

# Competition, Commitment, and Optimal Information Disclosure

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## **Abstract**

This paper studies optimal information disclosure in dynamic economies with income risk in which an incumbent firm acquires more information about an agent's persistent type than the rest of the market. If the incumbent can commit to long-term contracts but the agent can always walk away from the contract, the optimal disclosure prescribes no information revelation to the market in order to reduce the high-income type's outside option and maximize cross-subsidization across types. If also the incumbent lacks commitment, we show that low-income types receive their full information allocation and no cross-subsidization is feasible for any public information disclosure due to adverse selection. The optimal information disclosure entails a bad signal and a partially informative good signal: the good signal is assigned to all high-income agents and to some low-income agents. The share of high-income types with a good signal determines the outside's option of the high-income agents. The profit obtained by the incumbent in the second period due to its information advantage are rebated to the agent in the first period because of competition. At the optimal information disclosure, the allocation attains intertemporal consumption smoothing between the first period and the high state in the second period, hence generating an inverse of the well-known result in Harris and Holmstrom (1982). We extend the model to show how introducing agent's effort and idiosyncratic preferences over firms affect the optimal amount of information revealed to the market. Our results can be used to analyze the consequences of policy proposals like open banking.