

Political Connections and Misallocation of Procurement Contracts: Evidence from Ecuador*

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Abstract

This paper uses detailed ownership information of private firms in Ecuador and the identity of bureaucrats to document the effects of political connections on firm size and the allocation of government contracts. Reduced-form estimates show a significant positive effect of political connection on sales, assets, debt, and costs. Using contract-level data, we find that politically connected firms enjoy higher probability of winning discretionary contracts and charge higher prices for homogeneous goods and services than unconnected firms. Back-of-envelope estimates indicate a political connection premium of 475 million USD per year in overpricing. Further analysis from production function estimates suggest that politically connected firms are less efficient than unconnected ones. This translates into a 8 to 18 percent excess cost of provision.

Keywords: Corruption, contracts allocation, efficiency costs

JEL codes: D73, H72, P16

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