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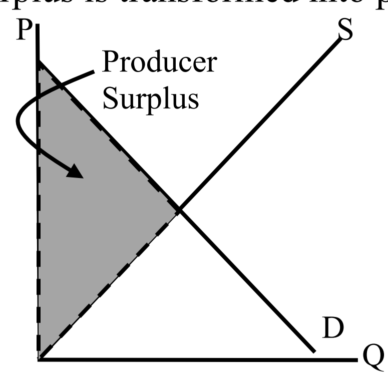
TOPIC 18: PRICE DISCRIMINATION II

I. Efficiency and price discrimination
   a. Part of price discrimination is a transfer payment (from consumer to producer surplus). This sounds bad, but a transfer payment is neutral. From an efficiency standpoint, everyone is treated equally.
   b. If price discrimination reduces output, then society becomes less wealthy.
   c. *However*, if it increases output, then society (probably) becomes wealthier. Price discrimination increases firm revenue which is needed to induce entry.
      i. Is it better to have a rare disease or a common one?
      ii. PD allows an increase in market size, and thus of revenue. PD helps cover upfront costs.
      iii. Remember, AIDs medication. Without PD, there might be fewer medications invented.

II. Perfect price discrimination
   a. *Perfect price discrimination*—when each customer is charged maximum willingness to pay
      i. *Examples*: mechanics, bank loans
   b. In PPD, consumer surplus is transformed into producer surplus.



   c. Note this is *as efficient* as if there was no price discrimination at all.
   d. College works with this; while the tuition colleges post on their website (the list price) is what gets headlines, that is very different from the price people actually pay (the net price). [The difference can be quite large.] (Note the difference axes for the private and public colleges.)

FIGURE CP-9 Average Published and Net Prices in 2023 Dollars, First-Time Full-Time In-State Undergraduate Students at Public Four-Year Institutions, 2006-07 to 2023-24

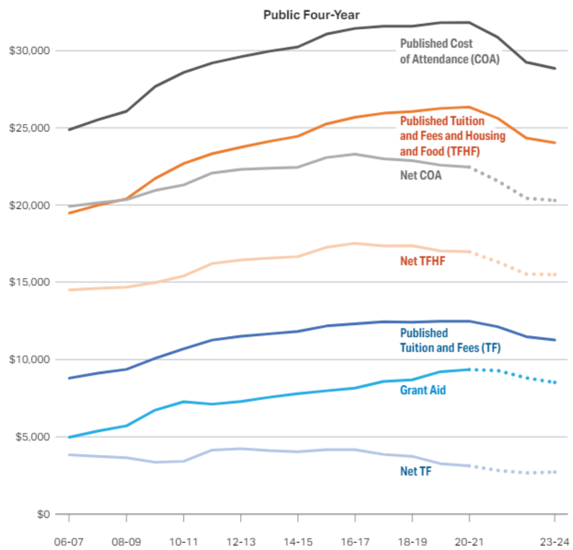
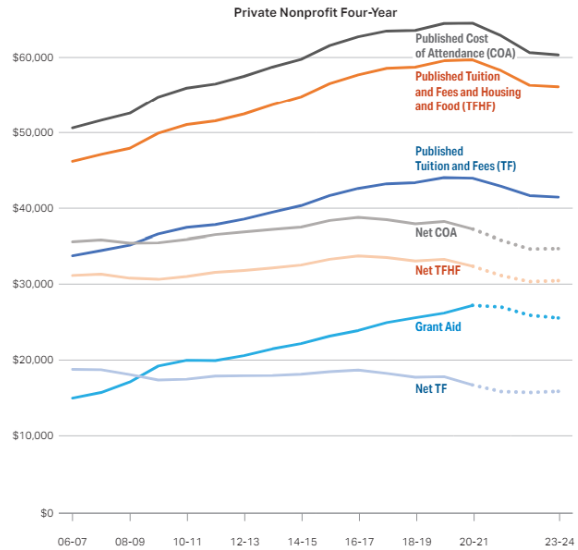


FIGURE CP-10 Average Published and Net Prices in 2023 Dollars, First-Time Full-Time Undergraduate Students at Private Nonprofit Four-Year Institutions, 2006-07 to 2023-24



e. Don’t think of the list price as the price the college charges. Think of it as the *highest* price the college charges, and that price is charged to the people who have a high willingness to pay. Remember, schools have a ton of information about applicants so they have a good sense of how much they willing to pay and can charge them accordingly.