

You are uninformed consumers.

- Advertised Content: “Topic on implications of asymmetric information for market performance.”
- Asymmetric Information: I know what the topic is, but you don't.
- You had to make your purchase decision in ignorance.



Uninformed Consumers

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Key Issues

- Why do we care?
- Will free markets get it right?
- Can governmental intervention improve market performance?



The Consequences of Poor Information

(why we care about
uninformed consumers)

Loss of Price Competition if Poor Price Information

- The other Diamond Paradox.

- Suppose consumers:

- have a small cost of going to the store;
 - know the distribution of prices stores charge; but
 - don't learn prices until they get to store.

- Then end up with monopoly pricing!

- Fortunately, there are other reasons for people to shop, and people do.

- Less extreme form.

- Less reason to cut your prices if other firms' customers don't see them.

Quality Information: Experience Goods

- Definition: Buyer able to judge the quality only after the good has been experienced.
- Can led to market breakdowns.
- Akerlof model of used cars.
 - Half good used cars, half bad used cars (“lemons.”)
 - At price reflecting average quality of cars, only bad cars may be offered.
 - There is no way for people with good used cars to sell them through the market.

Quality Information: Credence Goods

- Definition: Consumers cannot judge the quality even after consumption.
 - American medical care: the parking lot and television channels are what count.
- Why invest in quality if consumers can't tell?

We don't like to see consumers misled.

- Even if consumption level is efficient, there is a sense that it is bad for consumers to be misled.
- Similar to harm to competition component in antitrust welfare standard—there is a process component.

Other rationales for disclosure.

- The purpose of the [information disclosure] requirements is to facilitate effective competition in the provision of telecommunication goods and services. ... In markets where competition is limited or even absent, there are fewer checks on the conduct of the dominant firm, and customers, competitors, and potential new entrants have insufficient planning information.
- Information disclosure requirements also provide a check on Telecom's pricing conduct. ... The information disclosure requirements can assist monitoring to assess whether Telecom is making unreasonable profits, or engaging in predatory or unfair price discrimination.

http://www.med.govt.nz/templates/Page_4404.aspx

[emphasis added]

- Does second type of information have to be public?



Market Provision of Information

Hard Information, Monopoly and Skeptical Consumers

- The unraveling logic again.
 - Suppose buyer cannot observe product quality prior to purchase but knows that the seller could credibly reveal it.
 - Rational buyer will draw inferences from silence.
 - Sellers with highest quality reveal their information and unraveling takes place.

- Where does logic break down in practice?
 - Sometimes it doesn't!
 - Recommendation letters ranking doctoral students.
 - Are consumers sufficiently sophisticated?
 - Do consumers know what they don't know?
 - *E.g.*, Facebook tracks your visits to magazine web sites.
 - Soft information.

Competitive Pressure to Supply Information

- Would revelation create competitive advantage?
 - Product class versus brand effects.
 - Cigarettes and auto safety.
- Tacit collusion.
 - Repeated interaction and retaliation.
- Explicit collusion.
 - U.S. cigarette manufacturers.

What if it is hard for firm to make legally verifiable claims (soft information)?

- Reputations can sometimes be a solution.
 - Used car dealers rather than individual sellers.
 - Entry can be difficult.
 - May lead to quality premia for established firms: less price competition although not necessarily excess profits.
- Use of contingent contracts can depend on ability to verify ex post performance.
 - Contingent contracts can work as long as consumer has incentives to pursue a complaint if performance is poor.
 - *N.B.* New Zealand regulations provide for return of goods that are not of sufficient quality.

Third-Party Provision of Information

- Problems with credence goods and some experience goods suggests a role for expert ratings agencies.
- Obstacles:
 - Litigation.
 - Free-riding and other problems with the sale of information.
 - If advertiser supported, how to maintain reputation for objectivity?

User Ratings

- Many sites provide user reviews. Should we believe them?
- Ability?
 - Everyone is a critic.
- Incentives?
 - Self-promotion may be easy.
 - Steering business away from rivals can be difficult because of dilution.
 - Hence, bad reviews should have more power.
 - Evidence from Amazon books supports this view!
 - Anonymous critics raise complex privacy issues.



Disclosure Regulation

It's Hard to Do: Consumers Vary in Sophistication

- Consumers have different tastes for information.
 - U.S. regulations regarding disclosures of loan terms were found to be very confusing and unhelpful by some consumers but not others.
- Index Number Problem
 - It may be necessary to come up with a simple measure to capture many different dimensions.
 - Mobile phone price plans.
 - Loan information.

It's hard to create a simple and valuable index.

- The Credit Contracts Act required disclosure of the "finance rate" for a loan which was intended to provide a standardised measure of the credit's cost, combining interest and charges, that could be used by borrowers to compare loans.
- The Ministry of Consumer Affairs 1999 review of the Credit Contracts Act identified multiple criticisms of the "finance rate" concept which reduced its value as a source of information for consumers.
- The disclosure requirements in the CCCFA are intended to address the issues identified with the previous regime and to provide more robust and transparent information to borrowers. The provision of the annual interest rate and a clear itemisation of fees and charges applicable to a loan are intended to enable the borrower to more objectively consider loan offerings and their suitability.

It's Hard to Do: Unintended Consequences

■ Food Labeling

- Individuals consume more calories after eating “low-fat” food than “high-fat” food.
- Consumers don't like food labeled as healthy! “Low-fat soup” is less creamy than “soup.”
- Firms may lower prices of foods with “bad labels” which increases consumption by consumers who don't read labels.

■ Price information

- Transparency may facilitate collusion.
- *FCC v. MCI* on detariffing.

It's Hard to Do: Gaming

- When a public or private enterprise creates a simplified index, suppliers have incentives to “game” the index.
- Internet sellers, low-price options, and upselling.
- Universities and league tables.
- Food labeling: increase bad things missing from labels.

It's Hard to Do: So Many Dimensions to Consider

- Example: font size, weight, color, and type.
 - This is an example of why a focus on font size is misguided. (18 pt)
 - This is an example of why a focus on font size is misguided. (20 pt)

It's Hard to Do: Information Overload

You may terminate this Agreement within thirty (30) days after activating service without paying an Early Termination Fee. If you terminate after the 30th day but before expiration of the Agreement's Service Commitment, you will pay the carrier an Early Termination Fee for each wireless telephone number associated with the service. Either party may terminate this Agreement at any time after your Service Commitment ends with thirty (30) days notice to the other party. We may terminate this Agreement at any time without notice if we cease to provide service in your area. We may interrupt or terminate your service without notice for any conduct that we believe violates this Agreement or any terms and conditions of your rate plan, or if you behave in an abusive, derogatory or similarly unreasonable manner with any of our representatives, or if we discover that you are under-age, or if you fail to make all required payments when due or if we have reasonable cause to believe that your Equipment is being used for an unlawful purpose or in a way that may adversely affect our service, or if you provided inaccurate credit information or we believe your credit has deteriorated and you refuse to pay any requested advance payment or deposit.

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Desensitization

- California Proposition 65.

WARNING: This product [or area] contains chemicals known to the State of California to cause cancer or birth defects or other reproductive harm.

- These signs are everywhere.

- There is no penalty for posting an unnecessary warning sign.

Medical Information: Disease 1

Probability of Dying	This Year	Within Five Years
Surgery	8%	12%
Chemo	4%	22%

Medical Information: Disease 2

Probability of Surviving	This Year	For at Least Five Years
Surgery	92%	88%
Chemo	96%	78%

It's Hard to Do: Framing

Disease 1

Probability of Dying	This Year	Within Five Years
Surgery	8%	12%
Chemo	4%	22%

Disease 2

Probability of Surviving	This Year	For at Least Five Years
Surgery	92%	88%
Chemo	96%	78%

What if consumers are misinformed about themselves?

- Hyperbolic Discounting

- Offer a small discount today in return for agreement to pay early termination fee (which won't happen until the future).

- Projections of Their Better Selves

- Health club memberships and video rental late fees.

It's Hard to Do: Try It

- Consider a new social network that supports public policy discussion by government workers.
- It has a de facto or de jure privacy policy.
- What should be its disclosure obligations?
 - Dimensions of policy disclosed?
 - Specificity of disclosures?
 - User options?
 - Ease of finding statement and clarity of language?



Conclusion

Summary

- Suppliers may fail to disclose relevant information.
- Designing beneficial disclosure regulations can be really hard.
- Need to think about actual—not just intended—effects.
- Yes, we just heard someone say something negative about disclosure.