Barro and Lee (1996), other sources	Panel, fixed effects	Lee and Zou	Positive	None	No
Barro (2000)	Deininger and Squire (1996), Barro and Lee (1996), other sources	3SLS	Barro	Whole Sample: Insignificant; Poor: Negative; Rich: Positive	Three* countries	Yes
Forbes (2000)	Deininger and Squire (1996), Barro and Lee (1996), other sources	Panel, fixed effects	Perotti (lag 1)	Positive	Three* countries	No
Banerjee and Duflo (2003)	Deininger and Squire (1996), Barro and Lee (1996), other sources	Fixed, Random Panel; First Difference; Arellano and Bond	Perotti, Barro	Inconclusive: Positive for Perotti, Mixed for Barro Specifications	Three* countries	Yes