



The effect of listing price strategy on real estate negotiations: An experimental study



Eric Cardella ^{a,*}, Michael J. Seiler ^{b,1}

^a Rawls College of Business, Texas Tech University, Lubbock, TX 79409, United States

^b Raymond A. Mason School of Business, The College of William & Mary, P.O. Box 8795, Williamsburg, VA 23187-8795, United States

ARTICLE INFO

Article history:

Received 19 June 2015

Received in revised form 9 November 2015

Accepted 16 November 2015

Available online 23 November 2015

JEL classification:

R30

C70

C91

L11

PsycINFO classification:

2340

3020

3900

3920

3940

Keywords:

Listing price

Real estate

Negotiation

Flexible price

Experiment

ABSTRACT

When selling a home, an important decision facing the homeowner is choosing an optimal listing price. This decision will depend in large part on how the chosen list price impacts the post negotiation final sale price of the home. In this study, we design an experiment that enables us to identify how different types of common list price strategies affect housing negotiations. Specifically, we examine how *rounded*, *just below*, and *precise* list prices impact the negotiation behavior of the buyer and seller and, ultimately, the final sale price of the home. Our results indicate that the initial list price strategy does play an important role in the negotiation process. Most notably, a high precise price generates the highest final sale price, smallest percentage discount off the list price, and the largest fraction of the surplus to the seller, while just below pricing leads to the lowest final price, largest percentage discount, and smallest fraction of the surplus to the seller. This pattern seems to be largely driven by sellers making persistently higher and more precise counter-offers throughout the negotiation process when the initial list price is high precise. Interestingly, these effects generally attenuate with negotiating experience. Importantly, our experimental results are generally consistent, both in direction and magnitude, with the limited transactions-based empirical studies relating to real estate listing prices.

© 2015 Elsevier B.V. All rights reserved.

1. Introduction

A key decision in selling a home is selecting the listing price. Typically, this initial list price serves as the starting point in the negotiation process, a process which ultimately determines the final sale price. Given the magnitude of house prices, even a small percentage change in the final sale price can have significant financial ramifications for the seller. As a result, one of the chief aims of the seller is choosing the optimal list price that will generate the highest sale price. In making this

* Corresponding author. Tel.: +1 (806) 834 7482.

E-mail addresses: eric.cardella@ttu.edu (E. Cardella), Michael.Seiler@mason.wm.edu (M.J. Seiler).

¹ Tel.: +1 (757) 585 6100.

decision, it is imperative to understand how the choice of list price will impact the negotiation process and, consequently, the final sale price.

Although the set of possible list prices is large, since homes tend to sell for six figure amounts, real estate list prices tend to be clustered (Allen & Dare, 2004, 2006; Beracha & Seiler, 2014; Mason, Lee, Wiley, & Ames, 2013; Palmon, Smith, & Sopranzetti, 2004; Thomas, Simon, & Kadiyali, 2010). Specifically, a disproportionate number of homes tend to be listed at prices where the last three digits are 000, 500, or 900, or the last four digits are 0,000, 5,000 or 9,000. For example, Beracha and Seiler (2014) consider over 300,000 real estate transactions and document that 14% are listed with a price ending in 0,000, 16% ending with 5,000, and 35% ending in 9,000. Thomas et al. (2010) find that over 62% of the houses in their sample of over 16,000 transactions are listed with prices ending in 000. Mason et al. (2013) find that that in a sample of just over 1,500 houses listed on Zillow, over 70% have list prices with at least three trailing zeros.² Given the extensive clustering of list prices observed empirically, the motivation of this study is to shed light on how the *type* of list price impacts the negotiation process and, ultimately, the final sale price.

To do so, we develop a novel experimental design where we systematically vary the type of list price, enabling us to explore the effect of the initial list price strategy on purchase negotiations. Specifically, we study how variation in the *thousands* digit of the list price affects the negotiation behavior of buyers and sellers and, consequently, the final sale price. We consider three different types of listing price strategies: (i) *rounded*, (ii) *just below*, and (iii) *precise*. Consistent with the characterization used in Beracha and Seiler (2014), a “round” price is one where the thousands digit is either 0 or 5; “just below” is a price where the thousands digit is either 4 or 9; and a “precise” price is defined as having a thousands digit of either 1, 2, 3, 6, 7, or 8.

Within the experiment, participants engage in a stylized, bi-lateral housing negotiation. As part of the experimental design, we exogenously vary the list price strategy across treatments while holding the other aspects of the negotiation process constant. In the “rounded” (R) treatment, the list price is set to \$200,000; in the “just below” (JB) treatment the list price is set to \$199,000. For “precise” pricing, we consider two variations: the *high* precise (HP) treatment features a list price of \$201,326 whereas the *low* precise (LP) treatment features a list price of \$198,674. This systematic manipulation of the list price strategy enables us to compare outcomes across treatments to identify the corresponding effect of the list price strategy. Furthermore, we are able to observe all intermediate steps within the negotiation process including the entire sequence of offers and counter-offers, which allows us to identify how the various list price strategies separately affect the negotiation behavior of buyers and sellers. This level of investigation is not possible using transactions data because with transactions only the outcome is observable.

A small body of literature exists that focuses on the relation between types of list prices and real estate sales. Allen and Dare (2004, 2006) use transactions data from Florida and document that “charm” pricing is associated with higher final sale prices and smaller negotiated discounts off the list price, respectively. Palmon et al. (2004) use transactions data from Texas and find that “just below even” list prices are associated with lower final sale prices, compared to “even” list prices.³ Thomas et al. (2010) use transactions data from Long Island and South Florida, and find that “precise” list prices (those ending in 000) lead to higher final prices. Similarly, Janiszewski and Uy (2008) use transactions data from Florida and find that more precise list prices lead to a higher sale price to list price ratio (i.e., a lower negotiated discount). The most closely related study to ours is a recent paper by Beracha and Seiler (2014) who use data on over 300,000 residential real estate transactions in Hampton Roads, Virginia, spanning 1993–2011. The authors find that just below pricing is associated with the largest negotiated discounts. However, because just below pricing is also associated with the greatest degree of over-pricing by sellers, just below pricing leads to the greatest net proceeds to the seller. Because of the endogeneity of list price strategies, it is difficult to identify the effect of list prices on the size of the negotiated discount and the final price using empirical transaction data. By systematically and exogenously varying list price strategies, our study advances this prior empirical work by identifying the causal effect of various list price strategies on the negotiation process and the final negotiated price.

In particular, we contend that a controlled experiment affords us several advantages relative to these prior transactions-based empirical studies. First, we are able to systematically control for the fundamental value of the property being transacted, which is latent for real properties. This mitigates the endogeneity problem resulting from systematic over/under-pricing associated with certain list price strategies (e.g., Beracha and Seiler (2014), who document over-pricing of homes listed at a just below price). Second, we are able to abstract from the dimension of housing quality. Abstracting away from quality is important because with transactions data, housing quality is either imprecisely observed or not observed at all, which can lead to selection bias when estimating the effect of list prices. In other words, sellers with lower or higher quality properties may systematically gravitate toward certain list price strategies.⁴ Because the underlying quality of the property is

² As part of the same study, Mason et al. (2013) also conduct a pilot study where they ask experienced executives and MBA students to make initial price offers for goods of various prices. Their pilot study revealed that 48% of the prices were what they termed “maximally round” containing only one leading non-zero number followed by all zeros; furthermore, none of the prices were specified precisely down to the ones digit.

³ Allen and Dare (2004) define a “charm” price as a price ending in 500, 900, 4,900, 5,000, 9,000, or any other non-zero number. Hence, their characterization of a charm price does not match either of the three list price strategies we consider, and it encompasses (as a subset) what we define as just below and precise. Furthermore, their broad characterization of a charm price includes variation in all digits up to the thousands digit; thus, there is no clear way to connect our results regarding the effect of rounded, just below, or precise pricing with the results from Allen and Dare on charm pricing. Palmon et al. (2004) examine variations in the hundreds digit and characterize “even” prices as those ending with 000 and “just below even” as those ending with 900. Thus, their definitions would be along the lines of our definitions of round and just below pricing, respectively.

⁴ Palmon et al. (2004) point to such a concern by noting “selection bias might be present if sellers’ decision to list their properties at even or just-below-even prices is associated with some unobserved variables that are correlated with the inherent value of the property” (p. 129).

Download English Version:

<https://daneshyari.com/en/article/884886>

Download Persian Version:

<https://daneshyari.com/article/884886>

[Daneshyari.com](https://daneshyari.com)