

H4 Consulting Brief

Informed Symmetry

Many governments have an explicit or implicit objective of minimising regulatory interference and market distortions, which tends to encourage lighter touch regulatory interventions. Among these, are attempts to regulate markets by imposing obligations on parties to disclose information that would reasonably affect decisions about the fair value of a product or service. Let the buyer beware, but make it possible for them to be wary.

Most markets feature some information asymmetry. Different parties have different views about a fair price based on the information they see and some systems are unstable or prone to boom-and-bust cycles. Many free market advocates, however, object to assertive government regulation to protect vulnerable buyers. Governments, therefore, often seek to encourage efficiency, stability, and better access to information by imposing disclosure requirements on participants.

Publicly funded organisations are also exposed to risks of volatility, inefficiency, and periodic crises as lenders-of-last-resort and providers of social safety nets. Disclosure-driven regulatory strategies to reduce information asymmetry in developed markets have tended to reduce unwarranted price fluctuations.

regulatory strategies to reduce information asymmetry can work well for markets and products that are relatively straightforward



Publicly funded organisations seeking to reduce risks in complex markets need a mix of regulatory tools including, but not limited to, promoting information symmetry. More assertive regulatory tools are often needed in markets that are inherently riskier, more complex, or distorted by other government actions.

After the Great Depression, for example, many governments set up independent public institutions (central banks) to guarantee liquidity in financial markets. These institutions, somewhat buffered from political cycles, pursued monetary policy objectives by setting interest rates, acting as lenders of last resort, and imposing constraints on other lenders. Later deregulation, and failure to adequately regulate complex new financial products, contributed to more recent financial market disasters and their social costs.

Regulation promoting information symmetry—such as mandatory labelling, advertising, and disclosures—only works when products and services are relatively easy to understand and compare. With more complex products, like financial securities made up of bundled sub-prime mortgages, accurate information may be too difficult for a typical buyer to analyse and interpret.

Information symmetry strategies also work only when the information is reliable. For example, many buyers of financial securities who relied on ratings from credit agencies to assess risk ended up owning toxic assets.

Information symmetry often fails to correct distortions or risks created or exacerbated by other government actions, such as financial deregulation expanding cycles of optimism and risk-taking by sellers.

more assertive regulatory strategies are needed to balance markets and products that are risky, complex, or distorted by other government actions



Economies are more efficient when prices are fair. When unscrupulous sellers cannot extract windfall profits from 'dumb money' and more resources are directed to activities that offer the highest fair values, the whole economy benefits. Prospective buyers and competitors benefit from accurate information that is easy to access, interpret, and compare, and so can participate in markets with greater confidence. More assertive regulatory action is often warranted, however, in very risky or complex markets, where information is unreliable or difficult to understand, or where government action has already tipped the scales in favour of sellers and their lobbyists.

Advocates for free markets sometimes forget that functioning markets are a public good, guaranteed by the actions of stable and responsible governments, and that fair warnings alone do not make markets fair.

To find out more about how you can use this approach in your organisation, contact us: info@h4consulting.com.au
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