

# **The Challenges of Ultra-Peripherality: A New Economic Geography Perspective**

**Gianmarco I.P. Ottaviano  
University of Bologna  
Brussels, 15 December 2006**

# Motivation

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## Three key questions

- Has the concept of 'ultra-peripherality' received any attention on **economic models**?
- What implications those models have in terms of the effects of **European integration** on UPRs?
- What insight do they provide on **development policies** for those regions?



# Stylized Facts

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## Ultra-peripherality

- Remoteness
- Insularity (even 'double-insularity')
- Small size
- Difficult topography
- Harsh climatic conditions
- Strong dependence on few products

# Reading through the Facts

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## Sources of asymmetries

- **“First Nature”**: Regions differ in terms of their relative abundance of natural resources, their proximity to natural means of communication, and their climatic conditions

BUT

- Dramatic differences in economic development can be observed even between areas that are not very different in terms of those exogenous attributes .



# Reading through the Facts

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## Sources of asymmetries (cont.)

- **“Second Nature”**: observed regional unbalances must be driven by some other forces that are inherent to the functioning of economic interactions

AND

- that are able to generate uneven development even across ex-ante identical places

# Reading through the Facts

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## Sources of asymmetries (cont.)

- “**New Economic Geography**”: agglomeration forces are generated by market power and increasing returns to scale (*proximity vs concentration*)
- “New” and “New-New” effects of taste shifts, technology shifts and **policy shifts**



# “New” Effects

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## Agglomeration effects

- **Product market competition** promotes the geographical dispersion of economic activities.
- International differences in **production costs** foster agglomeration in low-cost countries.
- International differences in local **market size** foster agglomeration in larger countries.

# “New” Effects

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## Agglomeration effects (cont.)

- **Trade barriers** have a non-linear impact on the balance between agglomeration and dispersion forces.
- Agglomeration forces may generate ‘**cumulative causation**’ among firms’ location decisions.



# “New-New” Effects

## Selection effects

- **Market-seeking attraction:** larger local markets are characterized by tougher competition.
- **Cost-saving attraction:** in absolute terms technologically advanced regions are characterized by tougher competition. In relative terms, regions feature tougher competition in their sectors of comparative advantage.

# “New New” Effects

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## Selection effects (cont.)

- **Accessibility:** ‘hubs’ (i.e. regions that occupy a central place within the trade network) are characterized by tougher competition.
- **Selection:** Tougher competition generates richer product variety, higher productivity, lower prices, and higher welfare.



# Implications for UPRs

## 'First-nature curse'

- **Exogenous factors ...**

remoteness, smallness, insularity, adverse climatic conditions and frequent natural disasters map into limited 'market-seeking' and 'cost-saving attraction' as well as little 'accessibility'

- **... map into endogenous outcomes ...**

specialization in a limited number of exporting products dictated by first nature (such as tourism, sugar cane and dairy products)

- **... with possible lock-in effects**

due to second nature forces

# Implications for UPRs

## Impact of trade liberalization

### ■ **Multilateral trade liberalization:**

reinforces competition in all regions. This generates richer product variety, higher productivity, lower prices, and higher welfare everywhere

... but firms may relocate to central places

### ■ **Preferential trade liberalization:**

increases productivity of insiders while decreasing the average productivity of outsiders. This translates in parallel changes in product variety, industrial activity, and welfare

... but firms tend to relocate to central places



# Final Message

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## Impact of trade liberalization

- **‘Inequality’ - Trade liberalization induces a reallocation of resources from losers to winners:**
  - from less to more productive firms
  - from smaller to larger countries
  - from high-cost to low-cost countries
  - from outsiders to insiders in preferential trade agreements

# Final Message

## Impact of trade liberalization (cont.)

- **‘Efficiency’ - Reallocations deliver long-run gains through the survival of the fittest (“selection”):**
  - higher average productivity
  - lower average prices
  - larger average firm size
  - higher profits
  - richer product variety
  - lower markups



# Final Message

# Challenging the 'first-nature curse'

- ... unlocking ‘second nature’

**‘Intensive and extensive margins’** - Strengthen traditional productions and promote new ones by targeting:

- vertically-linked production chains
- indivisible investments (specialized schools, transport infrastructures, communication networks, power facilities, commercialization and export services)
- spillovers from demonstration effects (local development as 'self-discovery')