

Figure I

Overcollateralization. The q -agents are indifferent between trading contract $(0, q)$ and trading contract (Φ_p^*, K_p^*) . The dashed line is the indifference curve of q -agents.

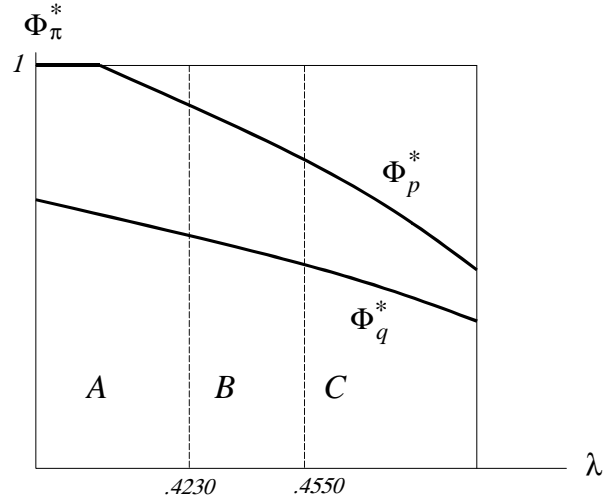


Figure II

The plot shows the optimal collateral rate, under full information, as a function of the default penalty. There are three regions. In region *A*, the full information equilibrium is not incentive compatible: agents of quality *p* would migrate to the *q*-exchange if the full information contracts were offered. In region *B*, the full information equilibrium is incentive compatible. In region *C*, the full information equilibrium is again not incentive compatible, but now the *q*-agents would migrate to the *p*-exchange if the full information contracts were offered.

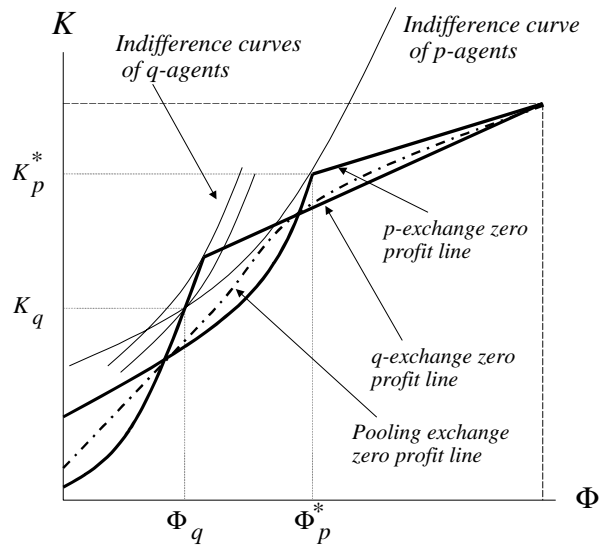


Figure III

Undercollateralization. The zero profit lines cross several times. In equilibrium, the p -agents are indifferent between trading contract (Φ_p^*, K_p^*) and trading contract (Φ_q, K_q) .

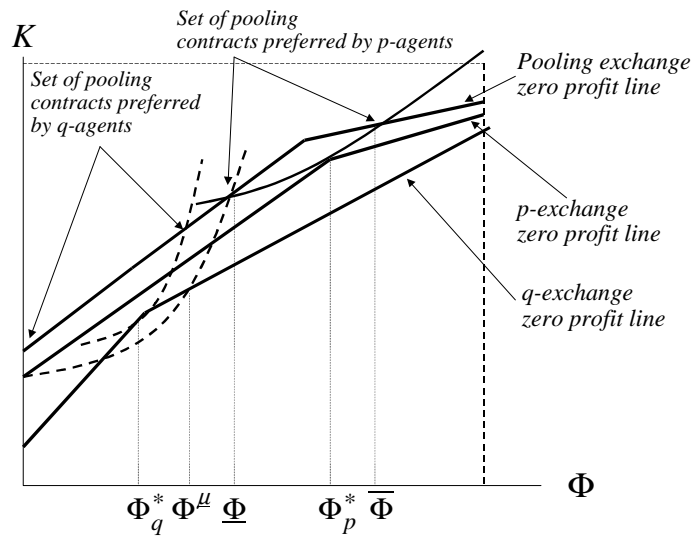


Figure IV

Impact of minimum margin requirements.