All in the mix: How establishments gain by clustering together

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Abstract

A neighborhood’s response to policies targeting business density depends strongly on the spillovers between small businesses. In this paper I build and estimate a continuous time search model of business entry where business’ profits are affected by such spillovers. I model entry as a joint decision between the potential entrant and the landlord and show that information on storefront ownership can provide useful variation to separate unobserved neighborhood attributes from spillovers, which is a fundamental identification challenge. I find that spillovers are particularly strong between businesses of the same type, with a few other strong spillovers across types. I use the estimates to answer two different questions. First, I look at how concentration of storefront ownership influences the business mix in steady state, and find that joint ownership dramatically increases the chances of the an equilibrium with higher overall profits. Second, I investigate if spillovers can sustain a permanent increase in occupancy rates following a temporary subsidy to business entry. I show that the effects of subsidies are strong in the short run, but dissipate ten years after the policy is terminated.