

## Moral Hazard

**Moral Hazard** : a person may take higher risk decision, if he/she knows the negative consequence will fall to another party.

- It occurs when an economic agent e.g. banker make a decision in their own best interest knowing that there are potential adverse risks and that, if problems result, the cost will be fallen to other agents.
- e.g. bankers who issue a mortgage to a risky customer knowing that there is high risk of default. But the bankers are paid based on how many mortgages they sold. A default of a mortgage was a problem for their banks, not for them.
- e.g. in insurance market people who have insurance may take higher risk as they know that insurance company has to cover that healthcare treatment.

