授课文本

Costly comparison

Cecilia Brennecke

AT FIRST glance, price-comparison websites are an example of capitalism at its best. Savvy consumers can use them to hunt down the best available deal for insurance, electricity or a mortgage. Firms providing such items, terrified of losing customers, feel an obligation to improve their offerings all the time. But recent theory and practice suggest the reality is more complex: comparison sites are simultaneously friends and foes of competition.

In 1971 Peter Diamond, an American economist, showed that even small "search costs", such as the time it takes to walk down the street to see what is on offer at a rival shop, can seriously undermine competition on price. Industries in which it is much harder to compare offerings and switch providers can expect sky-high prices and profits. In the past, this problem was acute in the insurance market. Many consumers, on discovering their insurance was running out, would lazily renew with their existing provider. The hassle of comparing competing offers, and the need to maintain coverage without interruption, hindered competition. That allowed firms to hike prices for existing customers.

Today, things are very different. Comparison sites have made shopping around and switching insurers a matter of just a few minutes' effort. In the British car-insurance industry, about a quarter of all sales, and more than half of new business, flows through them. That has caused fierce competition on price and eviscerated profits. In 2011 Towers Watson, a consultancy, in a note entitled "Why aren't we making money?", said that "unnecessary" price competition following the rise of comparison sites in Britain had cost insurers £1 billion ($1.5 billion) a year.

Consumers should celebrate that; the firms' losses are their gains. But there is a catch. Comparison sites, whether for insurance or something else, introduce a new layer of costs, including their own splashy advertising campaigns. In theory, competition in the market for comparison sites ought to keep those costs down. But in a recent paper, David Ronayne of Warwick University argues that consumers often lose out from comparison sites. They earn a commission for each shopper who uses them to buy insurance. That referral cost is

incorporated into the price the consumer ends up paying. If the increased costs outweigh the saving the comparison enables, consumers end up worse off.

For instance, suppose some consumers are loyal to a single comparison site, and do not use any others to compare prices. The lucky website can crank up its referral fees, safe in the knowledge that insurers must pay up if they want access to its captive market. Those fee hikes are then passed on to consumers in the form of higher premiums. In effect, consumers are taxed for their loyalty—just as they were before comparison sites were invented. Mr Ronayne argues that this problem can only be avoided entirely if consumers go to the trouble of checking every site.

These worries are not just theoretical. In 2014 Britain's competition regulator found that some comparison sites were using their contracts with retailers to ban them from offering cheaper prices elsewhere. That weakened rivals' incentive to cut fees, because prices on their site could not fall (which would help them gain market share). By keeping prices similar, the contracts also reduced the incentive for consumers to search on multiple sites, thus helping sites retain their users.

Weaker incentives to lower commissions means weaker incentives to lower costs, too. That might explain why comparison websites advertise so heavily, and sometimes offer free gifts to those who use them. In a recent paper, Ben Edelman of Harvard Business School and Julian Wright of the National University of Singapore argue that when a site knows that the prices merchants provide through it will always be the cheapest available, it cranks up investment in attracting customers, safe in the knowledge that the merchants and ultimately consumers will bear the cost.

The anti-competitive contracts are now banned, at least in Britain. But another competition investigation involving price comparison has sprung up. In April the European Commission alleged that Google (whose chairman, Eric Schmidt, is on the board of The Economist) had been abusing its dominant position in the market for search by artificially promoting its own comparison site, Google Shopping, in its search results. If most consumers were to rely on Google to compare prices, the search giant would, in theory, be able to attract hefty commissions.

Searching for search

How can you ensure the market for price comparison is competitive? Asking consumers to check multiple websites defeats the point of using them. One solution is to have only one site, but regulate it as a public utility. Alternatively, the government could run the site itself—much as the American government now runs comparison websites for health insurance under Obamacare.

But creating good search and comparison sites is hard, and governments are unlikely to do a good job of it. The Obamacare websites were riddled with problems on launch. Much better to acknowledge that consumers will always have to do some comparison

themselves to “keep the system honest”, argues Tony Curzon-Price of Britain’s Competition and Markets Authority.

Websites that compare the comparison sites can help, although it is easy to see how they could fall prey to the same problems. Any firm with captive users, be it a comparison site, a search engine, or a social-media platform, can charge a high price for access to the eyes of its customers. For all their innovation, internet middlemen are not unlike supermarkets, which help people select purchases by bringing lots of items to one spot for comparison. Shoppers would never imagine that a single store had the lowest price on all the items they need. They should not believe any website does, either.