

Does Haggling Provide Utility in Information Asymmetric Markets? Evidence from Sales Tactics

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Abstract

Economic theory has largely focused on the purely economic motive of haggling: to reach a better price, and a small body of research at the noneconomic. Even in the discussion of the noneconomic motives, which veers towards psychological roots of motivations for haggling, the paper contends that there remains an angle unexplored: that the act of haggling itself can provide economic utility to buyers under certain circumstances. The research finds that prices in markets with price information hidden to consumers, buyers can perceive utility in haggling—and prices in the market are inflated by buyers to meet this demand for haggling. Furthermore, the research suggests that haggling markets may have disappeared in many places in the world due to this demand for haggling disappearing.

The work draws on structured interviews with book salesmen in Dhaka's "Nilkhet" book market and a focus group discussion with apparel store owners in "Mohammadpur Krishi Market", another haggling-prone market. The data suggests that price in information-asymmetric markets is based not only on the asymmetry's favoring producers, but also on the expectation that customers will haggle and seek haggled purchases. Sellers are aware that consumers have a preference to haggle for a good prior to making a purchase, and will "top off" the price they would otherwise sell a good at with a "haggling buffer" to address the buyer's need to haggle. We can view this as a premium charged to the buyer for their interest in haggling. This premium works in tandem with otherwise expected market forces to create asking prices that rest above what these forces would dictate.

It not only accounts for the noneconomic aspect to haggling but, in what ends up being one of the most unexpectedly powerful suggestions of the research, also factors in how shifts in consumer behavior could have resulted in such markets mostly disappearing from developed economies around the world.

Keywords: Haggling, Price, Asymmetry, Negotiation, Behavior

Introduction

The act of haggling can be defined as the bargaining between two parties in reaching an optimal price that satisfies both parties. Haggling has been defined and observed by researchers in the past, but analysis has heavily leaned towards the idea of consumers bargaining for better value in their purchases. While psychological motivations for haggling have been explored, research has been mostly abstract and unexplained in economic terms. Bargaining models fail to account for noneconomic motivations for haggling and consumer mindsets. Price discrimination models speak of per-customer pricing, but fail to follow up on how haggling affects consumer perception of utility. This research marks its place in this gap in the current body of work through the behavioral economics tradition.

The paper combines a quantitative and qualitative approach, elaborating on each respectively in their discussion sections, and surmises its findings in a model presented at the end of the discussion.

Based on the data, a core objective of the paper is to develop a model that better explains the differential effect of utility from haggling on pricing in haggling markets. The paper intends to be revealing for consumer behavior in haggling markets and shed light on paths to possible future work. The first section of the paper is devoted towards understanding what the literature has to say on the intrinsic motivation behind haggling. After which, the methodology of the paper is presented where the model to be used is discussed at length. Subsequently, we delve into the empirical results where we test to see whether consumers really derive utility from the act of haggling with price information asymmetry pervasive in the market.

The questions this paper addresses are:

- Do consumers in a market with price information asymmetry perceive utility in the act of haggling?
- What is the effect of such utility existing or being absent?
- Can the presence or absence of such utility help explain market structure?

Literature Review

Building on principles in accepted literature, haggling can be seen as an intersection of a few dimensions of microeconomics. In their seminal book on bargaining, define bargaining as negotiating the terms of a purchase agreement or contract to establish an agreement between parties settling what each shall give and take or perform and receive in a transaction between them [1]. However, the authors draw a distinction between bargaining and negotiation: to negotiate is to bargain with others until a transaction is settled. Forwards the accepted notion that bargaining situations in consumer markets take on the form of people trying to purchase at a lower price [2]. Haggling takes on the properties of all the aforementioned situations.

Defines it as ‘a process of price formation which aims at establishing particular prices for specific transactions, acceptable to both buyer and seller, within the “price range” that prevails in the market’ [3]. How does it originate? Market imperfections often allow sellers to charge consumers different prices [4]. Haggling could arise from situations in which producers can charge prices on a per-customer basis, and result in bargaining situations in which both parties attempt to maximize their surplus. The market imperfection of information asymmetry, specifically, can result in the consumer not knowing what the price of a certain good should be, and requires them to initiate an ‘information search’ to find out more [5].

Forwards the idea that even as markets become non-monopolistic and competitive, information available affects the extent of price discrimination and consumer surplus in an industry [6]. However, authors do admit that consumer surplus is not good enough an indicator of consumer welfare, nor is its direct analysis sufficient to explain interactions in markets [2, 1].

Discovered from a set of almost forty in-depth interviews several noneconomic motivations for haggling [7]. They argue that psychological drives such as the needs for achievement, dominance and affiliation are drivers for the haggling process. Even in the study of game theory, discovered that these needs can significantly affect the outcome of a value payoff game [8, 9-11].

In all this significant work, we have yet to see the idea of the act of haggling itself being, or not being, of economic value. The differential effect haggling can have on market prices is consequently unaccounted for. We also fail to find mention of haggling slowly disappearing from developed markets. The work cited is significant in that it allows these questions to be asked and answered.

Methodology

Data and Method

This paper incorporates the use of a mixed-method study. Qualitative methods prove to be useful when attempts are made to uncover the root cause behind idiosyncratic behavior (Strauss, 1990). Furthermore, qualitative methods also prove to be effective when detailed responses are needed to be found out in which solely quantitative methods would not have been enough. In addition, in depth interviews provide more flexibility to the researcher than the standard questionnaire approach (Patton

1990) and have been used in numerous consumer studies seeking to understand motivations (Hirschman 1992; Otnes, Lowery, and Kim 1993). Thus, semi-structured in-depth interview on haggling behavior and possible connection to sales tactics was conducted with 20 shopkeepers in the “Nilkhet” book market (Nilkhet, Dhaka-1205) of Dhaka. This segment of respondents was chosen based on the pervasiveness of haggling, product homogeneity and information asymmetry: absence of reference prices for consumers. Purposive sampling was used to select respondents. Confidentiality was assured to participants. The survey was qualitative in nature to draw out valuable information on behavioral phenomena that numbers often fail to describe, but a quantitative aspect was kept to ensure the persuasive rigor of the data.

For the bookstore interviews, responses to four broad interview questions were appropriated to a 5-point Likert scale based on agreement with a statement. Discrete numerical values set to levels of agreement were as such.

Alongside, focus group discussions (FGDs) were performed with two groups of apparel store owners in the Mohammadpur Krishi Market. Statistical tests were performed with the IBM SPSS statistics software suite to measure the validity of the data and assess the computed information.

Hypotheses

The results were used to test the following general hypothesis (rather than four hypotheses for each question, which would reveal little):

H_0 : The act of haggling does not provide utility to customers in information asymmetric markets

H_1 : The act of haggling provides customers with utility in information asymmetric markets

This result would allow the following inferences:

1. What the effect of such utility existing or being absent is on market prices
2. What the effect of such utility existing or being absent is on market structure

The data and statistical analysis serve to back up the theoretical analysis presented later in the paper, which, along with a new model forwarded by the paper, is the crux of the work. The strength of the research lies in the qualitative analysis and discussion of results and proposed theory, but a quantitative aspect has been used to establish a foothold of authenticity for said work. Qualitative methods are better suited to draw out nuances in relatively mathematically obscure phenomena, and for better understanding human interactions. This is backed up by the fact that consumer studies often draw heavily on qualitative analysis. Although the data are from the study of specific markets, we purport that the principles of the research extend to the general. The research does not draw any distinctions based on the type of goods themselves.

Discussion

The quantitative results below support a discussion that draws on in-depth interviews:

Table 1: Response Means, Error and Confidence

Statement	Mean	Standard Error	Lower bound of confidence interval
Haggling over product prices is common place	1.80	0.117	1.56
Customers are likely to buy a product they've haggled for	1.40	0.197	0.99
Customers are likely to buy a product if a low fixed price is set from the beginning	1.25	0.228	0.77
Prices are set to reflect customers' tendency to haggle for lower prices	1.25	0.176	0.88

The data suggests that price in information asymmetric markets is based not only on the asymmetry's favoring producers, but also on the expectation that customers will haggle and seek haggled purchases. Sellers are aware that consumers have a preference to haggle for a good prior to making a purchase, and will 'top off' the price they would otherwise sell a good at with a 'haggling buffer' to address the buyer's need to haggle. We can view this as a premium charged to the buyer for their interest in haggling. This premium works in tandem with otherwise expected market forces to create asking prices that rest above what these forces would dictate. *Prices are increased in advance by sellers in anticipation that customers will more likely buy if they get to haggle for a good.*

A resultant view might follow that: the mechanism results in consumer surplus falling and producer surplus gaining an edge. This logic does not hold in the light of haggling truly producing a kind of utility for the consumer. The argument can be made that the market is simply charging the consumer for this through elevated prices from the get-go. Indeed, this paves the way for the next point of contention: how are non-hagglers accounted for? *Interviews and focus group discussions, sellers often identified two distinct groups of consumers: the majority being those looking to haggle, and a minority of customers ('five percent', one storekeeper went as far to stress) who perform their shopping searching different prices, but not participating in haggling.* A very important point of contention, considering that the vast majority of haggling markets have been replaced by markets with fixed prices in developed economies; most consumers are non-hagglers. This is discussed with the help of a Haggling Market-Price Model— a model proposed by this paper.

Haggling Market-Price Model

The *Haggling Market-Price Model* states that in a haggling market with multiple sellers, a seller is faced with two options: charge an elevated price that will satisfy the haggling customer and their need to bargain, or offer a lower fixed price which will appeal to the non-haggling customer who conducts their search without haggling. Based on this assumption, the following model can be used to describe haggling in markets, with the behavioral effect of gaining utility from bargaining considered:

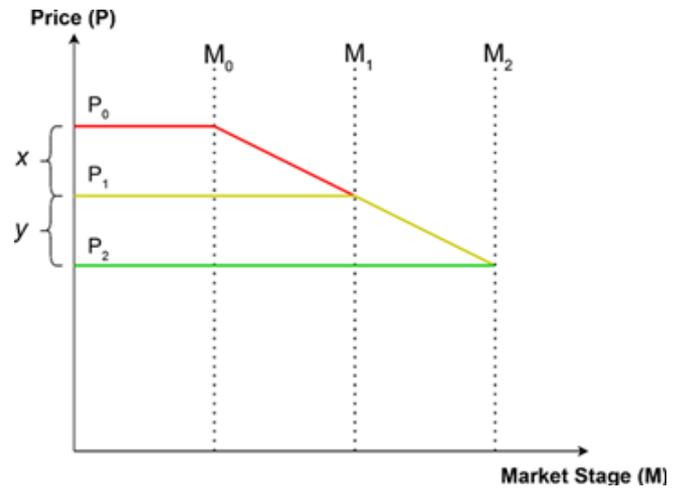


Figure 1: Haggling Market Price Model

- **Haggling Buyers** are buyers who in their information search, and product search, will act on opportunities to haggle – we will assume that they gain utility from the act of haggling (the extent and success are not relevant in our view)
- **Non-Haggling Buyers** are buyers who will not act on opportunities to haggle in their information and product search, choosing to instead take the price information at face value and continue the search
- **M₀** is a market with primarily haggling buyers and a market imperfection of information asymmetry
- **M₁** is a market with information asymmetry but in which most buyers refuse to haggle in their search
- **M₂** is a market without the market imperfection of information asymmetry (and therefore cannot house haggling situations, see assumptions below)
- **P₀** is the market price without market imperfections and non-haggling buyer's dominant
- **P₁** is the market price with the market imperfection of information asymmetry and non-haggling buyer's dominant
- **P₂** is the upper price level of prices sellers will ask of haggling buyers in a market with information asymmetry and haggling buyer's dominant
- **x+y** is the range of prices sellers will negotiate with those whom are identified as hagglers
- **y** is the range of prices sellers will offer to those they identify as non-hagglers

The model assumes markets exist in which haggling negotiations occur, that they must contain information asymmetry about product prices, and that such markets can seat two types of consumers: haggling buyers and non-haggling buyers. Non-hagglers perform information searches in the market but do not partake in haggling. An additional assumption is that sellers cannot identify whether a consumer is a haggler or a non-haggler.

We do not assume anything about the factors that result in the formation of these two separate groups, nor is it in the purview of the data collection (inferences however, we feel can be drawn later). Finally, we propose, that the market can develop in multiple stages, each which bring about a change in price levels and buyer-seller interactions.

We propose that an early market stage M_0 exists in which haggling buyers (those who gain utility from the act of haggling) are the dominant consumer group; price and information asymmetry exists. The market price range reflects the demand for haggling. As most buyers are haggling, consumers will face price levels ranging from $x+y$ (that is, P_2 to P_0), with the range x being dominant. This range x represents a postulated 'price buffer'. When faced with a consumer, sellers have the choice of:

- a). Offering an elevated price to take advantage of a possible demand to haggle
- b). Offering a fixed price that is attractive to begin with to a non-haggler who will search without participating in haggling

Sellers must 'bet' – they do not have prescience. Wrong "bets" can result in losing a non-haggler. The market, over time, develops into M_1 in which non-haggling buyers become dominant and only a minority gain utility from purchases. We infer that a change in consumer mindset results in this transition from M_0 to M_1 , but inference is not central to building my case. In this case, the prices offered move to a wedge in which sellers choose to what extent they will try to wield the power to discriminate, as offered by information asymmetry. In the market M_1 , a seller risks losing a customer by offering an elevated price as non-haggling buyers are dominant. They reflect demand for purchasing without utility gained from haggling. The dominant consumer type, non-hagglers, will carry their information search and be offered fixed prices within the range y . In the final market stage M_2 , information asymmetry disappears and the market price settles at P_0 , the 'ideal' equilibrium price. Bargaining disappears from the market.

Compared to haggling markets in developing economies, equivalent markets have transitioned to this final stage in developed economies, brought about by what can be hypothesized as a shift in consumer mindset and resolved market imperfections. It remains to be explored what kind of factors result in hagglers evolving into non-hagglers as an economy develops.

Conclusion

The paper finds that consumers do indeed gain utility from being able to haggle for a purchase in information asymmetric markets, but that this can change with a shift in consumer culture/mindset. The fact that consumers can gain utility from haggling has clear implications on price levels and market interactions. Profound, broader changes may result from changes in their mindset as well as market development stages in regards to bargaining. Haggling is likely symptomatic of 'underdeveloped' markets and consumer culture, and tapers off as markets and their consumers evolve.

That said, the main limitation of the research exists in it being the independent study of a sole student author and the resource and time constraints that naturally follow. Furthermore, multiple geographies could not be directly explored in the work and secondary sources were used to understand patterns in other coun-

tries. These can be resolved in future studies to test how well the observations translate across borders.

For one, if negotiations create behavioral discrepancies, how is the producer's selling behavior affected during bargaining? Are there significant economic effects as a result? In terms of the markets themselves, how do markets behave as they transition between stages of development? When does the change occur in which sellers find it, on average, more profitable to offer straight fixed prices? What implications does haggle and its disappearance have on producer and consumer surplus? Should utility from bargaining be considered in surplus calculations? Are there direct examples of haggling markets transitioning across the globe?

These are just some questions which can further elucidate the interesting phenomenon of haggling, its producing utility for consumers, and its presence and absence across markets and economies. In closing, we believe that the paper provides a convincing example of the concept of utility from nonfinancial and noneconomic drives in typically economic interactions: a concept that can shed a peculiar, but revealing light on oft-studied topics. We stand only to benefit from considering such behavioral mechanisms in future economic research.

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