Accepted Manuscript

Risk sharing in the small and in the large

Paolo Ghirardato, Marciano Siniscalchi

PII: S0022-0531(18)30084-X
DOI: https://doi.org/10.1016/j.jet.2018.03.001
Reference: YJETH 4756

To appear in: *Journal of Economic Theory*

Received date: 28 August 2017
Revised date: 30 December 2017
Accepted date: 1 March 2018

Please cite this article in press as: Ghirardato, P., Siniscalchi, M. Risk sharing in the small and in the large. *J. Econ. Theory* (2018), https://doi.org/10.1016/j.jet.2018.03.001

Risk Sharing in the Small and in the Large*

Paolo Ghirardato§ Marciano Siniscalchi¶

This version March 6, 2018
First version May 2014

Abstract

This paper analyzes risk sharing in economies with no aggregate uncertainty when agents have non-convex preferences. In particular, agents need not be globally risk-averse, or uncertainty-averse in the sense of Schmeidler (1989). We identify a behavioral condition under which betting is inefficient (i.e., every Pareto-efficient allocation provides full insurance, and conversely) if and only if agents' supporting probabilities (defined as in Rigotti, Shannon, and Strzalecki, 2008) have a non-empty intersection. Our condition is consistent with empirical and experimental evidence documenting violations of convexity in either outcomes or utilities. Our results show that the connection between speculative betting and inconsistent beliefs does not depend upon global notions of risk or ambiguity aversion.

1 Introduction

Consider an exchange economy with a single consumption good and no aggregate uncertainty. It is well understood that in such an economy risk-averse and (subjective) expected-

*We thank an Editor of this journal and three anonymous referees, as well as audiences at several conferences and departments, for helpful and stimulating comments.

§DESOMAS and Collegio Carlo Alberto, Università di Torino; paolo.ghirardato@carloalberto.org. Financial support from the Italian MIUR (grant PRIN 20103S5RN3) is gratefully acknowledged.

¶Economics Department, Northwestern University; marciano@northwestern.edu.