Undercover Economist: Match me if you can
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Whenever I shop at John Lewis, I see its price promise, "Never knowingly undersold", displayed in an attempt at reassurance. It makes me very suspicious indeed. Not that I doubt the promise to meet any competitor’s price. I’m sure that happens regularly. What bothers me is the possibility that this kind of promise drives prices higher, not lower.

The problem with a promise to match a competitor’s price is that it will discourage the competitor from cutting its price in the first place. If I went into business, one obvious way to win some customers would be to reduce my price. If the competitor’s emporium across the road boasted a price promise, I might not bother.

Imagine that a company threatened its competitors with the following statement: “We guarantee that there is no point in you trying to beat us on price. We send people around to your stores to make sure you’re not trying any funny stuff. Better, we pay our customers to look at your prices and tell us about them. So forget it. Keep your prices high and so will we, and nobody will get hurt.”

John Lewis doesn’t say that, and nor do any of the other businesses that make price-matching promises. Any company that tried it would be hauled up before the Office of Fair Trading in short order, not to mention the fact that customers would be unlikely to approve. Still, I am not sure that the difference between the promise to customers and the threat to competitors is anything more than rhetorical.

Price transparency is a double-edged sword. If customers can easily compare lots of prices, then they will seek out the best deal. But if customers can easily compare lots of prices, so can competitors, and if they quickly cut prices in response, they will also win back customers very quickly. Companies will realise that cutting prices to win market share is a mug’s game.

The price of airline tickets, for example, used to be notoriously opaque. Now you can log into a consolidator website and compare lots of different prices, but it’s far from clear that this has led to more cut-throat offers.

I asked for some quotes just now for a week-long return trip from London to New York in a fortnight’s time. The internet broker dug up 200 offers from five different airlines, most of which were for the exactly same price: £299. Only one itinerary, between less popular airports, beat that price, and did so by less than a fiver.

Of course, that pattern might indicate ferocious price competition, but since the last time I flew on that route it was on a half-empty aeroplane, I doubt that price transparency has given airlines much incentive to slash prices until every seat is sold. The fact that Byzantine regulations stand in the way of new competitors who want to fly the route cannot help: it makes it yet more tempting for the existing players not to fight too hard for market share. It is the possibility of new entrants to the market, rather than apparently fierce competition between a small number of players, that provides a more reliable source of competitive pressure.

It is all part of what economists call the “topsy-turvy principle” of competition: the more room there is for aggressive competition, the less likely it actually is to happen - loosely, cutting
prices in a transparent market is like starting a war with a nuclear superpower. In some cases, at least, we should regret the coming of internet price-comparison sites. A market where nobody knows what price the competition is offering is also a market in which it is worth haggling and shopping around.