

Decentralized Allocation of Human Capital

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Abstract

The standard two-sector growth model with physical and human capital characterizes a process of material accumulation involving simple dynamics; constant long run growth is observable when assuming conventional Cobb-Douglas production functions in both sectors. This framework is developed under a central planner scenario: it is a representative agent that chooses between consumption and capital accumulation, on one hand, and between allocating human capital to each one of the two sectors, on the other. We concentrate in this second choice and we argue that the outcome of the aggregate model is incompatible with a scenario where individual agents, acting in a market economy, are free to decide, in each time moment, how to allocate their human capital in order to produce goods or to create additional skills. Combining individual incentives, the effort of a central planner (i.e., government) to approximate the decentralized outcome to the optimal result and a discrete choice rule that governs the decisions of individual agents, we propose a growth framework able to generate a significant variety of long term dynamic results, including endogenous fluctuations.