

**Homework Assignment 8. Due: Thursday, March 30.**

1. (2 point) Describe the asymmetric information problems that an employer faces when hiring a new employee. How can this employer try to solve these problems?
2. (1 point) Explain how a sharp rise in interest rates can reduce the average quality of credit card applications?
3. (1 point) It is a well-known fact that one can get health insurance at a much cheaper price if one gets it as a part of large group (through employer, for example) as opposed to getting it individually. Why?
4. (1 point) Explain how restrictive covenants reduce moral hazard in debt contracts?
5. (2 points) Explain the relationship between return on assets and return on equity. What incentives does this relationship give a bank manager? Is this the desired outcome preferred by regulators? Discuss.
6. (2 points) Assume that a customer deposits \$1000 in her bank. Show in a T-account the effect of this deposit. If the bank is subject to reserve requirements, show in a second T-account the banks balance sheet indicating required and excess reserve. In a third T-account, show the change in the bank's balance sheet when the bank makes loans with the excess reserves.
7. (1 point) What is the impact of the Internet on asymmetric information problems?