Incentive Compatibility: Everywhere vs. Almost Everywhere

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Abstract

A risk neutral buyer observes a private signal $s \in [a, b]$, which informs her that the mean and variance of a normally distributed risky asset are $s$ and $\sigma^2_s$ respectively. She then sets a price at which to acquire the asset owned by risk averse “outsiders”. Assume $\sigma^2_s \in \{0, \sigma^2\}$ for some $\sigma^2 > 0$ and let $\mathcal{B} = \{s \in [a, b] | \sigma^2_s = 0\}$. If $\mathcal{B} = \emptyset$, then there exists a fully revealing equilibrium in which trade occurs. If $\mathcal{B} \neq \emptyset$, no such equilibrium can exist, even if $\mathcal{B}$ is of measure zero.

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