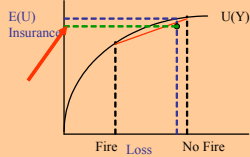


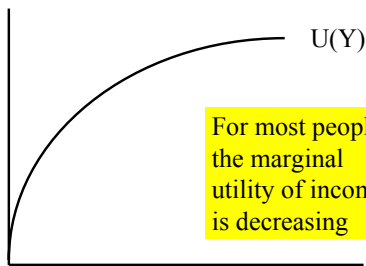
Buying Insurance



Some Cases

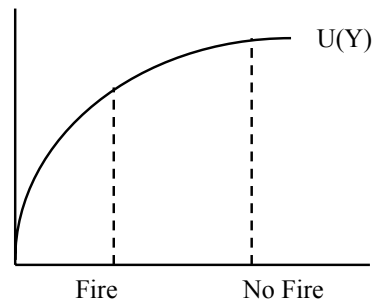
- The Case for Insurance
- How much for Insurance
- Does it always pay to buy insurance
- How much are you willing to pay to gamble?

The Case for Insurance

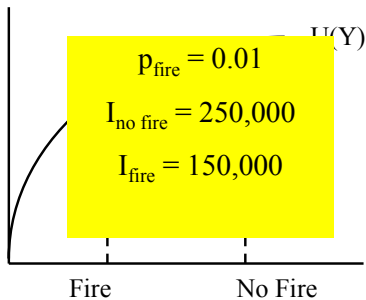


For most people,
the marginal
utility of income
is decreasing

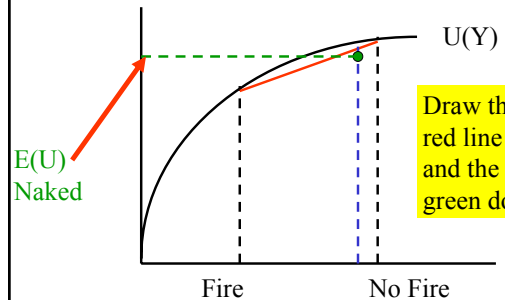
The Consequences of a Fire

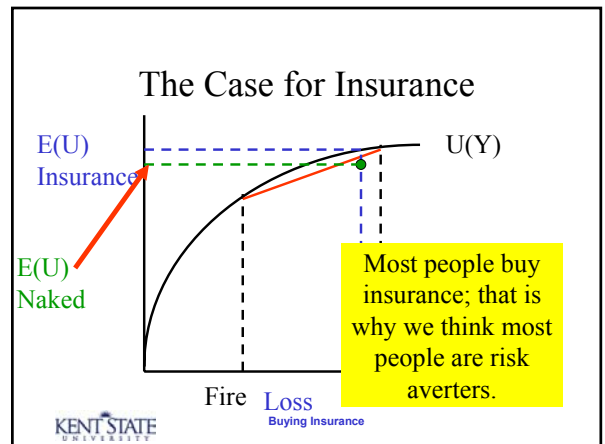
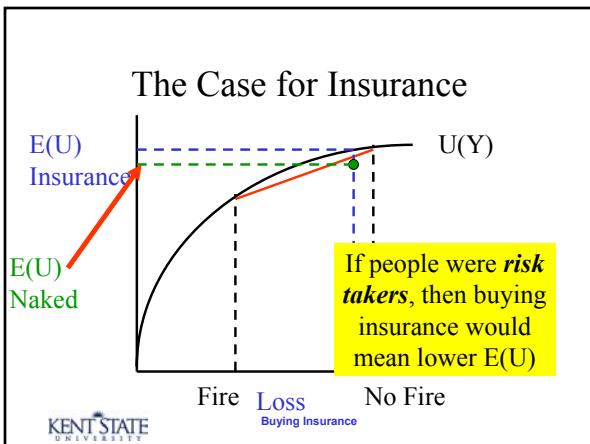
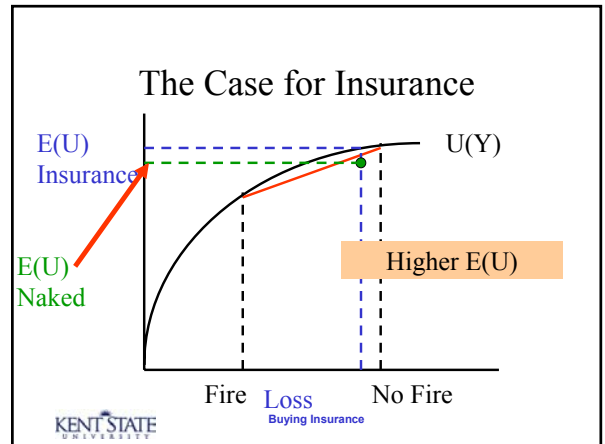
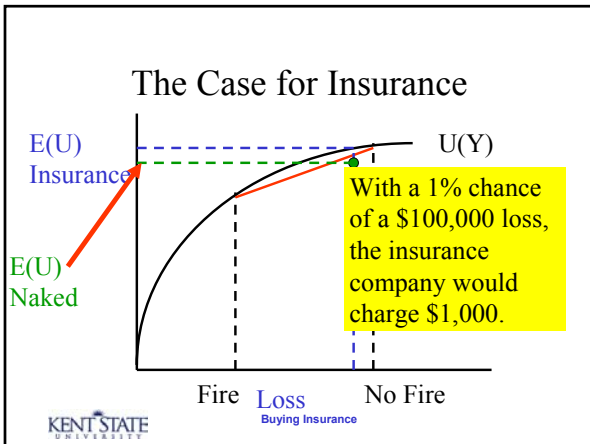
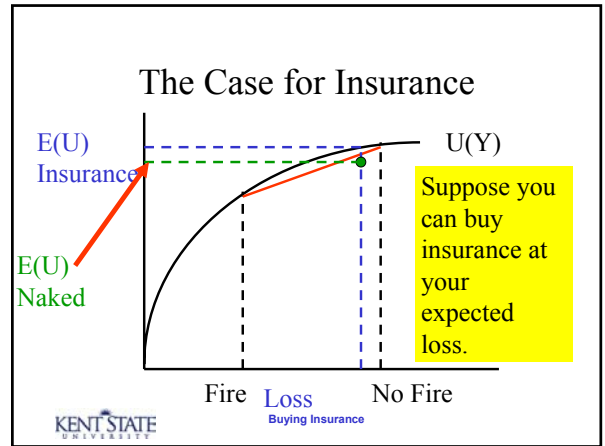
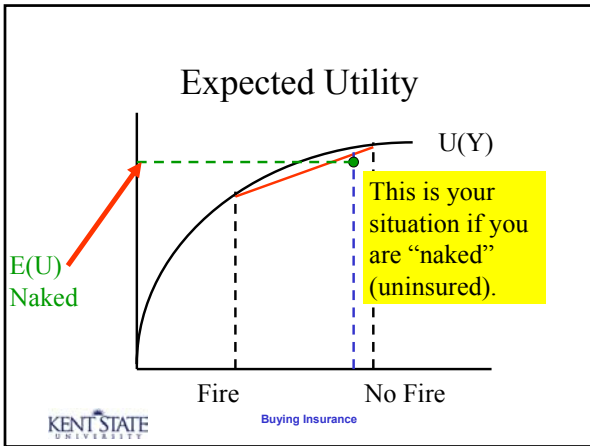


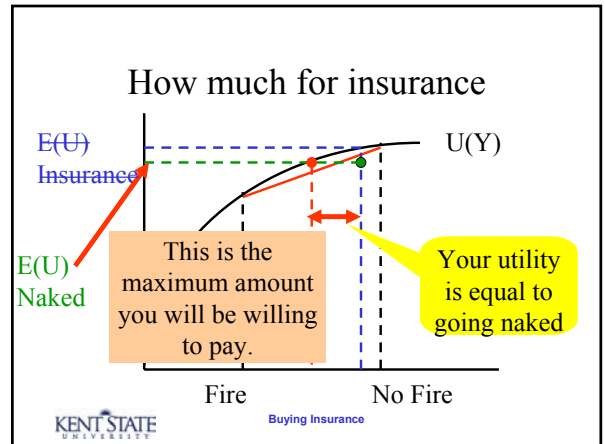
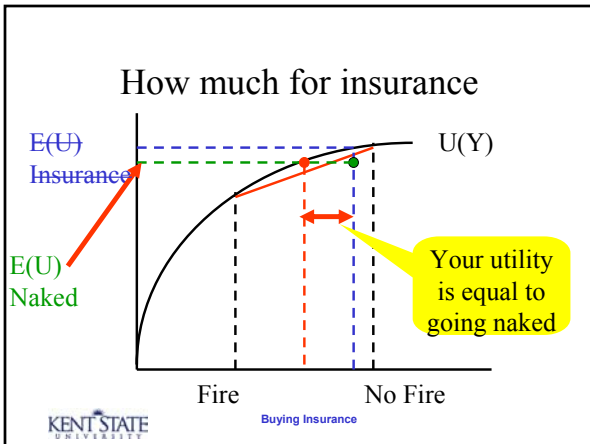
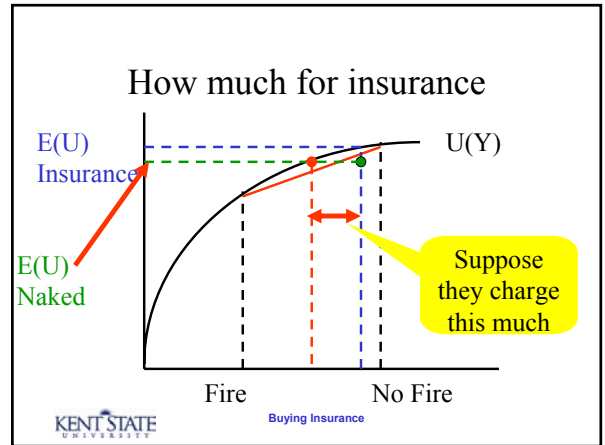
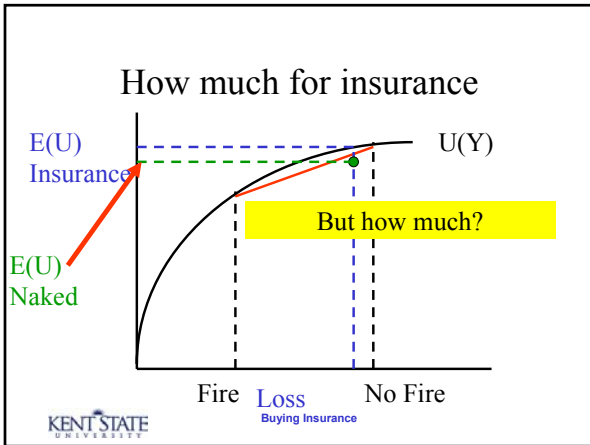
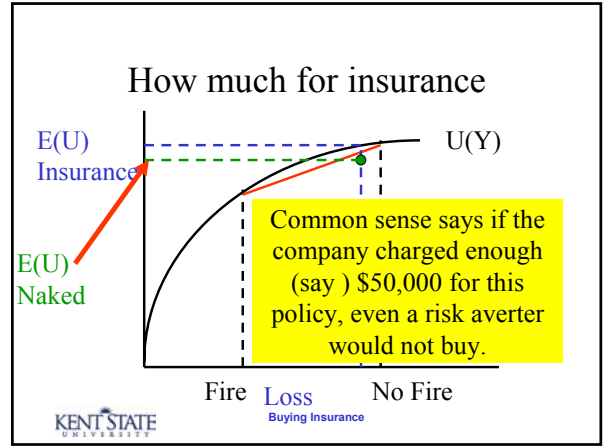
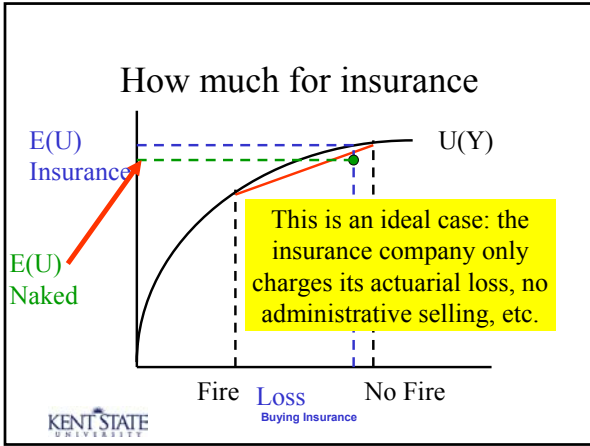
The Consequences of a Fire



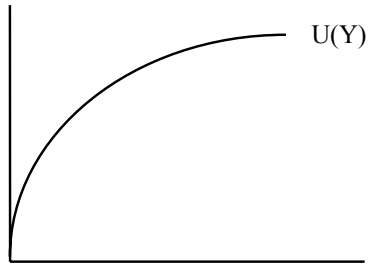
Expected Utility







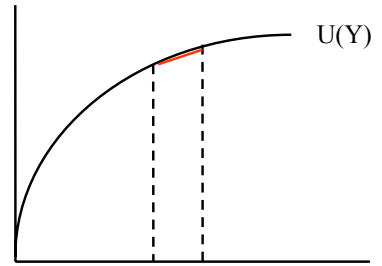
Does it always make sense to buy insurance?



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Buying Insurance

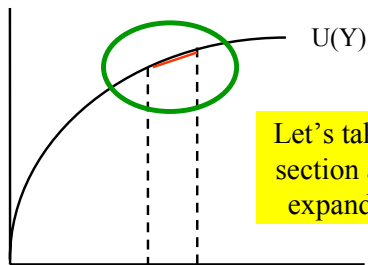
Does it always make sense to buy insurance?



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Buying Insurance

Does it always make sense to buy insurance?

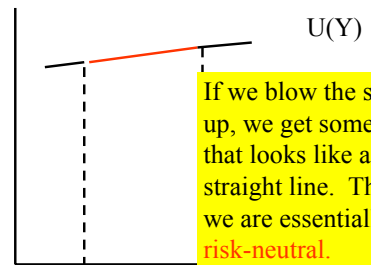


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Buying Insurance

Let's take a section and expand it

Does it always make sense to buy insurance?

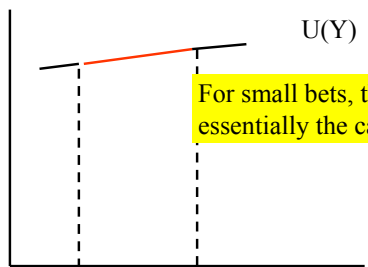


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Buying Insurance

If we blow the scale up, we get something that looks like a straight line. That is, we are essentially **risk-neutral**.

Does it always make sense to buy insurance?

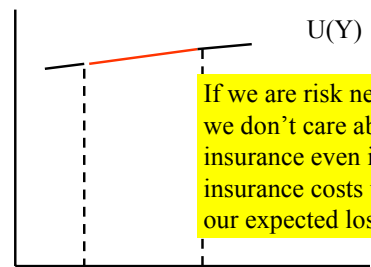


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Buying Insurance

For small bets, that is essentially the case.

Does it always make sense to buy insurance?

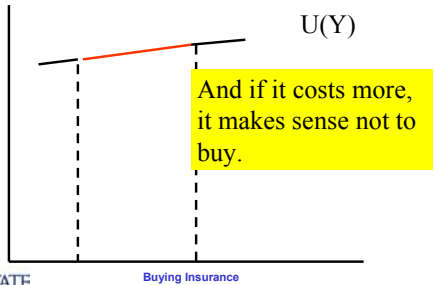


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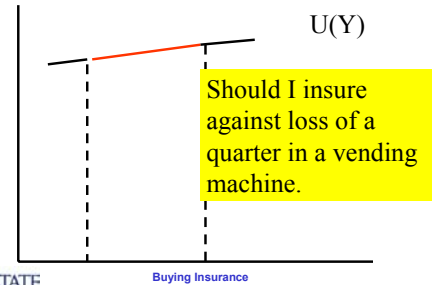
Buying Insurance

If we are risk neutral we don't care about insurance even if the insurance costs us our expected losses.

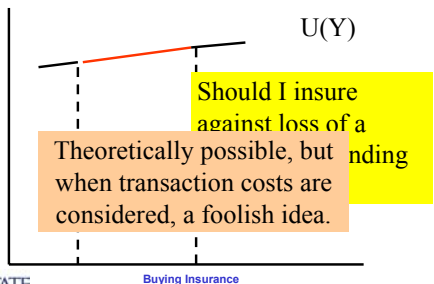
Does it always make sense to buy insurance?



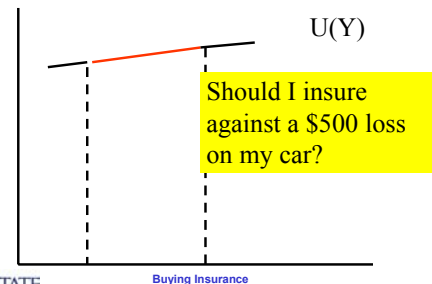
Does it always make sense to buy insurance?



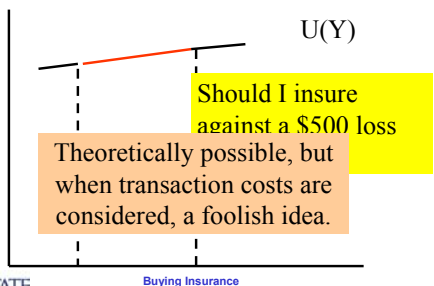
Does it always make sense to buy insurance?



Does it always make sense to buy insurance?



Does it always make sense to buy insurance?



Wagering

- Suppose you are a risk taker
- You are willing to gamble, but like a risk averter who is unwilling to pay too much for insurance, there is a limit to how much you are willing to lose.
- How much?

Wagering

- Find the red line
- Find the green dot

Gambling

If you want to gamble you must be a risk taker.

Gambling

Your utility function looks something like this.

If you want to gamble you must be a risk taker.

If you gamble

Lose

Win

Utility from staying home

Stay home

If you gamble

Lose

Win

Utility from staying home

Stay home

If you gamble

Utility from gambling

Lose

Win

Utility from staying home

Stay home

