Dual Pricing in a Model of Sales

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Abstract

In many industries, manufacturers, when dealing with retailers, make use of vertical restraints that explicitly take into account whether retailers intend to sell the manufacturer's products online or offline. An example of such a practice is *dual pricing*, whereby manufacturers set different wholesale prices for on- and offline sales. To shed light on this debate, we study the competitive effects of dual pricing in a clearinghouse model, in which a manufacturer contracts with so-called hybrid retailers, which sell the manufacturer's product not only in their brick-and-mortar stores but also on an online platform. We find that dual pricing is an essential tool for the manufacturer, in the sense that this vertical restraint allows it to fully exert its monopoly power-whereas uniform pricing does not. This does not necessarily mean, however, that this practice harms consumers and society at large, as the market outcome is distorted by market power regardless of whether dual or uniform pricing is used. In fact, we find that consumers and society benefit from dual pricing if the online market is sufficiently small or if the search costs faced by offline consumers are sufficiently high.

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