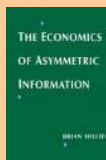


Asymmetric Information



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- It is important to distinguish between uncertain information and asymmetric information

Two Examples

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- I want to purchase health insurance
 - This is asymmetric information

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- **Neither you nor I has any particular insight into the weather**

The Health Policy

- Half the population is a good health risk, while the other half is a bad risk. For good risk patients, the right charge is \$1,000; for bad risks, \$10,000.
- How should the company price the policy?

Pricing the Policy

- While the company does not know who is a good and bad risk, people have a pretty good idea of their health.
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- In the extreme case, all good risks will decline and the company will be selling policies at \$5,500 which cost \$10,000 to service.

Pricing the Policy

- Who is a good idea of
- If the "lemon" problem
- In the company will decline and the company will be selling policies at \$5,500 which cost \$10,000 to service.

This is the classic "lemon" problem

Other Cases

- You want to switch jobs.
 - You know more about your reasons than potential employers

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 - You know more about your reasons than potential employers
- You want to borrow money
 - You know financial information not available to banks

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End

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