# Moral Hazard and Non-Exclusive Contracts [1]

## ABSTRACT

This paper studies equilibria for economies characterized by moral hazard (hidden action), in which the set of contracts marketed in equilibrium is determined by the interaction of financial intermediaries.

The crucial aspect of the environment that we study is that intermediaries are restricted to trade *non-exclusive* contracts: the agents' contractual relationships with competing intermediaries cannot be monitored (or are not contractible upon).

We fully characterize equilibrium allocations and contracts. In this set-up equilibrium allocations are clearly incentive constrained inefficient. A robust property of equilibria with non-exclusivity is that the contracts issued in equilibrium do not implement the optimal action. Moreover we prove that, whenever equilibrium contracts do implement the optimal action, intermediaries make positive profits and equilibrium allocations are third best inefficient (where the definition of third best efficiency accounts for constraints which capture the non-exclusivity of contracts).

[1] This is a much revised version of early work contained in a Delta-Crest Working Paper with the title 'Financial Markets, Asymmetric Information and Growth', and in Bisin-Guaitoli (1995). Thanks to Richard Arnott, Gary Becker, Peter Diamond, Jose' Scheinkman, Robert Townsend as well as Daron Acemoglu, Alberto Bennardo, Pierre Andre' Chiappori, Roger Guesnerie, Jim Peck, and seminar audiences at many universities. Financial support from the HCM program of the EEC, the Spanish DGICYT program and the C.V. Starr Center for Applied Economics is gratefully acknowledged.