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Strategic Contributions to Induce Private Provision of a Public Good

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This paper gives an explanation why government and large contributors often make contributions to a charity in-kind rather than in cash. We consider a charity that produces a public good with a strictly convex production technology and with more than one factor of production. It cannot convert contributions made in units of a factor into other factors, but it can use cash to buy any factor. Standard results on neutrality and full crowding out break down for in-kind contributions. In-kind contributions can even lead to crowding in at the margin, and the government can increase welfare even when private contributions are strictly positive. Similar results are obtained if the charity can commit strategically to an inefficient use of contributions.