Catastrophic Agglomeration: Indirect Evidence from the Tax Sensitivity of Firm Births*

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Abstract

A distinctive feature of recent economic geography models is their prediction of “catastrophic” agglomeration, whereby strong clustering forces can be triggered by small changes in some underlying parameters at critical thresholds. We search for evidence for the implied discontinuities in data relating the clustering intensity of industries to those industries’ sensitivity to differential tax burdens across locations. Using data on firm births in Switzerland we find that the tax sensitivity of firms’ location choices falls off sharply around a certain threshold of agglomeration intensity. This result is consistent with the jump discontinuity implied by the theory.

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