Regional Equilibrium Unemployment with Agglomeration Effects

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Abstract

Patterns of unemployment considerably vary along the geographical dimension. In this article, I study the role of agglomeration effects on the dynamics of local unemployment. An original model of the regional labor market with search and mobility frictions is built. The impact of place-based subsidies and unemployment benefits crucially depends on the sign and strength of the agglomeration forces. With agglomeration productivity gains, negative regional employment shocks are amplified because profit opportunities deteriorate, inducing higher mobility out of the region. The model is able to reproduce the strong persistence of the shock on the unemployment rate and the region’s size.

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