Obviousness and Risk Aversion
R&D Manager is deciding which of 2 projects to pursue

Project A
• Cost: $1M
• Chance of success: 50%
• Payoff if successful (without patent protection): $4M
  • Expected Value: $2M - $1M = $1M
• Payoff if successful (with patent protection): $6M
  • Expected Value: $3M - $1M = $2M

Project B
• Cost: $1M
• Chance of success: 10%
• Payoff if successful (without patent protection): $25M
  • Expected Value: $2.5M - $1M = $1.5M
• Payoff if successful (with patent protection): $37.5M
  • Expected Value: $3.75M - $1M = $2.75M
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If neither can be expected to lead to patent protection, manager will likely pick A -- socially inefficient.
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If only B can be expected to lead to patent protection, manager will likely pick B—socially efficient
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