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How fitting! The influence of fence-context fit on price discrimination fairness

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ABSTRACT

Price discrimination fairness research demonstrates that the level of familiarity consumers have with a price discrimination tactic influences their fairness judgments. In this paper, the authors empirically demonstrate that these findings are not universal. Specifically, the findings indicate that the fit between the (a) variables upon which the price discrimination tactic focuses and (b) the decision criteria by which products or services offered by the firm are judged (i.e., fence-context fit) moderates the impact of the familiarity on price discrimination fairness judgments. Two experiments examine how the factors of fence-context fit and familiarity lead to different price discrimination fairness judgments and provide process evidence of a critical affective component of consumer response to price discrimination tactics based on suspicion. The findings provide implications for managers to carefully consider price discrimination policies by taking adequate precautions in an effort to reduce perceptions of unfairness.

1. Introduction

Previous marketing research demonstrates that how consumers perceive the price fairness of an offer is a critical determinant of consumer response (Campbell, 1999; Sheng, Bao, & Pan, 2007; Carlson & Weathers, 2008; Bolton, Keh, & Alba, 2010). Unfair perceptions of a price can lead to buyers having lower purchase intentions (Bolton et al., 2010; Grewal, Hardesty, & Iyer, 2004), increased intention to spread negative word-of-mouth (Ferguson, Ellen, & Bearden, 2013) and lower intentions to shop with an entity (Campbell, 1999). If they wish to create an effective pricing strategy, marketing managers must be aware of how consumers view the fairness of prices in the proposed strategy.

The majority of research in price fairness focuses upon the attribution of the price increase (Vaidyanathan & Aggarwal, 2003; Martin, Ponder, & Lueg, 2009) and how a firm justifies its price increases to all consumers (Campbell, 1999, 2007; Bolton, Warlop, & Alba, 2003). Research in this vein often examines distributive fairness, based on whether the price is more or less fair across variations in the underlying cost structures, transaction differences, or business relationship stage (Bolton et al., 2003; Bolton & Alba, 2006). Consumers also frequently interpret price fairness in light of the principle of dual-entitlement, which suggests that consumers determine a price's fairness based upon a reference price and a reference profit (Kahneman, Knetsch, & Thaler, 1986a, 1986b; Vaidyanathan & Aggarwal, 2003; Haws & Bearden, 2006). If consumers feel a price increase is based on invalid reasons, they may infer negative firm motives that create negative implications for the firm (Campbell, 1999; Grewal et al., 2004; Bechwati, Sisodia, & Sheth, 2009; Martin et al., 2009; Homburg, Totzek, & Krämer, 2014).

Despite the risks, various firms implement revenue management policies that incorporate third degree price discrimination, whereby firms selectively price higher or lower to different groups of consumers (Wirtz & Kimes, 2007; Ferguson, 2014). As described by Samuelson and Marks (2008), first degree price discrimination encompasses monopolistic pricing to sell at each individual customer's maximum price. Second degree price discrimination deals with quantity discounts. Third degree price discrimination (the focus of this research) occurs when a firm charges different prices to different customer segments. This practice is alternatively referred to in the literature as variable consumer pricing (Heyman & Mellers, 2008). For clarity and simplicity, the term price discrimination is used to refer to third degree price discrimination for the remainder of the paper. In lieu of cost structure or transactional characteristics that must be defensible to all customers relative to other prices and seller costs (e.g., Bolton et al., 2003; Bolton & Alba, 2006), these firms often price discriminate based upon factors like time of purchase, location of service, temperature, or randomized price components between different customer groups with some paying more and some less for the same product or service (Kimes & Wirtz, 2002; Heyman & Mellers, 2008). In these scenarios, consumers also consider the fairness of the price discrimination practice itself (Wirtz & Kimes, 2007; Heyman & Mellers, 2008; Ferguson et al., 2013), often based on procedural fairness (Van den Bos, Lind, Vermunt, & Wilke, 1997; Ferguson et al., 2013). While research has established many affective factors that influence distributive price fairness judgments (Xia, Monroe, & Cox, 2004; Peine, Heitmann, & Herrmann, 2009; Wu, Liu,

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Chen, & Wang, 2012; Somervuori & Ravaja, 2013), surprisingly no research has addressed the affective mechanisms through which consumer perceptions of the price discrimination tactic influence price discrimination fairness judgments. The current paper addresses these gaps by providing process evidence of the roles that familiarity, affect, and fence-context fit play in determining price discrimination fairness judgments.

2. Literature review

Price discrimination is designed to capture market surplus, which exists when some consumers are willing to pay more than others for the same product. The main motivation for firms to implement price discrimination policies is the opportunity to reap large financial gains (Agrawal & Ferguson, 2007), but such implementation does not come without risks. While price discrimination is a well-known practice in certain industries (e.g., airlines and hotels), the concept of charging different prices to different customers is largely perceived to be unfair by most customers, and often assumed to be illegal, particularly in online environments (Turow, Feldman, & Meltzer, 2005). Despite these consumer perceptions, price discrimination is legal in most cases (provided the implementation is not based on a "suspect category," such as race). Thus, many firms employ price discrimination strategies despite the risk of negative customer reactions (Haws & Bearden, 2006; Ramasastry, 2005).

2.1. Consumer perceptions of price discrimination fairness and familiarity

When evaluating price fairness, consumers may consider two distinct components of the offer—the price and the strategy through which the price is determined (Ferguson et al., 2013; Heyman & Mellers, 2008). Both components weigh external information as a strong or weak justification of the offer's pricing, but the critical information in each process varies. Distributive fairness deals with how fair consumers perceive the price to be when compared relative to others' prices, retailer costs, or retailer profit (Bolton & Alba, 2006; Campbell, 1999; Ferguson et al., 2013; Kahneman et al., 1986a, 1986b; Xia et al., 2004) and how these prices are justified to all consumers by the seller (Bolton & Alba, 2006; Bolton et al., 2003; Campbell, 2007). Essentially, this comparison explores whether the price is fair relative to other prices, costs and overall value.

When consumers evaluate the price-setting strategy, they assess whether the seller has violated social or industry norms of what constitutes a fair rule (Heyman & Mellers, 2008; Maxwell, 2002). If the pricing rule (e.g., price discrimination strategy) is viewed as fair, a price is deemed fair (Dickson & Kalapurakal, 1994), which can have a positive effect on purchase intentions (Campbell, 1999; Kukar-Kinney, Xia, & Monroe, 2007). In contrast, a price discrimination policy that is seen as unfair or a violation of community rules can lead to negative implications for the seller (Heyman & Mellers, 2008; Maxwell, 2002). Thus, rate fences, defined as "rules that a company uses to determine who gets what price and can be used to help differentiate one transaction from another," (Kimes & Wirtz, 2003, page 128) are of critical importance to any company implementing price discrimination strategies.

Consumers process a multitude of reference prices and reference transactions and compare them to a normative social standard when evaluating price fairness (Kahneman et al., 1986a, 1986b). However, as knowledge structures related to price discrimination strategies develop over time, these social and industry norms are constantly evolving. Additionally, differential Price Tactic Persuasion Knowledge (PTPK; Hardesty, Bearden, & Carlson, 2007; Pillai & Kumar, 2012) may also be important in determining consumer response. In support of the notion of knowledge evolution, price discrimination research finds that the more familiar a practice becomes either through more widespread use or a longer-lived implementation in an industry, the fairer the practice is viewed (Kimes, 1994; Kimes & Noone, 2002; Kimes & Wirtz, 2003). Consistent with these findings, the first hypothesis is:

H1. : The familiarity of a rate fence will have a positive effect on perceptions of price discrimination fairness.

2.2. The potential role of fit in price discrimination fairness

Every rate fence is based upon a variable of discrimination (VOD), defined as the specific attribute (gender, purchase time, usage time, temperature, etc.) that is used to determine differential prices between customers. One limitation of previous price discrimination research is that existing manipulations of rate fences often confound VOD (e.g., discrimination by seat location) with retail context (e.g., a sporting event). Specifically, a VOD is typically paired with the retail context most familiar to consumers (e.g., discrimination by seat location at a sporting event), rather than manipulating each variable independently. For example, discrimination by seat location could be presented with a variety of retail contexts, both familiar (e.g., a Broadway theater) and unfamiliar (e.g., a fast-food restaurant). Yet, by examining only those combinations of VOD and retail context that demonstrate the best "fit" as perceived by consumers, the extant research has ignored the possibility of interactive effects between the two variables.

As defined across several areas of marketing research (e.g., brand extensions, cause-related marketing, celebrity endorsements), fit occurs between two objects or entities when an overlap between their conceptual or perceptual attributes exists (Park, Milberg, & Lawson, 1991; Kirmani & Shiv, 1998; Bridges, Keller, & Sood, 2000; Pracejus & Olsen, 2004; Kuo & Rice, 2015). This paper posits that fit between a rate fence's VOD and retail context occurs when overlap exists between (a) the rate fence's VOD (e.g., time, color or temperature), and (b) the decisional criteria most relevant in the retail context (e.g., ice cream shop, clothing store, or theater). For example, the time at which a show begins is an important consideration for consumers purchasing theater tickets, and the current temperature will likely impact a consumer's decision to purchase a frozen dessert such as ice cream. As such, rate fences that exhibit a high degree of fit between VOD and retail context (i.e., fence-context fit) are often the combinations most familiar to consumers.

Although the construct of fit has not yet been investigated within the price discrimination literature, the broader consumer behavior literature documents the impact of fit on consumer attitudes. For example, greater degrees of fit between the attributes of a firm and potential brand extension (e.g., brand image, user base, function) lead to more favorable evaluations of the extension (Park et al., 1991; Bridges et al., 2000; Albrecht, Backhaus, Gurzki, & Woisetschläger, 2013). Similarly, a good fit between a celebrity and firm positively impacts spokesperson efficacy (Kahle & Homer, 1985; Kirmani & Shiv, 1998; Rifon, Choi, Trimble, & Li, 2004; Kang & Herr, 2006; Rice, Kelting, & Lutz, 2012), and a good fit between a firm and charity increases participation intentions during a cause-related marketing campaign (Pracejus & Olsen, 2004; Rifon et al., 2004; Kuo & Rice, 2015). Most often, fit exerts positive influence through affective mechanisms that increase fluency (Kuo & Rice, 2015), reduce skepticism (Rifon et al., 2004), or allow for associative transfer (Dimofte & Yalch, 2011). Given the robust effects of fit across various domains of consumer research, the authors propose that fence-context fit will positively impact perceptions of price discrimination fairness, even in situations where the VOD is unfamiliar to consumers (e.g., temperature-based discrimination). Conversely, the positive effects of familiarity may be negated when fence-context fit is judged to be poor by consumers. Formally:

H2a. : Fence-context fit will have a positive effect on perceptions of price discrimination fairness.

H2b. : Fence-context fit will moderate the effects of familiarity on perceptions of price discrimination fairness.