Andreas Krause

Chapter 7.2

Credit rationing caused by moral hazard

Risk-taking by companies

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Risk-taking by companies

- Companies can choose between investments with different risks

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- Companies can choose between investments with different risks
- Banks seek to provide incentives to choose investments with low risks

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- Companies can choose between investments with different risks
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- They do so by setting loan conditions

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- Companies can choose between investments with different risks
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- They do so by setting loan conditions, the loan rate

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- Companies can choose between investments with different risks
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Company profits

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Company profits

- If successful, companies obtain their return
- $\Pi_C^i = \pi_i \left((1 + R_i) L \right.$ $\left. \right)$

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Company profits

- If successful, companies obtain their return and repay the loan
- $\Pi_C^i = \pi_i \left((1 + R_i) L - (1 + r_L) L \right)$

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- Banks are repaid the loan if the company is successful
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Bank profits

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- $\Pi_B^i = \pi_i(1 + r_L)\, L - (1 + r_D)\, L$

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Demand and supply

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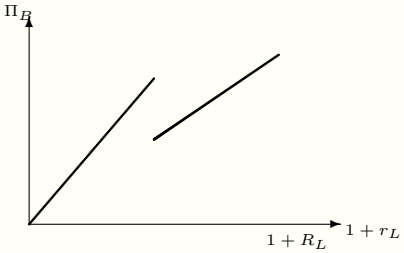

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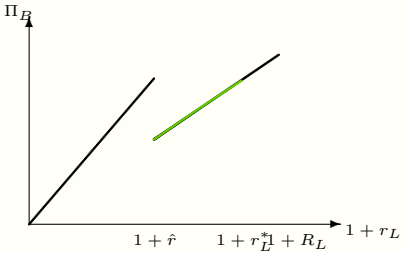

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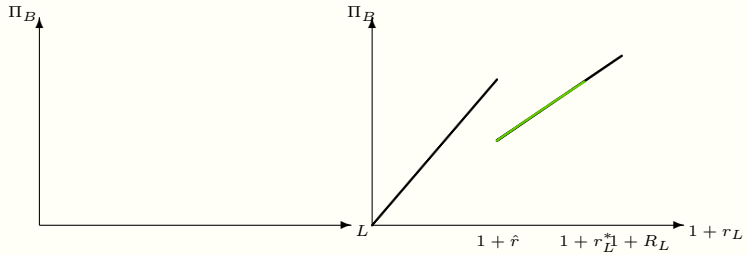

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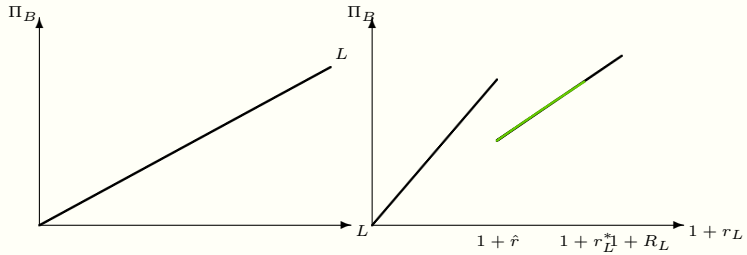

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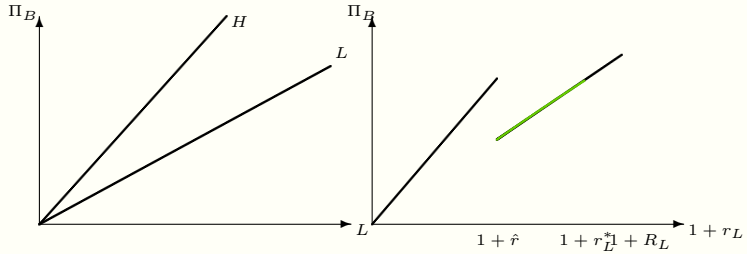

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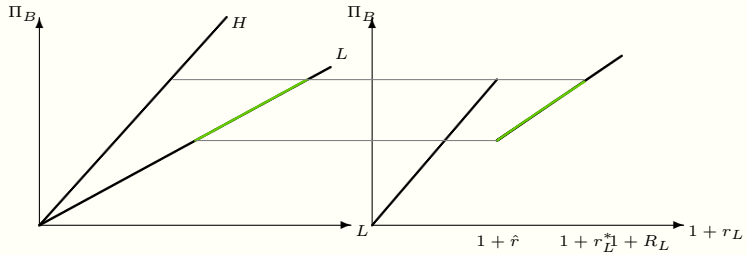

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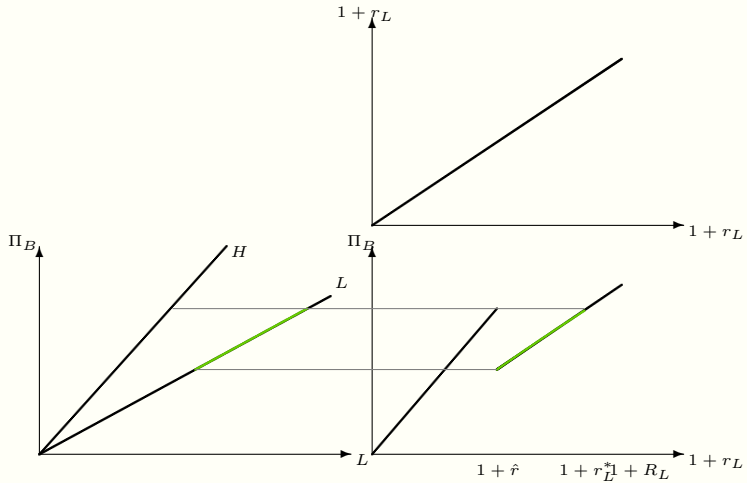

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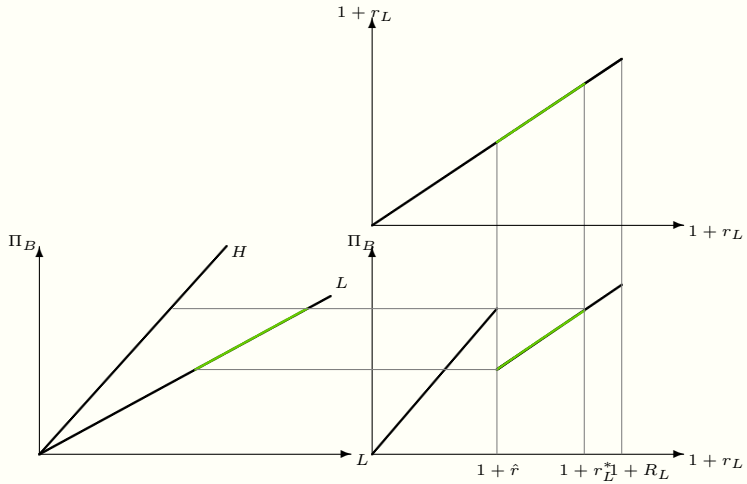

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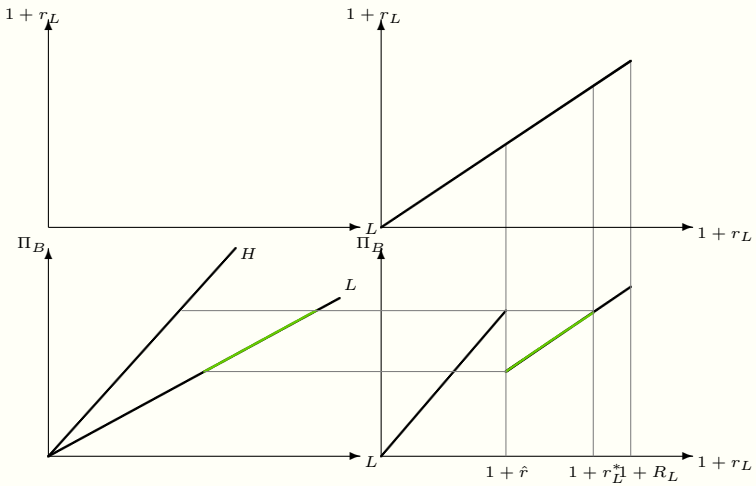

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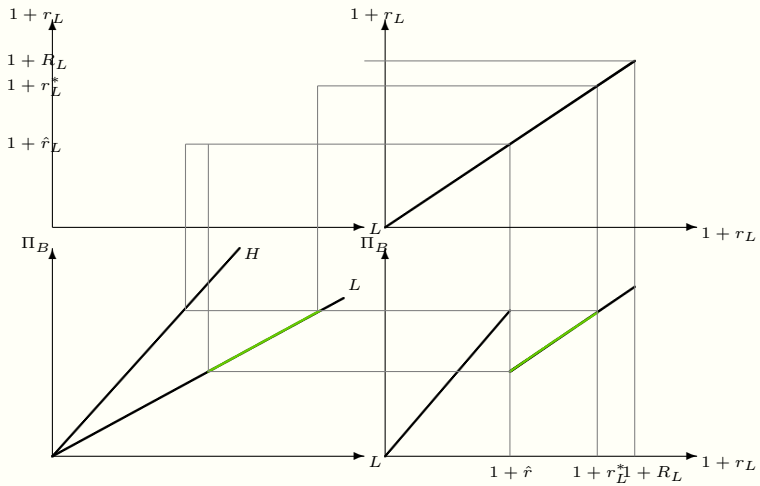

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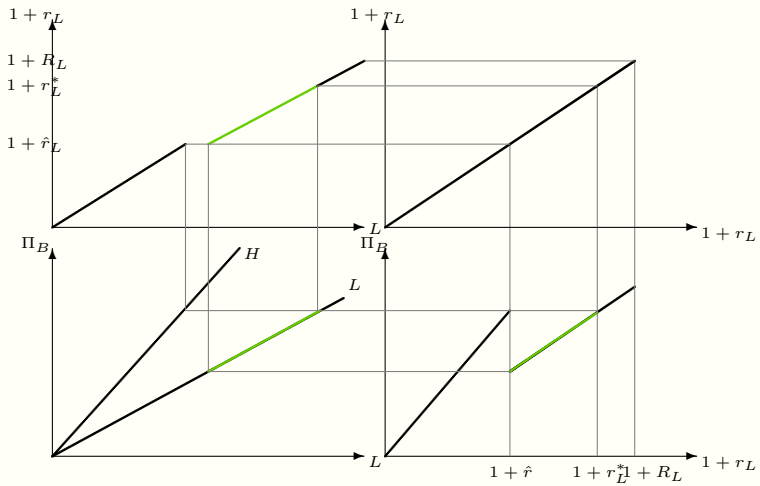

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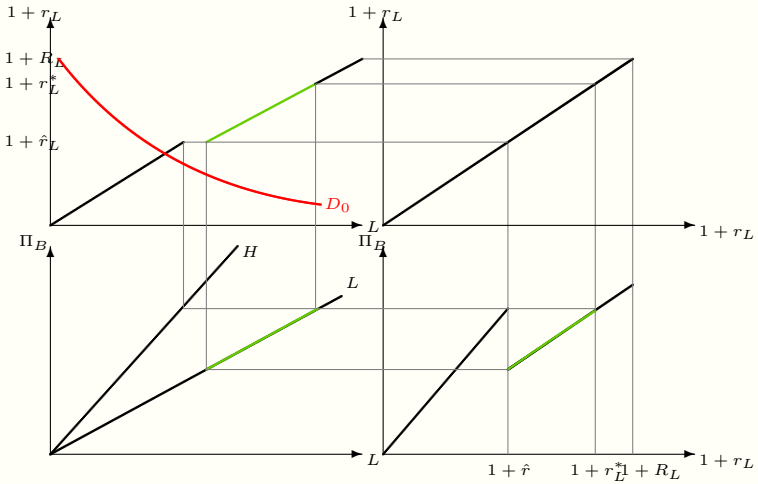

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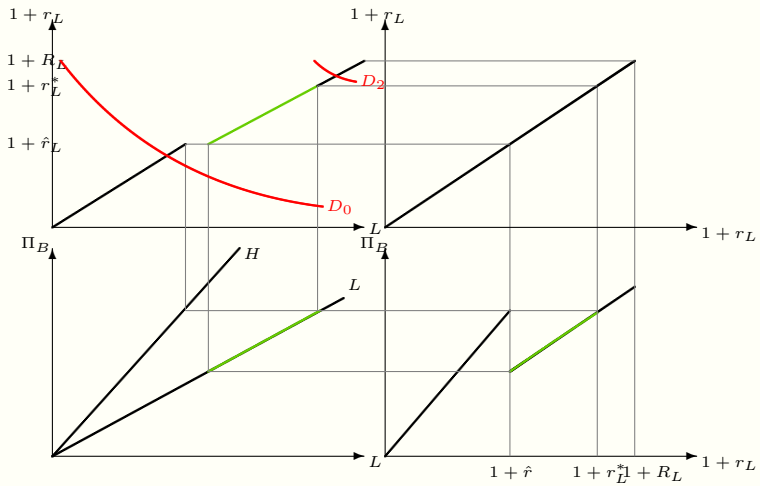

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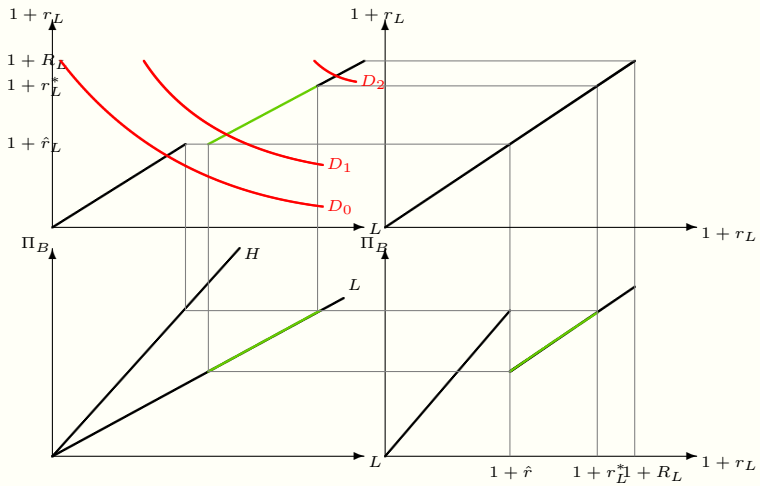

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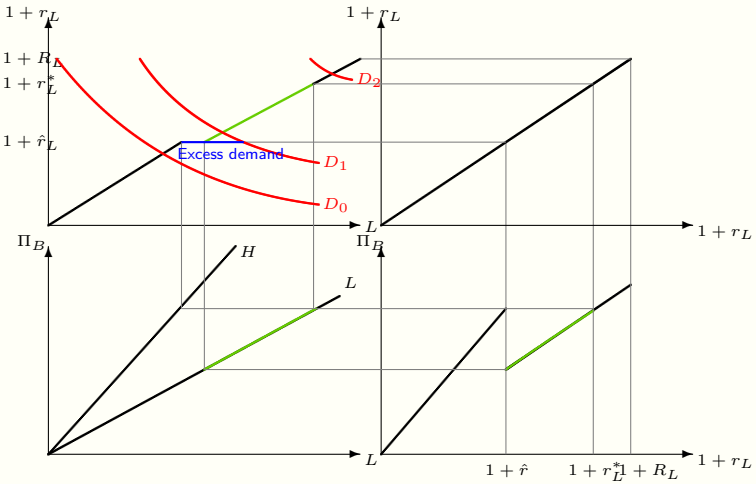

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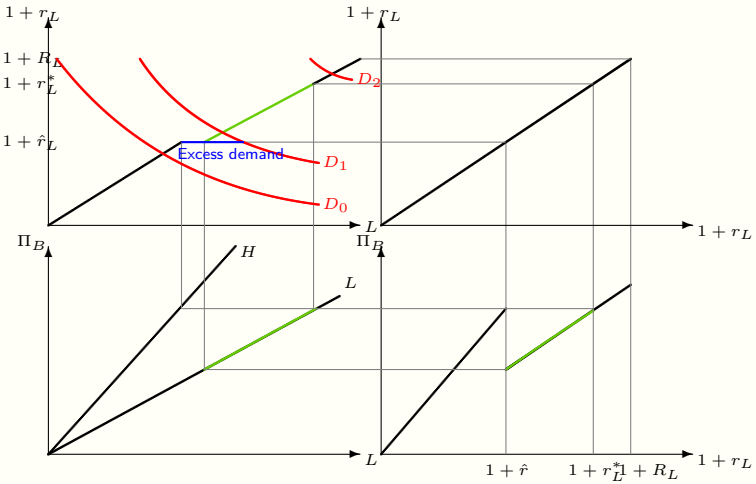

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Summary

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