

Content and telecom pricing in history and in the war for eyeballs

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Main points:

- ◆ growing opportunities for fine-grained charging and price
- ◆ strong public opposition limits deployment of such practices
- ◆ bundling, flat rates, ..., and especially personalized bundles offer a compromise that conceals sellers' motivation and practices

Underlying trends:

- incentives to price discriminate are increasing
- technology to price discriminate is improving
- privacy will be victim, since it inhibits price discrimination

Price discrimination likely to be most notable feature of *The New Economy*

Open architecture vs. drive to price according to value:

[Alexander Graham] Bell should have anticipated Bill [Gates] and let someone else put in the phone infrastructure while he collected by the minute and distance (and even importance of the call if he could have figured a way to monitor it) in perpetuity.

email from Warren Buffett to Jeff Raikes
of Microsoft, Aug. 21, 1997

18th Century: Beverley Beck Navigation

<u>Cargo</u>	<u>Toll per Ton</u>
Sand	2p
Timber, stone, salt	6p
Iron and lead	12p

There is extensive evidence that such practices often aid society's welfare, in accordance with standard economic doctrine.

“Frictionless capitalism” vs. reality:

Dell Latitude L400 ultra light laptop listed at \$2,072.04, \$2,228, and \$2,307 on Dell Web pages (designed for state and local governments, small businesses, and health-care companies, respectively).

Wall Street Journal
June 8, 2001

What will consumers accept?

THE NEW YORK TIMES, MONDAY, JUNE 27, 2005

ALL CONSUMING

David Leonhardt

Airline Tickets Can Be More in June Than in January. But Soda? Forget It.

REMEMBER the plan to charge more for a Coke on a hot day?

services at McKinsey & Company, the consulting firm. "Those are the situations



“Where companies get in trouble is where they base it purely on supply and demand,” said Mike Marn, director of pricing services at McKinsey & Company, the consulting firm. “Those are the situations where consumers really get up in arms. If you’re going to take advantage of the demand, you have to be able to say with a straight face that there’s a benefit that goes with it.”

Origins of government intrusion in U.S. business:

The demands that brought the first permanent regulatory commission to the United States resulted directly from the railroads' discriminatory pricing policies.

Alfred Chandler, Jr. *The Railroads:
The Nation's First Big Business*, 1965

Fundamental problems:

How to reconcile incentives to price discriminate with public loathing of such practices

Warning: better data collection and analysis tools are becoming available to customers

Other ways to skin the cat (other than explicit price discrimination):

Microsoft Office (for Windows 3.11)

components:

Access	\$225
Excel	\$225
PowerPoint	\$225
Word	<u>\$175</u>
Total:	\$850

Office Pro bundle: \$389

Site licensing:

# employees	value
900	\$ 0
10	\$ 10
10	\$ 20
10	\$ 30
10	\$ 40
10	\$ 50
10	\$ 60
10	\$ 70
10	\$ 80
10	\$ 90
10	\$100

1000 employees

Sales to individuals: optimal price either \$50 or \$60

revenue = \$3,000

Site licensing: revenue = \$5,500

Consumers' willingness to pay more for simple pricing:

What was the biggest complaint of AOL users? Not the widely mocked and irritating blue bar that appeared when members downloaded information. Not the frequent unsolicited junk e-mail. Not dropped connections.

Their overwhelming gripe: the ticking clock. Users didn't want to pay by the hour anymore.

Case had heard from one AOL member who insisted that she was being cheated by AOL's hourly rate pricing. When he checked her average monthly usage he found that she would be paying AOL more under the flat-rate price of \$19.95. When Case informed the user of that fact, her reaction was immediate.

'I don't care,' she told an incredulous Case. 'I am being cheated by you.'

from aol.com: How Steve Case Beat Bill Gates, Nailed the Netheads, and Made Millions in the War for the Web, Kara Swisher, 1998.

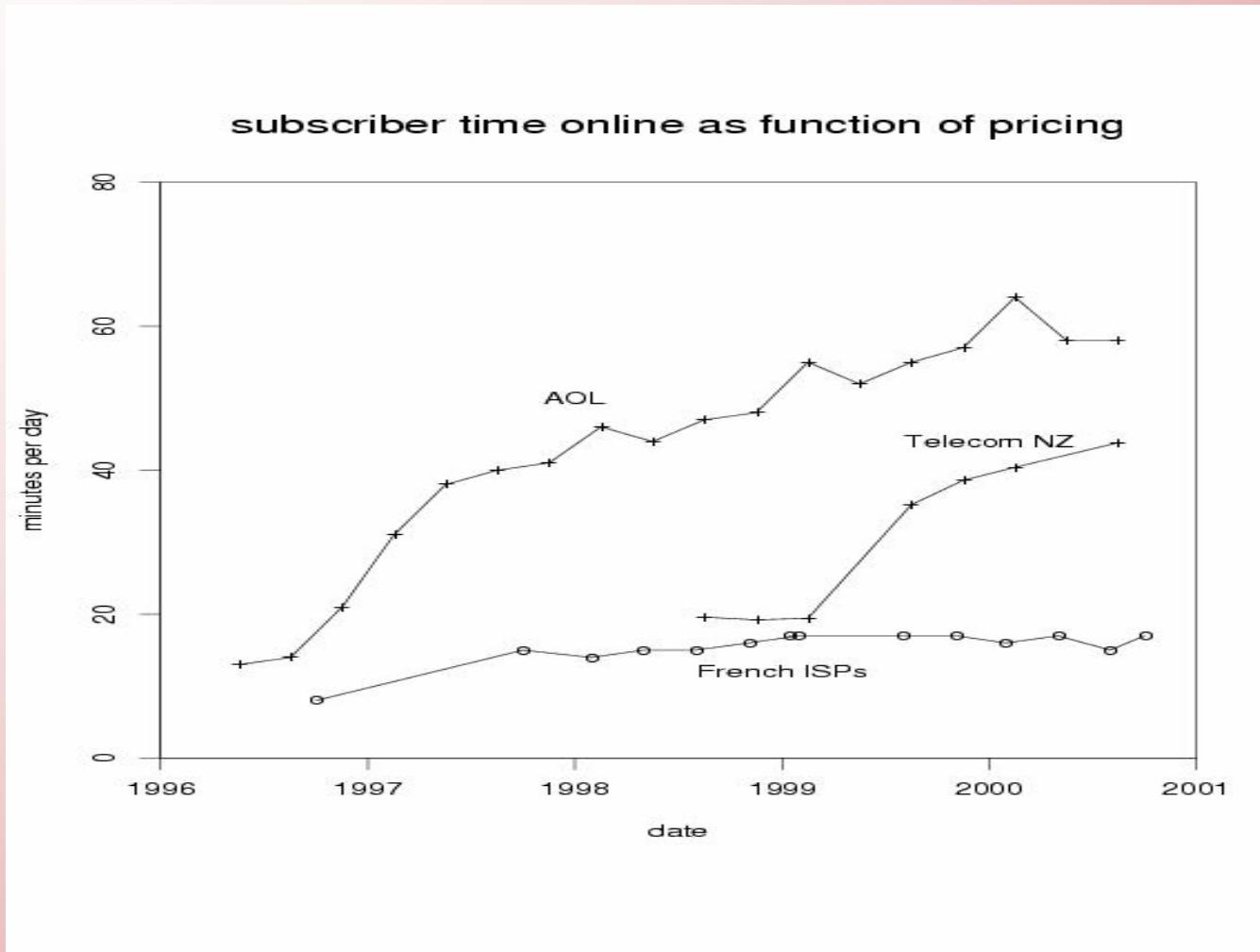
Increasing usage as key imperative:

AO, “Tragic loss of good riddance: The impending demise of traditional scholarly journals,” 1994: predicted that pay-per-view in scholarly communication doomed to fail because of the deterrents of usage charges

[Elsevier’s] goal is to give people access to as much information as possible on a flat fee, unlimited use basis. [Elsevier’s] experience has been that as soon as the usage is metered on a per-article basis, there is an inhibition on use or a concern about exceeding some budget allocation.

K. Hunter of Elsevier, 2000

Flat rates as a way to stimulate usage:



Network effects:

Although about three million computers get sold every year in China, people don't pay for the software. Someday they will, though. And as long as they're going to steal it, we want them to steal ours. They'll get sort of addicted, and then we'll somehow figure out how to collect sometime in the next decade.

Bill Gates, 1998

Conclusions:

- ◆ Expect continued tension between drive to price discriminate and public opposition
- ◆ Flat rates and bundling (ideally personal bundles) a compromise that conceals seller practices
- ◆ Expect spectrum of practices, with expensive and infrequently purchased goods subject to sophisticated pricing, inexpensive and frequently used ones covered by simple (flat rate in extreme cases) plans

Further data, discussions, and
speculations in papers and
presentation decks at:

<http://www.dtc.umn.edu/~odlyzko>

