Understanding Fairness Perceptions For Price Decreases

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The price fairness literature has focused largely on price increases. However, many firms (e.g., Walmart) have recently been criticized for practices implemented to help reduce costs (e.g., reduced benefits to employees). We examine factors affecting price fairness perceptions for price decreases. In doing so, we broaden the traditional focus in price fairness research (based on dual-entitlement) from the firm-consumer dyad to a triad which includes the employee. Our findings highlight a new factor – harm to others – which impacts fairness perceptions and illustrate the usefulness of cognitive moral development for understanding individual differences in sensitivity to price fairness issues.

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**SYMPOSIA SUMMARY**

“Do Unto Others…”: The Influence of Others on Perceptions of Price (Un)Fairness

A. Peter McGraw, University of Colorado, Boulder, USA

**SESSION OVERVIEW**

The session examines factors influencing the perception of price (un)fairness. Prior research has examined many factors affecting fairness perceptions, such as the firm’s motives for the price change (Campbell 1999) and the role of past prices, competitors’ prices, and sellers’ costs (Bolton, Warlop, & Alba 2003). Such research has tended to focus largely on factors directly related to the firm (e.g., costs, profits, motives). Yet, firms’ pricing actions often result from other actions which may be beneficial or harmful to consumers. In addition, pricing actions may be perceived differently depending on what group of consumers is affected and how. The papers in this symposium focus on how the situation in which others affected, for better or for worse, by a price change influence perceptions of price unfairness.

In the first paper, Campbell develops a conceptual framework of the relationship between price and perceived (un)fairness, proposing that, symmetric to inferred motives, consumers may make inferences about the potential or realized harm to the consumer from the pricing action. Specifically, she explores how company characteristics and the identity of affected consumers affect price unfairness judgments. Her findings, across three studies, demonstrate that perceived harm to consumers of a price action can influence perceptions of the unfairness of the price action. Both the need for the product and the relative disadvantage of the consumer predicted perceived fairness of various price actions when costs of production were decreased. The results have implications for our understanding of perceptions of price unfairness and, more broadly, for understanding differences in consumers’ perceptions of how markets do, and should, work. Consumers appear to be considering the relative affordability of products and to believe that fairness is implicated when consumers can be harmed by relatively high prices.

The second paper, by Varki, Miller, and Banerjee, builds on the notion that perceived inequities on “others” affect price perceptions. They examine situations in which prices are decreased (thus benefiting the consumer himself), but the decrease is accomplished through cost-cutting actions which negatively affect others (e.g., laying off workers), thus forcing an inherent trade-off between the self and others when it comes to price unfairness perceptions. Specifically, the paper examines whether the harm caused to others (such as employees) affects consumers’ fairness perceptions of the reduced price, and whether consumers’ ethical perspectives moderate their fairness perceptions. The findings demonstrate that price decreases can be perceived as unfair and that ethical perspective does affect perceptions of price unfairness. In addition, the findings indicate that the reason for the price decrease matters, and provide insight into the effect of various managerial cost-reducing actions on consumers’ perceptions.

The third paper, by Schwartz and McGraw, also examines a situation in which consumers implicitly must make a trade-off between their own well-being and that of others. However, unlike in the second paper where consumers benefit by lower cost at the expense of others, in this paper, consumers are faced with a higher cost that benefits others. Specifically, Schwartz and McGraw investigate the effect of relationally reframing, or changing the perceived normative ‘rules’ at work within a trade-off, to undo the unsettling nature of the consumer exchange. They present results from a series of studies showing people’s perception of pricing fairness significantly varies depending on the nature of the good (e.g., medication vs. software) and the relational frame of the message. They show that communal-sharing messages (e.g., the price increase will help bring other safe, effective drugs to market), relative to market-sharing messages (e.g., the price increase is based on supply and demand in the marketplace), reduce distress over medication prices and ease perceptions of unfairness for price increases.

The discussant in this session is Lisa Bolton (Wharton) who has done influential work in the area of pricing, and fairness perceptions more specifically (e.g., Bolton et al. 2003).

By bringing together the three papers and discussant, the session improves our understanding of factors that affect perceptions of price unfairness and in particular, the influence of perceived harm (to consumers, employees, or unknown others) on such perceptions. Each paper in its own way examines the moral (and not just financial) aspect of price perceptions. The first paper focuses on consumer inferences about potential or realized harm to the consumer as a result of consumer need for the product (manipulated by type of product) and the relative disadvantage of the consumer (manipulated by type of consumer). The second paper also focuses on perceived harm, but examines the effect of harm to others (e.g., employees) rather than to consumers themselves. Moreover, it raises the question of how perceptions of price unfairness are perceived for price decreases and the role ethics play in such perceptions. The third paper considers the role of others but focuses on how justifications of higher prices which invoke others (e.g., benefits to society) change perceptions of price fairness by removing the need to make difficult moral trade-offs between money and well-being. Together, the papers provide insight into harm to consumers, employees, and society, that influence perceptions of price unfairness from an ethical standpoint. These factors are of particular importance considering current ethical concerns about company actions and current practices in the pharmaceutical industry. Finally, the papers serve to further our understanding of both perceptions of price unfairness and, more broadly, perceptions of how markets do, and should, work.

**References**


**EXTENDED ABSTRACTS**

“The Role of Inferences of Impact on Perceptions of Price (Un)Fairness”  
Margaret C. Campbell, University of Colorado, Boulder  
Perceptions of price (un)fairness (PPU) encompass a consumer’s subjective sense of a price as right, just, or legitimate versus wrong, unjust, or illegitimate. PPU influence multiple important marketplace factors such as willingness to pay, intentions to conduct business with a firm, and re-purchase intentions (Campbell...

Because of the importance of PPU, a growing body of research explores how perceptions of unfairness arise. Perceptions of price (un)fairness have been shown to rest on notions of dual entitlement (KKT 1986) whereby consumers and firms are seen as having rights to their reference prices and profits, respectively. A consumer may assess a given price relative to her reference price and react based on whether her entitlement expectations are violated. Violations of consumer reference prices that increase firm profits are perceived as unfair.

Recent research has expanded upon the classic dual entitlement framework. One stream has focused on understanding references consumers might use. For example, PPU can be influenced by reference points such as: past prices, competitor prices, firm costs, and type of product (e.g., Bolton and Alba 2006; Bolton et al. 2003; Ordonez, et al. 2000). A second line of research focuses on identifying variables, in addition to reference price and profit, that influence consumers’ perceptions of (un)fairness. Research demonstrates that PPU are influenced by the inferences the consumer makes about the firm’s motives for a price change (Campbell 1999), attributions for the price (Vaidyanathan and Aggarwal 2003; Xia et al. 2004), stimulus-based affect, and the source of the price (Campbell 2007).

Existing research provides evidence that characteristics of the firm influence PPU; the research presented here proposes that additionally, characteristics of the consumer can influence PPU. Specifically, we propose that, symmetric to inferences about the firm, such as inferred motives, consumers may make inferences about the potential harm to consumers from a pricing action and inferred harm can influence PPU. Thus, factors that affect inferred harm are expected to moderate the impact of pricing actions on PPU. Three experiments explore how several factors that influence perceived harm affect price (un)fairness judgments.

Consumers differ in relative advantage and disadvantage. The extent of disadvantage influences the degree of harm inferred from relatively high prices such that it was hypothesized that PPU would be higher when the consumer is relatively disadvantaged. Thus, Study 1 explored inferred harm from “consumer disadvantage” as an influence on PPU. Following KKT, we examine the effect of either decreasing or maintaining price when costs decrease. Inferred harm was manipulated by using two types of consumers. Study 1 had a 2 (price action: no change versus pass along half of a cost decrease) X 2 (consumer type: industrialized versus developing country). While there was no effect of the price action, consumer type significantly impacted PPU. Respondents indicated that it was more unfair to increase profits (by either not changing or only partially passing on the cost decrease) when the consumer was relatively disadvantaged (industrialized country) vs. relatively high prices for products for which consumers have a more critical need, Study 2 explores the effects of “need criticality” on PPU. Inferences of potential consumer harm are manipulated by the criticality of a product. The 2 (price change: decrease vs. no change) X 2 (product: furniture vs. pharmaceuticals) design shows a marginal effect of the price change on PPU (different from KKT); respondents perceived it to be less fair to maintain prices in the face of a price decrease (4.55) than to decrease prices (5.11; p<.07). In addition, the company type had the expected effect such that price fairness was lower in the case of medicine (4.45) than furniture (5.25; p<.01). Importantly, inferred harm was seen to mediate the effects of the product type on PPU.

Study 3 primes the concept of consumer need to further explore the role of perceived harm on PPU. The first two studies use different types of consumers (developing versus industrialized countries) and types of products (medicine versus furniture) that vary in terms of the harm of being unable to afford the product. However, while these vary as intended, they could also vary in unintended ways. Study 3 more directly examines the role of need/harm by priming the concept for the same group of consumers and the same product. Further, this uses a non-essential good (a movie ticket) and a potential price decrease (a price discount for senior citizens). A 2 (prime: comfortably situated versus uncomfortable situated) X 2 (senior discount: present versus absent) shows the predicted interaction. When the idea that seniors have greater need is accessible, a senior discount is perceived to be fair and a lack of a discount is unfair, whereas when the idea of need is not primed, there is no effect of a senior discount on PPU.

This research indicates that inferences of harm to consumers can influence perceptions of the (un)fairness of a price action. Both the need for the product and the relative disadvantage of the consumer influenced the perceived fairness of maintaining or decreasing prices. Further, in study 2, inferred harm mediated the influence of the price on PPU. These findings have implications for our understanding of PPU and, more broadly, for understanding consumers’ perceptions of how markets do, and should, work. The evidence suggests that consumers make inferences about the potential harm that could be caused to consumers by price actions. Consumers appear to consider relative affordability of products and to believe that fairness is implicated when consumers can be harmed by relatively high prices. It is important to take this into consideration in conceptualizations of PPU and, more broadly, of market mechanisms.

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Prior research on price unfairness perceptions has tended to focus on price increases and typically examines this issue based on the principle of dual entitlement (Kahneman, Knetch, and Thaler 1986). According to this principle, fairness perceptions are governed by a belief that firms are entitled to a reference profit and customers are entitled to a reference price. In the current research, we depart from this prior research in two ways. First, we focus on perceptions of price decreases rather than increases. Specifically, we explore how consumers respond to firms who lower prices at the expense of other constituents. Second, we expand on the traditional focus in price fairness research from the firm-consumer dyad to a triad which also includes the employee.

Our expanded perspective brings into focus an interesting dilemma for the individual consumer when confronted with a price decrease. With a price decrease, there is the potential for the individual to benefit at the cost of another, such as when a firm enables a price decrease through cost-cutting actions which harm employees. Numerous examples of such situations exist. For example, Walmart has been criticized for keeping costs down by not providing health benefits to its workers, though the ultimate beneficiary of lower prices is the consumer itself. Similarly, Nike has been criticized for its use of sweatshops and cheap foreign laborers. Thus, in determining the relative fairness of these actions and whether to patronize such firms, the consumer must inherently tradeoff their own good vs. that of an unknown other. Consequently, we expect that such decisions will be influenced by the consumer’s ethicality or degree to which s/he is self-interested vs. other-focused.

Kohlberg (1969) suggested that individuals evolve along moral stages which relate to the degree to which people act to promote their self-interests vs. selfless interests. Since individuals at higher levels of moral development are more likely to act to promote selfless interests, such individuals are more likely to perceive pricing practices which harm others (but benefit the self) as more objectionable than those at lower levels of moral development. Thus, in this paper, we examine how the ethical perspective of consumers (as measured by their cognitive moral development) affects their perceptions of price unfairness. In doing so, this paper integrates the relevant literature on ethics with the literature on price unfairness perceptions.

We examine the effects of price decreases and consumers’ cognitive moral development (or ethical perspective) on price unfairness perceptions in two studies. The first study, which uses a 2 x 2 between-subjects design that crosses the existence of harm to others (harm: present, absent) with respondents’ level of cognitive moral development (CMD: high, low), illustrates that price decreases can be perceived as unfair and that, consistent with expectations, cognitive moral development moderates these perceptions. Cost savings effected by harming others (e.g., by paying lower wages to employees or cutting employee benefits) led to the resulting price decrease being perceived as less fair than when the price decrease was effected through cost saving actions that did not harm others (e.g., acquiring new production facilities or savvy investments). However, only consumers with high levels of cognitive moral development actually perceived such decreases as unfair.

The second study delves more deeply into the process underlying consumers’ price fairness judgments for price decreases. The study used a 2 x 2 x 3 x 2 between-subjects design, crossing firm reputation (high, low), reason for the price decrease (intention: to increase sales, to remain competitive), level of harm (none, low, high), and level of cognitive moral development (low, high). Findings indicate that consumers perceive price changes as being increasingly unfair as the degree of harm to others increases; however, the point at which consumers react to these changes depends on both the firm’s intentions and the consumer’s level of cognitive moral development. When (harmful) cost-cutting actions are undertaken to increase sales, actions are perceived as unfair regardless of the consumer’s level of cognitive moral development. However, when these actions are undertaken to remain competitive, cognitive moral development does matter—any level of harm is viewed as unacceptable by those at high levels of cognitive moral development, while only high levels of harm negatively impact fairness perceptions for those with low levels of cognitive moral development. Despite these differences in fairness perceptions, consumers appeared to evaluate the relative benefits to self vs. others similarly regardless of their level of cognitive moral development.

As a whole, our findings demonstrate that price decreases can be perceived as unfair, but that such perceptions depend on the consumer’s level of cognitive moral development, the manner in which the cost savings are realized, and company intentions. By expanding our focus beyond the traditional firm-consumer dyad to a triad which includes the employee, we identify a new class of factors—harm to others—which impact fairness perceptions. In addition, our work highlights the usefulness of cognitive moral development for understanding price fairness perceptions and for explaining individual differences in sensitivity to price fairness issues. Implications for modeling the fairness judgment process, using cognitive moral development as a segmentation variable, and managing consumers’ reactions to price changes are discussed.

References

“Justifying the High Price of Medication: How Relational Framing Reduces Consumer Distress”
Janet Schwartz, Princeton University
A. Peter McGraw, University of Colorado, Boulder

Over the last three decades advancements in medicine have lead to enormous gains for pharmaceutical companies. As the industry enjoys significant profits, health care costs have risen at
rates far outpacing inflation. And much of those costs are shared, in one form or another, by consumers. Although prescription drug costs are not the only contributor to rising prices, consumers and policymakers are becoming increasingly more educated and critical of the pharmaceutical industry. The industry has responded with increased public relations and marketing efforts to assuage concerns that medication prices are strictly profit-driven.

The current paper investigates marketing strategies that pharmaceutical companies use to justify the price of medication. In particular, we are interested in how the industry uses relational rhetoric to conceal a focus on profits—a focus that, incidentally, is required of all publicly traded companies. Consider for a moment a quote from Billy Tauzin, president of PhRMA, an industry lobbying organization:

“...truth is that we are—as an industry—focused on one thing: the patient. Granted, we’re a business—a pretty darn big business. But we’re a business OF people working FOR people. We make lives better through better health.”

Tauzin’s focus is clearly one of solidarity with the patient-consumer. This rationale is a common example of an industry pricing justification where consumers can comfortably believe that everyone is working together and are thus willing to accept higher prices to help reach the ultimate communal goal of improved public health and well-being.

Why might a focus on benefits to all people ease consumer tension? We argue that the message shifts attention away from market norms associated with pricing and refocuses attention on the norms that govern community membership. Fiske (1992) has proposed that people use four types of relationships and their norms to organize, evaluate, and coordinate most social interactions. Here we focus on two most relevant to our investigation:

Communal sharing (CS) splits the social world into emotionally charged classes that differentiate in-groups and out-groups without degree of distinction. Everyone in a community shares certain rights and incurs certain duties.

Market pricing (MP) makes possible ratio comparisons of the values of diverse entities through the use of a single value or utility metric. This structure underlies capitalism and monetary transactions from simple loans to complex financial instruments. Prototypical relations include most business to customer and business to business exchanges.

We propose that the pharmaceutical industry’s strategy is effective because people find it difficult to confront explicit trade-offs between health and money. Put another way, people are reluctant to apply market-pricing rules to ‘things,’ like medicine, that they feel should be governed by communal-sharing rules (Fiske & Tetlock, 1997). Such taboo trade-offs are distressing to contemplate (see McGraw, Tetlock, & Kristel, 2003; Tetlock, et al. 2000) and people are thus motivated to avoid making such trade-off calculations. In addition, people are skeptical of those (e.g., pharmaceutical and insurance companies) who would make such trade-offs on their behalf.

In this paper, we investigate the effect of relationally reframing, or changing the perceived normative ‘rules’ at work within a trade-off, to obfuscate the unsettling nature of the exchange (see McGraw & Tetlock, 2005). We present the results of a series of studies showing people’s perceptions of pricing fairness significantly varies depending on the nature of the good (e.g., medication versus software) and the relational frame of the message. We show that communal-sharing (CS) messages, relative to market-pricing (MP) messages, reduce distress over medication prices and ease perceptions of unfairness for price increases, in part because price increases benefit consumers in the future.

In Study 1 participants were randomly assigned to the role of either patient user or investor in a company that had just launched a successful new sleep aid. It was stated that the pharmaceutical company had been criticized for the medication’s price and the participants were asked to evaluate a statement from the company’s CEO. In one condition the CEO provided a CS justification (high R&D costs for beneficial medications, patient well-being) and in the other condition, an MP justification (competition, investor well-being). Regardless of their roles as users or investors the MP strategy was more aversive than the CS message. Investors, however, were less distressed by the MP justification than users.

In Study 2 participants were randomly assigned to review hypothetical statements from either a pharmaceutical or software company attempting to justify raising prices on a very successful product to make up for R&D losses on another product. This is a common defense in the pharmaceutical industry, but paradoxically one that previous research has identified as generally unacceptable (Kahneman, Knetsch, & Thaler, 1986). Half of the participants saw a CS rationale and the other half saw an MP rationale for the price increases. Both messages were judged equally fair for those reviewing the software company’s statements. However, the MP rationale was judged more unfair than the CS rationale for the pharmaceutical company. That is, people were generally distressed at the price increase but particularly so when a pharmaceutical company’s rationale was market driven.

Study 3 examined whether CS justifications were effective for any medication or medications necessary for health. Participants read statements from a pharmaceutical company attempting to justify raising prices on a successful medicine to compensate for R&D losses on another medicine. The product was varied so that participants considered either a cosmetic anti-wrinkle treatment or a cholesterol lowering medication. The CS and MP messages were judged equally fair for the anti-wrinkle treatment’s price increase. However, the MP rationale was judged more unfair than the CS rationale for the cholesterol medication.

References


