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Symmetric and Asymmetric Information Modeling in Economic Growth

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ABSTRACT

This study presents a model which can be used to improve our understanding of relationships involving asymmetric information. The results show that when there is asymmetric information it is profitable to make some of the salary dependent on the outcome (to give the agent an incentive to work hard). Yet, not all the salary is outcome dependent, since the agent is risk-averse. In short, the optimal contract is the result of a tradeoff between optimal risk-allocation and optimal incentive mechanisms. The effort (and, as a consequence, the amount produced) will be lower under asymmetric information than symmetric information.

Keywords: A principal-agent problem, economic growth, symmetric and asymmetric information