Optimal Credit Scores Under Adverse Selection

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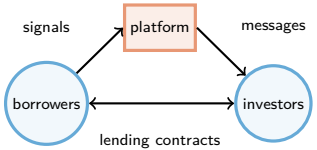
Motivation

- Better data, better outcomes in financial markets?
- If adverse selection is a major concern, not necessarily!
- How can data sharing be designed to benefit all potential borrowers?
- Selective disclosure credit scores

Model



Theoretical results

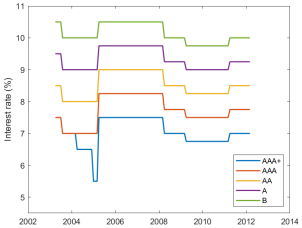
Optimal disclosure policy $\Rightarrow$ three rules-of-thumb

1. Markets with higher prices should have higher price elasticities of the expected value for investors*;
2. When signals are combined, the signal with the high full disclosure price has a low elasticity*;
3. Each message should combine one or two signals.

Empirical application

- Rural credit markets in Thailand. Thin formal segment. Extensive data from Townsend Thai Project.
- BAAC interest rate rules updates $\Rightarrow$ source of exogenous variation in interest rates
- Wager and Athey (2018) causal forests $\Rightarrow$ joint distribution of values and signals
- Full disclosure to the optimal policy: gains \$3 per household per month

BAAC Interest rate structure for farmers



Optimal policy vs full disclosure