

## The controversy over the growing use of dynamic pricing by firms



Some experts argue that for dynamic pricing to be successful for a business, great care needs to be taken with how the policy is presented and explained to its customers. **Jon Guest** takes a look at the concept

Imagine the following situation. You walk into a shop and see an item that you would quite like to purchase. You check the price label and decide to buy the product after a quick visit to your favourite café for a drink and piece of cake. Thirty minutes later, you return to the shop and are surprised to see that the price of the item has increased by 20%. This is in response to a surge in other customers buying the product while you were in the café.

This is an example of dynamic pricing, where a firm with market power adjusts prices relatively quickly in response to changing market conditions, i.e. changes in demand and supply.

### Traditional versus flexible pricing approaches

Traditionally, prices set by firms in retail markets have been less flexible. They may eventually adjust to market conditions, but this could take weeks or even months. Typically, prices for an item on a particular day do not respond to changes in the number of people who want to buy the good — they

remain constant. If a product is very popular, the shop sells out and the consumer sees empty shelves. The price does not instantly adjust so that demand is equal to supply.

However, the price strategies of many sellers are changing as developments in technology make it possible to take a more flexible approach. For example, algorithms automatically adjust the prices of many goods on Amazon Marketplace in response to large quantities of real-time data on consumer behaviour. If there is strong demand for an item and it is selling well, the algorithm will automatically increase the price. If there is weak demand and large amounts of unsold stock it will decrease prices. Prices for popular items change every 10 minutes and can fluctuate by more than 20% in just 1 hour.

Other sectors where businesses have been using this approach for many years include the airline, hotel and ride-hailing (Uber) industries. Ticketmaster implemented a dynamic pricing strategy into the primary ticket market for live music events a couple of years ago.

### The price of a pint

There is evidence that the use of dynamic pricing is becoming more widespread. In a consumer confidence survey undertaken for Barclays in September 2023, 47% of the respondents had noticed more examples of companies raising prices for goods/services in response to higher demand at peak times.

One recent example made newspaper headlines in September 2023. The Stonegate group, the largest pub company in the UK with around 4,500 premises, announced that it was going to start increasing the price of a pint of beer by 20 pence during busy periods when there was greater demand.

Economic theory predicts that the use of dynamic pricing gives companies the opportunity to increase their revenue. Robert Cross, who chairs a revenue management company, argues that:

If you're a business, it's irresistible because it will improve your margins... Anywhere there is a mismatch between what a customer is willing to pay, and the actual price is ripe for dynamic pricing.

There are also advantages for consumers as they avoid the hassle and irritation of waiting in long queues as the instant rise in prices removes any excess demand for a product. It also reduces the opportunity cost of shopping as people can spend the saved time on more enjoyable activities. However, there will clearly be some winners (those paying lower prices when demand is low) and some losers (those paying higher prices when demand is high). Therefore, the overall impact of consumer welfare is ambiguous.

## Public reaction

Whenever a firm tries to implement dynamic pricing, it faces one major problem. There is evidence that most consumers really dislike the policy. For example, when Stonegate announced its new pricing strategy it led to a backlash on social media with many customers calling on people to stay away from their pubs. The following are some comments posted by customers:

Stonegate pubs will not be having my company or my money at the weekend, simple.

Dynamic pricing is annoying enough on cab apps, this can't become the norm in pubs.

Absolutely outrageous. Boycott these venues.

In a survey of over 2,000 people carried out by YouGov in November 2022, 52% of respondents strongly opposed the use of dynamic pricing of tickets for live music events. Just 1% of the respondents strongly supported its use.

## Questions

- 1 Explain the difference between surge and dynamic pricing.
- 2 Using a diagram, explain how dynamic pricing can increase a firm's revenue.
- 3 Discuss some ways that consumers may benefit from firms using a less flexible pricing strategy, i.e. where prices do not adjust so quickly to changes in demand and supply.
- 4 In the YouGov survey on ticket prices, the dislike of dynamic pricing was far lower among 18–24 years olds than other age groups. Suggest some possible reasons for this finding.
- 5 Using the concept of loss aversion, consider some different ways that Stonegate could have presented their new pricing policy.

## Weblinks

*Guardian* report on Stonegate's controversial dynamic pricing decision:

[www.tinyurl.com/5h8fdfma](http://www.tinyurl.com/5h8fdfma)

Barclays coverage of recent British spending habits:

[www.tinyurl.com/2zkbtvx7](http://www.tinyurl.com/2zkbtvx7)

YouGov story exploring the issue of 'surge' ticket pricing: [www.tinyurl.com/2dvcm8mw](http://www.tinyurl.com/2dvcm8mw)

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