Productivity in a Distorted Market: The Case of Brazil’s Retail Sector\footnote{I thank the team at IBGE, the national statistical office of Brazil, for their hospitality and providing me access to the firm level data. IBGE ensures confidentiality of responses by requiring researchers to work on site at CDDI with output checked before leaving the premises. This paper benefited greatly from comments by Marcel Timmer, Carmen Pagés-Serra, and seminar participants at the University of Groningen, the IARIW conference, and the Inter-American Development Bank.}

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Abstract

In the Hsieh and Klenow (2009) \cite{Hsieh2009} model of monopolistic competition with heterogeneous firms, distortions create a wedge between the cost and marginal revenue product of factor inputs. We use census data for Brazil’s retail sector to study implications for aggregate productivity and relate distortions to regional variation in regulation using a differences-in-differences approach. We show the importance of distinguishing effects by firm size and type of distortion. Difficulty in access to credit creates distortions to capital for small firms, but has no discernible effects on medium and large-size firms. On the other hand, taxes on gross profits create distortions to output mainly for large firms. The potential gains from reallocation have not diminished during the 1996-2006 period, despite the process of services liberalization in the 1990s.

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