

Microeconomics, Module 24, "Risk and uncertainty" (chapter 18)

*Required reading:*

(The attached PDF file has better formatting.)

Updated: July 6, 2005

{The Landsburg textbook is excellent. We say to read certain sections and to skip others. This does not mean that certain sections are better; it means that the homework assignments and exam problems are based on the sections that you must read for this course. Some of the skipped sections are fascinating, but they are not tested.}

Read section 18.1, "Attitudes towards Risk," on pages 593-605. This section is trivial for actuarial candidates; you learn about expected values (see page 595) and other items that you already know. Focus on the conclusions in light brown type: one page 598 at the bottom, three on page 599, and one on page 605. Know how firms differ from individuals (page 605). The final exam tests these conclusions.

Skip the sub-section on "Risk and Society" on page 606.

Read section 18.2, "The Market for Insurance," on pages 606-608, skipping the last sub-section on "Uninsurable Risks." On the Course 6 syllabus (or the Exam 8 syllabus for the CAS) you read the Bodie, Kane, and Marcus text, which has a better explanation of uninsurable risks; this last sub-section of the Landsburg text is not correct, so the final exam does not test it. The diversification is among the shareholders (or owners) of the insurance company, not among the risks.

This chapter is long, but the reading for this course is just a few pages. Most of the material in this chapter is covered in the corporate finance course and is not repeated here.