

# Accepted Manuscript

Limited attention, competition and welfare

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PII: S0022-0531(18)30627-6  
DOI: <https://doi.org/10.1016/j.jet.2018.09.012>  
Reference: YJETH 4829

To appear in: *Journal of Economic Theory*

Received date: 7 March 2016  
Revised date: 24 September 2018  
Accepted date: 29 September 2018

Please cite this article in press as: Hefti, A. Limited attention, competition and welfare. *J. Econ. Theory* (2018), <https://doi.org/10.1016/j.jet.2018.09.012>

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## LIMITED ATTENTION, COMPETITION AND WELFARE\*

By Andreas Hefti<sup>†</sup>**Abstract**

This article presents a tractable framework that embeds the allocation of limited attention into competition theory. Motivated by evidence from psychology and marketing a setting is studied where firms can manipulate consumer attention and compete in prices among perceived alternatives. The introduction of limited attention changes the positive and normative predictions obtained from otherwise standard models, such as Salop-style competition. Further, the model identifies when limited attention is beneficial or harmful to firms, and explains why the individually rational decision to become less attentive in presence of more choice options may be catalyzed to a collective inattention trap over the market mechanism.

JEL Classification: D43, L13, D01, L11, D62, C72

Keywords: Attention; Imperfect Competition; Bounded rationality; Product Differentiation; Salience; Contest Theory

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\*This article consolidates two previous working papers “Attention and Competition” (ECON working paper, 2012) and “Attention, Competition and Obfuscation” (Working paper, 2014).

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