Empirical Research on Sketchy Pricing: Discussion

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Terms of Engagement Today

"Sketchy" Pricing ===
Multiple margins*questionable (non-)disclosure practices

Pedagogical Approach:
- To panel's papers: take-aways, not quibbles
- Use take-aways to:
  - Highlight state of evidence (vis potential applications)
  - Identify key evidentiary gaps: "cliffhangers"
  - Motivate a new research design that would fill some gaps
  - Use this to highlight how/why policy should support R&D

Ellison and Ellison:
Take-aways and Cliffhangers

Take-aways:

- Innovation that promotes transparency may also promote obfuscation.

- Important to analyze *market outcomes* (e.g., equilibria)

Cliffhangers re: longer-run dynamics.

- Do we see an arms race between transparency engines and obfuscation strategies? What does this look like?

- If no arms race, why not?

Morwitz and Santana: Take-aways and Cliffhangers

Take-aways:
- Drip pricing matters a lot... sometimes upon sometimes. E.g.,
  - Depends on experience. Sometimes.
  - Depends on what included in base. Sometimes.
    - Drip pricing doesn't (does) affect choices if mandatory surcharges included in car (airline) base price

Cliffhangers:
- Are there regularities in how consumers respond to information/framing?
  - Not just content, but timing, source, other aspects of context?
- General challenge for models and applications of "nudging", debiasing

Busse et al:
Take-aways and Cliffhangers

- Average car buyer grasps that both new vehicle price and trade-in value affect net purchase price, and negotiates close to full offset.
- Is this offset an empirical regularity for (consumer responses to) sketchy pricing in auto purchase market? No.
  - Near opposite pattern holds on other key margin. Car buyers who pay higher margins on car also pay much higher margins on financing (and vice versa).
- Cliffhangers:
  - Can a single model of consumer choice explain multiple (seemingly disparate) phenomena?
  - What explains equilibrium and whether/how it evolves?
    - Growth (dearth?) of negotiation-free options (Saturn RIP)?
    - Growth (dearth?) of unbundled financing?

(Slightly) Bigger Picture:
Bodies of Evidence on Sketchy Pricing

- Is sketchy pricing prevalent? Prevalent enough.
- Does it affect (market) outcomes? Presumably.
- Does it create worse outcomes? Maybe. (Probably?)
- Why persist (why doesn't competition solve)? Don't really know.
- Why does it "work"? (cognitive/behavioral channels vis consumer decision making). Don't really know.
- How "work" (search, upfront choice quality, downstream usage quality)? Don't really know.
- How improve outcomes? Don't really know.
  - Many policy levers (including some less-obvious ones)
- Does intervention that improves outcomes in partial equilibrium work in general equilibrium? Don't really know.
  - Enforcement costs
  - Countervailing investments in deception
- **Overall evidentiary state: humbling**

So where do we go from here?

- A research approach
- Some policy approaches

Research Approach:
A Sketch

- One way to tackle problems with many moving parts is build theory model and test it
- A good theory yields distinct, testable predictions
- If those predictions supported can use model for equilibrium/policy analysis
- Example: Gabaix-Laibson (2006 QJE)
- Application: credit cards. Interesting economically (if not jurisdictionally to FTC?)
  - Price discrimination
  - Multi-homing
  - Intensive as well as extensive margin

Theory: Gabaix-Laibson
(As Applied to Credit Cards)

- Base price: printer (contract rate)
  - *(Could also/instead be float, teaser rate)
- Add-on price: cartridge (penalty fees)
  - *(Could also/instead be contract rate)
- Some consumers (*myopes*) don't infer that *shrouded* add-on prices are high prices
  - And/or they underestimate future use of add-on
- Why don't issuers compete by unshrouding/debiasing? Because it turns myopes into unprofitable *sophisticates*
- [Shrouded equilibrium ("curse of debiasing") more stable if:
  - Debiasing costs higher?
  - Switch costs higher? ("Thanks but no thanks effect")
  - See also Heidhues et al (2012)
  - Important to develop testable hypotheses re: innovations that would destabilize a shrouded equilibrium]

General Setup for Proposed Test in Credit Card Market

Key pieces of research design:

- Issuer willing to experiment with *debiasing* in its direct marketing
  - Or could be 3rd-party (advice provider, agency)
- On sample of consumers for whom researcher observes full set of credit card accounts
  - Via issuer's ability to pull credit reports
  - From consent obtained to do soft pulls
  - From participation in a market research panel (a la Lightspeed, Mintel) where consumers provide access to account/transaction/solicitation data
- Test hypotheses that unshrouding will:
  - Change consumer behavior: lower use of add-on
  - Be (weakly) unprofitable for issuer
  - Be unprofitable for issuer's competitors: when try to steal customers by debiasing, they simply change behavior *in their existing accounts*
  - (Does not) affect competitor shrouding behavior?
  - Effects on shopping/advice engines?

Proposed Research Design: Finer Points

- "Treatment" effectiveness on consumer choices largely unknown. Need to test different versions.
  - Focus on different add-ons (contract rate; penalty fees)
  - Information types
    - Competitor prices
    - Own prices
    - Costs based on typical usage
    - Costs based on projected usage ("our model predicts you will…")
    - Cost horizon
- Direct mail/marketing (dominant channel in card market) is conducive to debiasing research. Tight control over content:
  - Cheap to do randomized-control testing
  - With less worry than usual than information treatments are undone or diluted by high-touch marketing

Models Highlight Rationales for Government-Supported R&D

- Underinvestment in debiasing innovations: subsidize*
  - Takes costly experimentation
  - That may be unprofitable in expectation, even when socially beneficial
  - Non-excludable even when profitable: public good problem?
  - Also suggest another research design: have 3rd-party disseminate debiasing strategies to some suppliers (thru e.g., randomizing rollout timing), track all supplier responses
- Sharp tests may require outcome data from multiple providers: coordination problem
- Some innovations may rely on machine-readable data ("smart disclosure"): standards problem

- *Caveat: does debiasing R&D help deceptive R&D?

Wrapping Up

- Panel papers make important contributions
- But we still have a long way to go (vis empirical evidence-based policy)
- I suggested some meta-strategies for navigation:
  - Empirical research that focuses on theory-testing
  - Policy levers that focus on supporting R&D
- And also sketched a research design for implementing R&D in the credit card market