

Productivity in a Distorted Market: The Case of Brazil's Retail Sector¹

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Abstract

In the Hsieh and Klenow (2009) [Hsieh, C., Klenow, P., 2009. Misallocation and Manufacturing TFP in China and India. *Quarterly Journal of Economics* 124:4] 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.

Keywords: Resource allocation, Productivity, Retail sector, Brazil

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