

# Book Review: *Priceless – The Myth of Fair Value (and how to Take Advantage of It)*

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*Priceless* is an informative and at times insightful glimpse into the psychology of pricing and the numerous quirks of decision making. Poundstone begins with an extensive overview of the history of economics and psychology (now known as behavioural economics), taking us right back to the early experiments of one SS Stevens, whose pioneering work in the field of psychophysics paved the way for further research into perceptual and behavioural traits. As Poundstone navigates his way through the intricate and often entertaining history of the subject, illustrated with countless examples and case studies, he explains how people estimate numbers, react to the same thing in different ways depending on how it's presented, are deceived by prices, and make most decisions without really thinking about them.

In contrast to classical economics and challenging John Stuart Mill's *homo economicus*, behavioural economics attempts to reveal how irrational many decisions actually are, especially when it comes to something like price. There are now numerous books dedicated to the subject - so what does Poundstone have to add to the debate? Well, apart from his well-researched historical overview of the development of the movement, the answer lies (or at least it should lie) in the subtitle of his book: "The Myth of Fair Value (And How to Take Advantage of It)".

As Dan Ariely demonstrates in *Predictably Irrational*, most decisions aren't based on 'rational' analysis, but it is still possible to identify predictable patterns of behaviour. Poundstone takes up this line of thought, explaining that the brain "constructs desires and beliefs on the fly... which can lead to inconsistent prices and choices," before going on to explore many of the ways our everyday decisions are manipulated through a variety of implicit and explicit pricing tactics, including anchoring, decoy pricing, charm pricing, bundling and unbundling and discounting.

The first lesson in Poundstone's book is that price is not an absolute, because price is really just a number, and numbers are only understood in relation to one another. What this means is that people are more sensitive to the differences between numbers and not to the number itself. Given that most buyers don't really know the actual cost that went into manufacturing the product they're considering buying and are therefore unable to make an informed decision about whether the asking price is 'fair', the first question they're likely to ask is how does this price compare with prices for similar products? Well, they could

compare product X by company A with product X by company B and go for the cheapest, but the smart company wants the buyer to compare product  $X_1$  by company A with product  $X_2$  by company A and purchase either  $X_1$  or  $X_2$ . How do they do this? Poundstone explains using the example of two bread makers, priced at \$279 and \$429 respectively, both manufactured by the William-Sonoma company. The \$279 model was released first and sales were ok, but after introducing the \$429 model, sales for the cheaper model nearly doubled. It didn't matter that sales for the more expensive version were terrible, the very presence of the \$429 model made the cheaper version more attractive. This is a classic example of the anchoring technique.

Anchoring is now such a widespread tactic that almost anyone selling anything anywhere is making use of it. By creating a reference point, sellers are priming buyers by providing them with a kind of measuring stick so the focus becomes the difference in price and not the price itself. What's particularly interesting in the case of luxury goods, and perhaps Poundstone misses the point here, is that certain products are so specialised that companies like Whole Foods can charge prices that wouldn't normally be tolerated, because these products often don't have an effective reference point making it difficult to assess the 'fairness' of the price tag. However, let's not forget that there's also a strong value message which comes with a high price tag, which also influences customer behaviour. Isn't the same true of something like theatre tickets? Poundstone makes brief reference to the \$480 premium tickets on sale for *The Producers* on Broadway in October 2001, but what becomes clear after reading his book is that the \$480 ticket is going to affect customer's perception on a range of levels and not just the 'that's a crazy price' reaction.

While Poundstone doesn't explicitly deal with the price of theatre tickets, it is possible to apply some of the principles he outlines to the arts. One of his chapters helps to explain why people complain about the price of tickets for popular concerts and shows. The answer: because they don't consider them to be fair. Poundstone gives a good example about a shop selling snowploughs to demonstrate this point. Following a severe snowstorm, the shop took advantage of the increased demand for snowploughs by raising the price dramatically. The problem was that customers who remembered the previous lower price were now outraged that they were now going to have to fork out more money for what was exactly the same product. Herein is the crux of the problem: people's perception of what's fair is often contradictory and rarely in line with classical economic models.

Fairness depends on context, which is different for different people, hence the implied myth of fair value. There is often no clear agreement between customers about what the price of a product ought to be, and often the same customers will make contradictory decisions depending on their own experience as they approach a purchase. To paraphrase Einstein, it really is all relative, but that's not to say that anything goes and price is arbitrary. Whilst buyers may not agree on what the price of a product *ought* to be, sellers on the other hand offer prices that products *could* be. The difference in approach to a transaction between buyers and sellers and how people view losses and gains differently are loosely dealt with throughout the

book as Poundstone gives a brief overview of Kahneman and Tveksy's Prospect Theory and then deals with the psychological behaviour of participants in the Ultimatum Game.

Poundstone concludes with the view that "we spend our lives searching for the lowest price, the highest salary, the most money." But this is clearly a very one-sided prospect. To what extent are people really choosing on price alone, and at what point has the decision gone beyond a question of price to a question of something else? Surely, the same complex psychological factors that can affect people's decision-making when it comes to price are exactly the same factors that affect individuals when they make a purchase in general. Questions about the purpose of the purchase must also come into play.

By focusing so much on price alone, Poundstone doesn't deal with that part of the purchasing process which involves comparing not one price to another, but one purchase to another. A \$100 pair of jeans may look cheap compared to a \$2000 pair of jeans, but for the price of a \$100 pair of jeans, you could buy something else entirely: a restaurant meal for two, a pair of theatre tickets etc. So let's not forget that if people don't want any of those things then no price and therefore no pricing tactics which take advantage of the myth of fair value will make any difference, and for those people who do decide to purchase, price will still largely be shaped by demand.