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Determinants of perceived and actual knowledge of commission paid by contributors in the pension funds industry

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Abstract This paper examines the determinants of perceived and actual knowledge of commission paid by contributors in the Chilean pension funds industry. Results show that price consciousness and brand credibility are positively associated with perceived and actual knowledge of commission paid by pension fund contributors. Results also show that financial literacy is only positively associated with actual knowledge of commission paid by contributors. Additionally, results show that price based advertising exposure is only positively associated with perceived knowledge of commission paid by contributors. This association is stronger for contributors with a high use of the price-quality cue. Based on the findings presented, implications for managers, regulators and researchers are drawn.

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Introduction

Frequently, managers, regulators and researchers use common assumptions to analyze and discuss the effects of price on the consumer decision making process, and which strategies the firms should use in order to set prices and to communicate them to customers. One such assumption is that customers know (to a reasonable degree) the prices of

the goods and services they purchase (Frank, 2006). However, studies examining customers price knowledge have revealed that while the customer may possess accurate knowledge of prices in certain categories, customer knowledge of prices varies significantly across various product categories and in some cases may be far below levels required for optimal decision making (Dickson and Sawyer, 1990; Estelami and Lehmann, 2001). Despite the practical significance of a customer's price knowledge, few studies on price knowledge are existent and most of the existing research has focused purely on manufactured goods (Estelami, 2005; Rödiger and Hamm, 2015). Published studies of price knowledge in services are far less frequently

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available and little is known about the level of price knowledge for services in general, and financial services in particular (Estelami, 2005).

In Chile, pension fund providers (*administradoras de fondos de pensiones, AFPs*) are firms with the exclusive objective of managing pension funds, along with the provision of all benefits and guarantees established by law. As a retribution for its services, these firms charge a commission to each of its contributors in order to finance its activities. A pension funds provider is required (by regulation) to charge the same variable commission over taxable salary to all of their contributors. In the Chilean pension funds industry, Hidalgo et al. (2008) demonstrated that matching the industry's price leader reduced the firm's profits, and thus diminished the firm's incentive to offer the lowest commission rates. They comment that contributors do not exhaustively search for information about commission paid nor do they evaluate commission paid in the Chilean pension funds industry. Hidalgo et al. (2008) suggest that contributors are passive information receivers. As a result, the level of knowledge contributors have about commission paid to their pension fund providers is quite limited. This lack of knowledge surrounding commission paid serves as a catalyst for creative and sometimes manipulative marketing practices. In contrast, high levels of knowledge surrounding commission paid would make a contributor capable of understanding and assessing diverse offers from pension fund providers.

Empirical evidence suggests the existence of ample variance in terms of price knowledge across both consumers and firms (Estelami et al., 2001; Olavarrieta et al., 2012; Samoggia, 2016). Consequently, how valid it is to treat contributors and pension fund providers in the same homogenous group is questionable because in practice it is likely that they both have varying important characteristics, which may have implications for the knowledge of commission paid by contributors. If these characteristics influence the knowledge of commission paid by contributors, managers and regulators need to understand those differences in order to create and to regulate pricing strategies in the pension funds industry.

This paper examines the determinants of perceived and actual knowledge of commission paid by contributors in the Chilean pension funds industry. An empirical study utilizing a survey administered through personal in-home interviews has been carried out. The study uses this data to measure the knowledge of commission paid – the dependent variable – and to estimate models of price consciousness, the use of the price-quality cue, financial literacy, brand credibility and price based advertising exposure as the explanatory variables. This approach is consistent with earlier studies on customer's price knowledge (e.g., Conover, 1986; Dickson and Sawyer, 1990; Estelami and De Maeyer, 2004; Le Boutillier et al., 1994; Olavarrieta et al., 2012; Vanhuele and Drèze, 2002). This study measures actual knowledge of commission paid, that is, what contributors actually know, as well as perceived knowledge of commission paid, that is, what contributors think they know about commission paid in the context of the Chilean pension funds industry. Both knowledge constructs were included in the study since past research has shown that what customers think they know is not always a good indicator of their actual

knowledge (Gaston-Breton and Raghurir, 2014; Mägi and Julander, 2005).

Conceptual framework

The review of the literature and the hypothesis development follows the structure of the framework shown in Fig. 1. This section reviews the literature to derive hypotheses about the effects of price consciousness, the use of the price-quality cue, financial literacy, brand credibility and price based advertising exposure on perceived and actual knowledge of commission paid by contributors in the Chilean pension funds industry.

The effects of price consciousness, the use of the price-quality cue and financial literacy on the knowledge of commission paid by contributors

Previous studies define price consciousness as the degree to which the consumer focuses exclusively on paying a low price (Alford and Biswas, 2002; Jung et al., 2014). Highly price-conscious consumers usually attempt to minimize the price paid and typically face lower price search costs due to enhanced psychological (e.g., enjoyment) and economic (savings) benefits from conducting price search than less price-conscious individuals, and therefore engage in higher levels of price search (Alford and Biswas, 2002; Kukar-Kinney et al., 2007). Consequently, highly price-conscious consumers process more price information than less price-conscious customers (Le Boutillier et al., 1994; Gauri et al., 2008). Previous studies of manufactured goods show a positive relationship between price consciousness and the level of actual price knowledge (e.g., Jensen and Grunert, 2014; Olavarrieta et al., 2012). Thus, highly price-conscious contributors could regularly beat the market, by knowing when and where to hire the services of a pension fund provider, which is derived from an accurate knowledge of commission paid by contributors. Hence:

H1. Price consciousness is positively associated with (a) perceived and (b) actual knowledge of commission paid by contributors.

Price plays two distinct roles in a consumer's evaluation of product alternatives: as a measure of sacrifice (i.e., amount of money customer must sacrifice) and as an informational cue (i.e. quality and status inference) (Völckner, 2008). Price could influence ones image or opinion of a pension fund provider. Research in pricing has established that when quality is unclear, price is used by individuals as more than a simple measure of monetary sacrifice, and is often used as a proxy for quality (Dodds et al., 1991). The complexity of the pension funds and its associated components (e.g., pension fund's assets and return on investment, customer service) further complicate the notion of quality, thereby increasing reliance on simpler quality cues, such as commission paid by contributors (Sivakumar and Raj, 1997). Although the relationship between price and quality may be a true reflection of objective quality variations, it is also often a result of the inability of the consumer to objectively determine quality using any source of information other

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