APEC 3001 Discussion

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Today's Agenda

1. Housekeeping
2. Quantity Discounting
3. Two-Part Tariffs
4. Questions

Housekeeping

- State your presence in the Zoom chat for a record of attendance
- Take a minute to download these slides from Canvas under Week 12
- Writing Assignment 3 is due today, April 16th @10PM CDT
- Problem Set 6 is due Thursday, April 22nd @10PM CDT
- Follow link in TA bio on course Canvas page to sign up for Wednesday office hours
- For additional support, Peer Tutors are offered through the University library SMART Learning Commons

Second-Degree or "Indirect" Price Discrimination

When to use it:

1. The firm has market power and can prevent resale
2. The firm's customers have different demand curves
3. The firm cannot directly identify which customers have which type of demand before purchase

Indirect price discrimination is a pricing strategy in which customers pick among a variety of pricing options offered by the firm

Quantity Discounting

- Quantity discounts are a form of indirect price discrimination
- **Quantity discounting** is the practice of charging a lower per-unit price to customers who buy larger quantities
- The firm chooses these discounts so they are incentive compatible with each customer group
- **Incentive compatibility** is the requirement under an indirect price-discrimination strategy that the price offered to each consumer group is chosen by that group
- The firm wants to sell in bulk at a discounted price to incentivize customers with a lower willingness-to-pay (higher price elasticities of demand) without making the discount too attractive to customers with a higher willingness-to-pay

Indirect Price Discrimination - Figure It Out 10.3

Suppose you are a pricing analyst for MegaDat Corporation. Two types of clients use your software product. Type A's inverse demand for your software is $P = 120–10Q$, where Q represents users and P is in dollars per user. Type B's inverse demand is $P = 60–2Q$. Assume the marginal cost of supplying software is \$20 per user.

1. If you can determine which buyer is which before a purchase is made, what price will you charge each type?
2. Suppose you cannot tell which type of buyer each client is. Suggest a possible way to use quantity discounts to have buyers self-select into the pricing scheme set up for them.
3. Determine whether the pricing scheme you determined in part (b) is incentive compatible.

Two-Part Tariffs

- A **two-part tariff** is a pricing strategy in which the payment has two components, a per-unit price and a fixed fee
- The firm employs a two-part tariff to capture the entire surplus in the market when they have market power and *identical* consumer demand curves

Some examples of a two-part tariff include:

- Video game systems: fixed fee (console), per-unit price (games)
- Zipcar: fixed fee (annual membership), per-unit price (hourly rental fee)
- Popular clubs: fixed fee (cover charge), per-unit price (beverages)
- Amazon Prime: fixed fee (yearly charge), per-unit price (any purchases)

Two-Part Tariffs - Figure It Out 10.5

Assume you have been hired as an intern at the Golden Eagle Country Club golf course. You are assigned to set up a pricing scheme for the course, for which typical structure is to charge an annual membership fee and a per-round fee. Each of your customers is estimated to have the following demand curve for rounds of golf per year:

$$Q = 300 - 5P$$

If Golden Eagle can provide rounds of golf at a constant marginal cost of \$50 and charges that amount per round to its customers, what is the most customers will be willing to pay for an annual membership?

Questions

Any remaining questions?

Additional Support Resources

- Boynton Mental Health Services
- Student Counseling Services
- Let's Talk
- Educational Workshops
- Academic Skills Coaching