
What Price Fairness?

Abstract:

In fact, dynamic pricing might already be illegal. I'm no lawyer, but it looks to me as if the Robinson-Patman Act, which outlaws price discrimination across state lines (though strictly speaking only if it hurts competition), could be invoked to prevent dynamic pricing. But it's a judgment call—one that depends on how much you value fairness versus how much you want to promote e-commerce.

Recently it came to light that Amazon has been charging different customers different prices (for movies, not books). The company insists that the price differentials were random, a way of testing the market. But many buyers accused the online retailer of tailoring its price to the consumer's characteristics. And even if Amazon's prices really were random, the outrage of those who had paid a few dollars extra suggests that "dynamic pricing" is about to become a major consumer issue, maybe even a political issue.

By PAUL KRUGMAN

Why do I buy books from Amazon.com? Location, location, location. Not Amazon's—mine. The bookstores of central New Jersey are actually better than you might expect, but London it's not.

Browsing in a physical bookstore is still the best way to find books you weren't looking for. But if there's a specific book I want, I go online. Convenience, not price, is the selling point: I would buy those books from Amazon even if I were charged a couple of dollars extra.

And maybe Amazon will charge me a few dollars extra.

Recently it came to light that Amazon has been charging different customers different prices (for movies, not books). The company insists that the price differentials were random, a way of testing the market. But many buyers accused the online retailer of tailoring its price to the consumer's characteristics. And even if Amazon's prices really were random, the outrage of those who had paid a few dollars extra suggests that "dynamic pricing" is about to become a major consumer issue, maybe even a political issue.

You see, despite that outrage, dynamic pricing won't go away. Both the nature of e-commerce—the ease with which sellers can figure out who you are and what you want—and the nature of "new economy" business in general make it almost irresistible. The only thing that is likely to stop it is government action.

Dynamic pricing is a new version of an old practice: price discrimination. It uses a potential buyer's electronic fingerprint—his record of previous purchases, his ad-

dress, maybe the other sites he has visited—to size up how likely he is to balk if the price is high. If the customer looks price-sensitive, he gets a bargain; if he doesn't he pays a premium.

To see why this is not just attractive to sellers but arguably good for the economy, look at how the publishing business works now. Books must be sold at a price well above the actual cost of producing one more copy. Otherwise the publisher couldn't cover costs that don't depend on how many books are sold—editing, typesetting and, yes, writing. But by charging, say, \$25 for a book that costs only \$3 to produce the publisher loses some potential profitable sales.

So publishers try to sort customers indirectly. Most books are offered first in hardcover, then some time later in paperback. The paperback is cheaper to produce; but mainly its lower price is a way of pulling in price-sensitive customers after the juice has been squeezed out of the well heeled and impatient.

But in the world of e-commerce, such crude market segmentation isn't necessary. When I log on to Amazon, the site offers me quite accurate recommendations—not just for books but for music, which is spooky considering that I've never bought music online. In other words, Amazon's computers have got my tastes pretty well pegged. So I'm sure similar algorithms would have no trouble figuring out which customers are likely to be repelled by a high price and which are likely to ignore it—and tailoring the prices customers are actually offered accordingly.

This would obviously be good for Amazon. But it would also be good for the overall book business. Publishers would be willing to publish more titles, book buyers who would otherwise have delayed their purchase until the thing came out in paper would be spared the wait. And it would be good for any other business with high fixed costs (it's expensive to offer the thing at all) but low marginal costs (it's cheap to satisfy one more customer)—a combination that has become ever more common as we have moved from an economy that mainly made physical things to one that increasingly deals in digital embodiments of ideas.

But dynamic pricing is also undeniably unfair: some people pay more just because of who they are.

In fact, dynamic pricing might already be illegal. I'm no lawyer, but it looks to me as if the Robinson-Patman Act, which outlaws price discrimination across state lines (though strictly speaking only if it hurts competition), could be invoked to prevent dynamic pricing. But it's a judgment call—one that depends on how much you value fairness versus how much you want to promote e-commerce.

One thing is clear: The next battle in the eternal conflict between equity and efficiency may well be in cyberspace.

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