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Ms 913

"Stylized facts on the interaction between income distribution and the great recession"
By Aiginger and Guger

The paper focuses on an important subject: how income inequality during the period preceding the financial crisis may have led to that crisis. It starts with a nice concise overview of the literature in a section called 'hypothesis' which actually spells out different hypotheses. However, this does not lead to the precise formulation of one or more hypotheses to be tested in the rest of the paper. This seems to work instead on a rather broad notion of testing the correlation between a composite output indicator representing the effects of the crisis on the one hand and on the other hand, first, an equally composite indicator of the level of inequality preceding the crisis, and, next, a composite indicator of the preceding change in the level of inequality. When no serious correlation is found the paper first discusses correlations using two separate elements used for the composite inequality indicators: the Gini coefficient and the wage share respectively. After that it continues discussing a mixture of method, data problems, and policy measures, and touches upon international interlinkages that may help to understand the lack of results from national-level data. As a result it tends to lose a clear line of arguing and ultimately throws up more questions than it answers.

Below this is illustrated with a number of analytical comments followed by some issues of presentation.

<u>Analytical</u>

Basic framework: Comprising countries such as China and India in the analysis necessitates two things which are absent from the paper: 1) a view on the effects of different stages of development in the sense that countries which are still expanding the monetisation of their production likely have very different growth rates which cannot be treated on a par and need correction, 2) a view on their integration in the world economy and therewith the important role of interlinkages between national economies (the mention of imbalances and of the leaking away of savings and spending show conceptual awareness but not pursued in the former case and selective in the latter case). Naturally, the second point is also relevant between developed economies only as Eurozone problems have aptly demonstrated.

Method1: a lot is made of the principal component approach to build indicators, as a way to maximise the use of information. However, it is not well explained how this proceeds and details are given for only one of the three indicators. As already mentioned the indicators are very quickly put aside to the advantage of some of their building blocks. This undermines the value that the reader can attach to the indicators.

Method2: it is not clear if GDP growth has been corrected for population growth, which differs very significantly between countries and does not affect the inequality measures at the other side of the equation.

Method3: 'low' interest rate are mentioned several times – seemingly not on a real basis (inflation tumbled in the same Eurozone countries).

Method4: the use of 'long data' (around fn 3) is not well explained and integrated though it does play a role in the argument.

Important detail with consequences: the Gini is – as the authors observe – available for accidental years only, and it is also uncorrected for the national economic cycle. From more frequent data it seems possible that inequality change may often be episodic, pointing to potential game changers; it seems questionable how the current approach could be used in such a case. In addition, the Gini is too wide to really be used as a measure of polarisation (though its development reasonably mirrors that of top income shares). The Gini is explained as referring to 'net household income' but likely it is net and equivalised household income, given the OECD as a datasource).

The relation of personal and functional distribution is suggested as an avenue for new research, without mention of existing literature (e.g. Glyn (2009) or Atkinson (2009), *Employment Outlook 2012*).

<u>Text & presentation</u>

For the easy reader the Pre-crisis focus tended to get lost as the first and only indicator table regards recent output performance. For this and other reasons the other two indicators should equally be presented. In addition, the restriction to top-10 and bottom-10 performers leaves out 15 economies comprising all major rich countries.

The text makes no direct references to the tables and graphs at all.

The first footnote appears twice; there are two typos: 'for a particular the effect' ? (p. 21) and in Note 1) for Table 2.

What is meant by 'Ranked data' ? (17, bottom line).