Concluding remarks

In this book we have tried to understand the spatial structure of economic activity in the European Union (EU-15). We were specifically concerned with regional differences in unemployment rates that exist in the EU both within and across member countries. We have shown that the spatial configuration of unemployment rates cross European regions follows a quite distinct spatial pattern and closely resembles the core-periphery pattern of overall economic activity. On average, unemployment rates are low in the “European Banana”, high in the poor, peripheral “objective 1”-areas and on an intermediate level in the regions with intermediate income per capita levels.

Theoretical research about the interrelation of regional unemployment and regional economic agglomeration is astonishingly underdeveloped, given the real world relevance of these phenomena. The class of modern agglomeration theories, like ‘new economic geography’ or the ‘new trade theory’, are mostly silent on the issue of unemployment. Regional labour market theories like the wage curve-approach on the other hand leave no room to account for regional agglomeration. We have therefore developed own theoretical approaches. In chapter E we have formulated a model that combines the idea of a wage curve with a technology in spirit of the new agglomeration theories. In this model, there is an endogenous tendency for spatial concentration due to the presence of localised increasing returns to scale in combination with transportation costs. This technology spurs divergence of real income levels across regions. If combined with a wage curve based on efficiency wages, also regional unemployment disparities will open up. Central agglomeration areas will face a lower unemployment rate than backward peripheral locations. The unemployment disparities in turn lead to a magnification of real wage differences, since the low-unemployment area needs to pay a higher efficiency wage premium.

The model approach proposed in chapter E is able to account for the empirical evidence on the regional dimension of economic activity in the EU-15, because it predicts a core-periphery pattern of regional unemployment rates that resembles the spatial structure of overall economic agglomeration. The model highlights that labour mobility is not an adjustment force that leads to a gradual erosion of spatial asymmetries, like conventional neoclassical theory is implying. If the underlying production technique exhibits scale economies, internal migration leads to a perpetuation of spatial differences.

Apart from this, we identify selectivity as an additional source why labour mobility can lead to regional divergence instead of convergence. If only high skilled labour is geographically mobile, migration perpetuates rather than cures regional disparities. This is so even in a very conventional neoclassical setting with a Cobb-Douglas production function.
The constant returns to scale model that is presented in chapter F is used to analyse the implications of union wage setting for regional unemployment. We have argued that continental European labour markets are characterised by collective bargaining at the sectoral level without notable regional differentiation of union wages. Regional wage differentiation occurs through a wage drift of effective over contracted earnings. The uniformity of national union wages irrespective of regional productivity differentials, however, has implications for the spatial unemployment structure. If a single region is hit by an adverse asymmetric shock, and wages can not adjust to reflect the regional productivity level, higher unemployment results in the negatively affected region. Bad news become even worse as high unskilled unemployment spurs emigration of mobile high skilled labour out of the disadvantaged area. The blooming region on the other hand benefits from the immigration of human capital through a decrease in unemployment and an increase in effective wages for the local unskilled workforce.

Divergence trends become even more pronounced if the model structure allows both for selective labour migration and for endogenous agglomeration economies. A theoretical approach in this spirit is developed in section F6. The results of this framework can be summarized such that regional disparities get larger as migration proceeds, in particular because the group of migrants tends to include mainly high skilled workers. If a national union wage is introduced, one can show that divergence occurs not only with respect to regional wages, but also with respect to regional unemployment rates. In equilibrium, the blooming region is advantaged over the blurring one along two dimensions: it has a lower regional unemployment rate, and higher regional wages.

The model approaches from chapter F imply a spatial structure of key economic variables that is compatible with the approach from chapter E: Regional unemployment rates and wage levels are negatively correlated in equilibrium. The two theoretical models are thus complementing each other. Even though they differ to some extent with respect to their underlying assumptions and rely on different theoretical mechanisms and channels, they reach comparable conclusions, which are consistent with the observed empirical evidence. However, we have argued that the framework from chapter E is more concerned with the trans-national unemployment clusters across the European Union as a whole, whereas the models from chapter F specifically address intra-national unemployment disparities.

Throughout this book, we have largely abstained from any policy discussion and adopted a purely positive perspective. But regional economic disparities are also a great concern for policymakers. It is the declared political will that the level of territorial inequities within the EU-area shall be reduced (Art.2, Treaty of the European Community). Therefore, a vast amount of resources is spent each year by the European Commission to achieve economic and social cohesion in the EU by means of regional policy. This figure will almost surely not decrease over the
and bring along with them a dramatic increase of regional inequities within the European community.

The theoretical analysis in this book somehow supports the anxiety of policymakers that free market mechanisms alone might lead to regional divergence and more spatial inequity. Further economic integration, which e.g. leads to more mobility of labour across space, might not be an equilibrating force, but rather perpetuate existing regional disparities. But what does this purely positive statement imply for the conduct of regional policy?

We have argued at other places (Suedekum, 2002a,b) that policymakers should not draw the conclusion that centripetal agglomeration tendencies must necessarily be countervailed by means of policy. If localised increasing returns are at work in reality, there might rather be a case for policymakers to sponsor spatial economic concentration. This is so, because aggregate agglomeration advantages like those discussed in chapter D can only be realized under an asymmetric distribution of economic activity.

Furthermore, regional policy might not even be able to effectively oppose private agglomeration tendencies. As shown by Suedekum (2002b) and Martin (2000,1999), regional policies can, through secondary market adjustments, lead to actual effects that are exactly opposite to the political intentions. That is, various types of regional policy might actually lead to more instead of less territorial inequity.

The implications for public policy shall not be discussed further at this point. It should, however, be noted that one must sharply distinguish between positive and normative questions also in the context of geographical economics. This book – for good reasons, we believe – was concerned only with the positive issues.