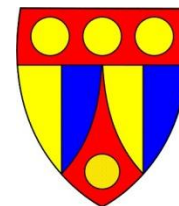


The Ethics of Price Discrimination

Juan Elegido

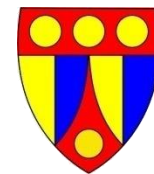


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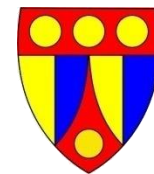
Previous article

- Elegido, J.: 2009, "The Just Price. Three Insights from the Salamanca School," *Journal of Business Ethics* (forthcoming).
- A price is fair if it is that obtainable in an open market
- I have found no published articulated argument for a more demanding standard



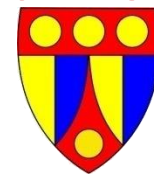
Introduction

- Price discrimination is charging different customers different prices for the same product or service
- It exists when the ratio of the prices of two similar products is different to the ratio of their marginal costs. (Stigler, 1987)
- It is pervasive
- It can have a large impact on a company's profits
- Modern technology makes it possible to practice it in ever more refined ways



Types and examples - I

- First Degree: *Personalized pricing*
 - Traditional markets
 - Nigerian lawyers
- Second Degree: *Versioning*
 - Hardcover books and paperbacks
 - Air travel: excursion and regular tickets
 - Regular sales
 - Market skimming
 - Coupons and rebates
 - *Dynamic pricing* by airlines and hotels



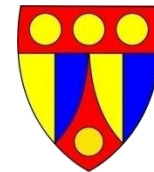
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Types and examples - II

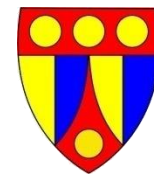
Third Degree: *sorting customers by groups*

- Different prices of laptops for small businesses, health organizations and local governments
- Different prices for male and female haircuts
- Higher discounts for new buyers of enterprise software than for older customers who are upgrading their product



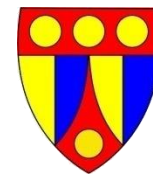
Interest for business ethics

- It is increasingly common
- Many people intuitively consider it unethical
- Most business ethics textbooks include it among unethical practices
- Economists defend it in many cases
- I have found no detailed discussion of it in the business ethics literature



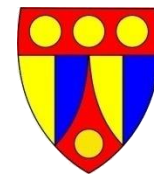
In some cases it does not seem so bad ...

- Flexible tuition scholarships in American Universities
- Discounts for students and senior citizens
- Different subscription rates to academic journals for individuals and libraries
- Cheaper prices for the same drug in poorer countries



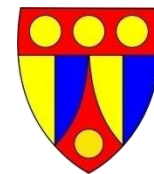
Preliminary issues

- Illegal in some countries
 - But only when it substantially lessens competition or tends to create a monopoly
- If may express contempt or dislike for a group or class
 - But the ground of this being unethical is not price discrimination itself.



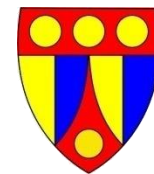
SOAKING THE RICH

A young doctor in a developing country wants to establish a medical practice in the rural community in which he was born. He can see 400 patients per month. So, to cover his costs of \$4,000 per month he should charge on average \$100 per visit. However, most people in his community can at most afford to pay \$5 per visit. An economist friend suggests to him to charge 90% of his patients only \$5 per visit, but charge \$55 per visit to the 10% of his patients who can afford to pay this amount.



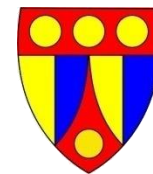
IT SEEMS A GOOD SOLUTION

- Every party is better off than if there is no clinic
- It does not even result in extraordinary profits for the doctor
- The differential pricing does not indicate less concern or lack of respect for anybody
- And yet... “some people pay more just because of who they are” (Krugman, 2000)



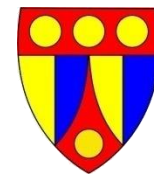
FUNDAMENTAL POINTS

- Agreement that all people deserve
 - “equal concern and respect” (Dworkin, 1977)
 - equality in regard to fundamental legal rights and freedoms, to possibilities of political participation, and to social opportunity (Gosepath, 2007)
- No contemporary philosopher of note argues for full equality of outcome in economic and social matters
- Full equality incompatible with with special relationships



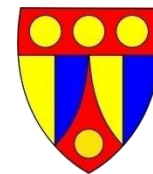
A WONDERFUL PRODUCT

A firm has developed a product that increases a car's petrol mileage, saving \$100 in petrol per can of the product. Initially the product will be marketed only in Florida and California. The firm intends to sell the product at \$60 per can in Florida and \$75 per can in California as Californian consumers are more willing to pay for new products



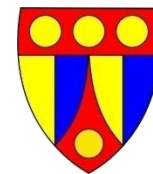
BIRTHDAY GIFTS

Assume that currently the exchange rate $\text{€}/\text{\$}$ is 1.4. Today is my birthday and, being in a good mood, I offer to sell to somebody $\text{€}10$ for only $\text{\$}5$. To a second person I offer $\text{€}10$ for $\text{\$}7$ and to a third one $\text{€}10$ for $\text{\$}10$. All three are familiar with current $\text{€}/\text{\$}$ exchange rates and they accept eagerly.



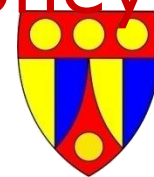
DELIBERATE REDUCTION OF QUALITY

“It is not because of the few thousand francs which would have to be spent to put a roof over the third-class carriages or to upholster the third-class seats that some company or other has open carriages with wooden benches. What the company is striving to do is to prevent the passengers who can pay the second class fare from travelling third class; it hits the poor, not because it wants to hurt them, but to frighten the rich.”
(Dupuit, 1849)



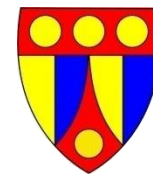
BUT...

- Price discrimination may be needed
 - To be able to offer the product
 - To reduce prices to all
 - To pay reasonable salaries or offer competitive returns to investors
- No responsibility to give customers *the very best deal possible* when this conflicts with other legitimate interests (Elegido, 2009).
- The key requirement is giving more than proportionate value for the money charged



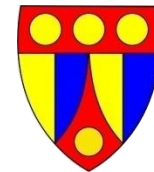
THE JOYS OF TRAVEL

You arrive in a city late at night and move into a hotel. On checking in you are told that the rate per night is \$300. You find it steep, but it is late, you are tired and outside it is raining heavily. The following morning, you strike a casual conversation with a fellow guest and you learn that he made his reservation online and is paying \$80 per night.



WRONGED?

- Fundamentally, it depends on the percentage of guests who pay that rate
- If high enough, the service the hotel gave you was worth the money you paid for it



CONCLUSION

- There is no independent ethics of price discrimination
- Provided that the price a buyer pays is lower than the value of the product or service he buys, as indicated by actual demand in an open market, that price will not be unjust
- Whether or not there is price discrimination is simply irrelevant

