

Agglomeration economies and the regional policy choices of countries*

Ugo Fratesi[†]

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Abstract

This paper investigates the effects of agglomeration economies on the regional policy choices of countries.

The analysis uses a 2-country-4-region model with agglomeration economies, an immobile production factor and a mobile one, allowing the study of international capital and profit flows; moreover, different assumptions on bilateral transport costs allow to obtain results in different spatial settings.

Countries are allowed to allocate their policy efforts towards either domestic region, or a combination of the two, pursuing equity, efficiency, or a welfare function which weights both objectives.

The paper shows that concurrent and often conflicting interests co-exist, between regions and between owners of mobile production factors vs. owners of mobile ones.

Trade-offs arise especially when agglomeration economies are strong, but their emergence is also linked to two other important control variables which can affect the results: (i) the spatial settings of the economy, in particular the existence of peripheral regions, and (ii) the differences of territorial characteristics between the regions of which a country is composed or, as it is increasingly defined, the territorial capital of the regions, whose effects can be exogenously introduced in the model.

Also investigated are the international effects of regional policy, through the effects of the policy decisions of one country on the equity and the efficiency of the other one.

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[†]Politecnico di Milano, BEST, piazza Leonardo da Vinci, 32, 20133 Milano, Italy. Telephone:+39-02-2399-3966. E-mail: ugo.fratesi@polimi.it. <http://www.fratesi.net>.