Summary

• Internet Efficiency View
• Frictionless Commerce (Brynjolfsson, Smith) – 3 Questions
  – Online competition => lower and homogenous prices?
  – How frequently can retailers adjust their prices in response to changes in supply/demand?
  – Does brand matter for homogenous goods sold online?

Internet Efficiency View – Price competition, location irrelevant, zero economic profit, consumers have complete information.

But, we do see price dispersion…. Mention price dispersion, menu costs.
Summary

• Frictionless Commerce Results
  – Prices for homogenous goods like books, CDs lower on the Internet
  – Price changes in the online world in smaller increments than in the offline world
  – Significant price dispersion across online retailers

Mention implications – more efficient in terms of price levels and menu costs
But, price dispersion (retailer heterogeneity in terms of branding, trust responsible?)

Possible reasons for lower prices –
  lower search costs – Internet price intermediaries
  lower entry costs
  lower operational costs

Implication -> more sales through the Internet (as it is a more efficient channel)

Possible reasons for lower menu costs –
  Change a single entry in a database

Possible reasons for price dispersion –
  Bertrand marginal cost pricing result requires many assumptions –
    Products are perfectly homogenous
    Zero search costs
    Consumers have perfect information about prices
    Retailers have no spatial advantage in attracting consumers.
    “Law of One Price”

So, may be a violation of one of the assumptions?
Salop and Stiglitz models – two types of consumers –
result – some stores charge low prices
  to attract the value-conscious consumers and some
  to sell to uninformed consumers
result – some stores charge high prices

So, why do we see so much dispersion?
Also prediction of the model – the low-price store will be the sales leader. But, empirically, do we observe it? Ex. Amazon

Possible explanation –
  Heterogeneity in consumer information (due to product and retailer heterogeneity) and non-zero search costs
Summary

• *Consumer Decision-Making at an Internet Shopbot (Brynjolfsson, Smith) – 3 Questions*
  – How important is brand in determining customer choice?
  – Is brand more important for some types of consumers?
  – How do consumers react to the allocation of total price to different components?
Summary

• CDIS Results
  – Branding can be important even for homogenous goods.
  – Branding assumes different levels of importance for different consumers.
  – Branding especially important for consumers who care about non-contractible aspects of the product bundle.
  – Higher sensitivity to certain components of the price.

Reasons for price dispersion and for bypassing the lowest price –
Undercuts Kuttner article (branding very important)

Reasons for higher sensitivity to particular components of the price –
Prospect Theory (perception of unfair pricing policies) – behavioral economics

How important is branding in Internet markets for less homogenous goods?
Summary-Salop and Stiglitz

• Search Costs > 0, Equilibrium not at perfectly competitive price. Permanent price dispersion is possible.
• Informed => Uninformed (positive externality)
• Uninformed => Informed (negative externality)
• Imperfect Information => Price rigidities
• Implications for product quality, variety.