

WWZ Research Seminar

Faculty of Business and Economics, University of Basel

Tuesday, December 13, 2022, 12:30, S15, HG, WWZ and Zoom

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"Why do inefficient policies persist? Evidence from Energy Subsidies in Brazil" (joint with Claudio Lucinda and Noah Miller)

Abstract

Policymakers often rely on energy subsidies as a strategy for to control inflation, and transferring wealth to sub-groups of the population. Once introduced, these subsidies tend to persist in time. Taking advantage of an unexpected announcement to phase out a persistent energy subsidy in fuel markets in Brazil, we estimate its effects to Petrobras – Brazil's main oil company controlled by the government, in an event-study setting. We then embed these econometric estimates into an equilibrium model to examine the overall costs, the distributional impacts, and political economy considerations of this program.

Our central result implies that the continuation of the energy subsidy would have resulted in an overall cost to Petrobras of approximately \$18.827 billion Brazilian reais. This subsidy would have transferred approximately \$9.088 billion to consumers. For every dollar transferred to consumers via an artificially fixed lower gasoline prices, the distortionary cost of was roughly \$1, and many orders of magnitude higher than other alternative subsidies that don't protect consumers against fluctuations in international crude oil prices or cash transfers. Further, although the political coalition that supported the government would have likely benefited more from these other alternative instruments, the highly inefficient price freeze persisted, which is consistent with a policymakers with risk averse preferences for policy change.

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