

The Effects of Relaxing Entry Regulations on Prices and Welfare: Evidence from a Public Procurement Auction

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Abstract

Entry regulations are prevalent worldwide. Relaxing entry regulations can lead to lower prices but it may worsen the quality of works due to the presence of low-level new participants. In this paper, we quantify the impacts of switching from an invited auction to an open auction to investigate whether competition or relaxing entry regulations lowers the quality of works. An invited auction is a kind of the regulation of entry in public procurement while an open auction is close to the market mechanism. We obtain a unique data set including the information on the final payment and the quality score of work reviewed after the completion of work in addition to the bids and the completion time in each auction. The quality score includes the information on the performance of work in addition to the information on the completion time. Moreover, we suggest two sources of the potential benefit of introducing open auctions to analyze when introducing open auctions is more beneficial: the performance of auctions across projects of different sizes and the effects of the presence of new participants. By exploiting a policy change of introducing open auctions, we find that for large-scale projects, the switch to reduce by up to 34% in terms of the final payments because the presence of new participants induces aggressive bidding behavior in open auctions. For small-scale projects, the switch to open auctions does not lower the procurement costs. We do not show the trade-off between the procurement costs and the quality of works.

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