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The Editors
Journal of Public Economics

Dear Editors,

I am submitting “The Price of Exclusion: SME Set-Asides in Public Procurement” for consideration at the *Journal of Public Economics*. The paper quantifies a tension that the procurement-policy literature has noted but not separated: SME set-asides expand access to public contracts by removing the very bidders that discipline the auction price. The replacement is partial and expensive in markets where the protected pool cannot recreate the competitive discipline that exclusion removes.

In São Paulo’s centralized electronic procurement platform, a 2018 legal reinterpretation mechanically pushed medical and hospital supplies into SME-only tendering. I exploit the platform’s reverse-auction format to recover type-specific willingness-to-supply distributions from losing bidders’ drop-out prices under the maintained independent-private-values clock interpretation, and decompose the set-aside price change into a lost-discipline component and a protected-pool offset that combines SME entry with composition changes. In standardized non-pharmaceutical procurement, the protected pool responds (SME participation roughly doubles) but does not replace the excluded discipline: the full set-aside generates a static welfare loss of 28.9 percent of the open-regime price at a marginal cost of public funds of 0.30, with the exclusion component accounting for 72 percent of the decomposition. A 10 percent SME price preference, simulated as a static design benchmark, keeps non-SMEs inside the auction at near-zero static welfare cost while still delivering positive SME-favoring redistribution; the implied welfare weight required for a planner to prefer full exclusion is 2.42. Pharmaceutical procurement is reported as a boundary case where the protected pool is thinner, composition turnover is larger, and the welfare ranking becomes model-sensitive.

The paper sits in the welfare-anchored tradition of public-spending evaluation that this journal hosts (Marion 2007; Nakabayashi 2013; Coviello and Mariniello 2014; Coviello, Guglielmo, Lotti, and Spagnolo 2026) and connects to the broader state-effectiveness agenda (Krasnokutskaya and Seim 2011; Athey, Coey, and Levin 2013; Bosio et al. 2022; Best, Hjort, and Szakonyi 2023). The contribution is to move the comparison from average policy costs to price formation: the paper identifies which bidder pool supplies the price-forming order statistic once a set-aside excludes non-SMEs, and recasts the policy choice as a frontier between two redistributive instruments rather than a binary between SME support and no support.

I declare no conflicts of interest, and the paper has not been submitted elsewhere. Replication materials are available on request and will be deposited upon acceptance per the journal’s data policy.

Sincerely,

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