RESEARCH NOTE

Concerning Kuznets Curves, Persistent Inequality, Inflation, and Redistribution

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The evolution of inequality and its impact on aggregate outcomes of an economy is the subject of various strands of past and contemporary economic research. The nature of how inequality changes over time, and its economic impact, is, however, still a matter of some controversy (see, for example, the survey by Zweimuller, *Empirica*, 2000). A subset of this literature that is of interest from the point of view of this paper relates to the political economy implications of inequality. Specifically, we are interested in the dynamic link between inequality and inflation, viewed from a political economy perspective.

In order to address this issue, we consider dynamic extensions of some political economy models in the literature with persistence in inequality introduced via the mechanism of intergenerational altruism (Dolmas et. al., *Canadian Journal of Economics*, 2000; Bhattacharya et. al., *Canadian Journal of Economics*, 2005). Inflation in our models is a mechanism of redistribution, and we find that the link between inequality and inflation within any period or over time depends on institutional and preference related parameters. Furthermore, we find that differences in the initial distributions of wealth can yield a diverse set of patterns for the evolution of the inflation and inequality link. In some cases, there appear to be limit cycles; the pattern for inequality resembles a series of "Kuznets curves," i.e., inequality increases and then decreases over time, and this pattern appears to repeat itself.

Interestingly, in some cases, the corresponding pattern for inflation may also be very similar. In other cases, inequality initially appears to follow a Kuznets curve type

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of pattern, and then increases again; the corresponding pattern for inflation is similar. The model also provides a political economy rationale for why the patterns of inequality can reverse over time. An implication of this feature of the model is that, depending on the data set in question, one can find either a U shaped or inverted-U shaped relationship for the dynamics of inequality, thus, providing a political economy rationale for appearance and disappearance of Kuznets curve type phenomena.