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## Charitable giving, suggestion, and learning from others: Pay-What-You-Want experiments at a coffee shop

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## ABSTRACT

We examine consumer behavior under Pay-What-You-Want (PWYW) pricing by conducting a series of field experiments that implemented different pricing schemes at a coffee shop: PWYW, PWYW with charitable giving, PWYW with charitable giving and a suggested price, and—for comparison—a regular fixed price group and a fixed price with giving group. We find that the PWYW scheme, when combined with charitable giving and a suggested price, yields net revenue as large as that under the fixed price scheme. We also find that consumers under PWYW with charitable giving are responsive to a suggested price and seek to learn from others.

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### 1. Introduction

Recent studies found that consumers do not behave like self-ish individuals under the Pay-What-You-Want (PWYW) pricing scheme. Kim, Natter and Spann (2009) conducted three field experiments of PWYW at a buffet restaurant, a movie theater, and a beverage shop, and found that no one actually paid zero at any of the three sites. Gneezy et al. (2010) combined PWYW with charitable giving for souvenir photos at a theme park and found that the alternative pricing scheme, although it promoted charitable giving, is more profitable than the standard fixed price scheme.

Previous studies attempt to determine consumers' decision-making process under PWYW. Using consumer survey responses, Kim, Natter and Spann (2009) find that those who are more altruistic or concerned about fairness pay more, whereas those who are more price-conscious pay less. Gneezy et al. (2012) infer consumers' motivation by comparing results across different treat-

ments and by surveying consumers. They conclude that consumers under PWYW pursue a self-signaling purpose; people are uncertain about their own morality and, thus, want to reinforce their belief that they are nice by paying a positive price when they do not have to do so.

The main aspect of PWYW on which this study focuses is that consumers have the exclusive power to choose their own price but have no knowledge of the proper type of behavior. Given a lack of explicit rules, a normative anchor, or experience, consumers find themselves needing to figure out “the right thing to do.” Such a situation may create significant uncertainty. For example, when an individual visits a foreign country and does not know the country's tipping custom, he may follow his own country's norm but, by doing so, may end up tipping too much or too little. Thus, the individual may follow unverified suggestions or imitate anonymous others around him.

To shed light on consumers' underlying decision-making process under PWYW, we conduct a series of field experiments at a coffee shop in South Korea. Specifically, we implement the standard PWYW, PWYW with charitable giving in which half of the total payment is donated to a charity (PWYW + C), and PWYW with

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charitable giving and a suggested price (PWYW + CS).<sup>1</sup> To the best of our knowledge, our study is the first to introduce a suggested price in the context of PWYW with charitable giving. By comparing PWYW + C and PWYW + CS, we examine consumers' responsiveness to a price suggestion. As benchmark cases, we implement a regular fixed price scheme (FP) and a FP with charitable giving (FP + C). We collect detailed individual-level sales data on items that each consumer purchases, itemized payments, and the exact time of purchase. The individual-level data allow us to examine how consumers are influenced by others' behavior. In doing so, we add field-experimental evidence to the growing body of literature on peer effects or spillover in pro-social behavior (Gächter, Nosenzo and Sefton, 2013; Smith, Windmeijer and Wright, 2015).

There have been several studies examining PWYW theoretically (Isaac, Lightle and Norton, 2010; Chao, Fernandez and Nahata, 2015) and empirically (Chandran and Morwitz, 2005; Kim, Natter and Spann, 2009; Regner and Barria 2009; Riener and Traxler 2012; Johnson and Cui 2013). Gneezy et al. (2010) is the first study to look at consumer behavior under PWYW when it is combined with charitable giving. The fact that not all consumers free ride under PWYW implies that at least some consumers are willing to pay their "fair" share. The opportunity of charitable giving may as well affect the amount of the fair share. To the best of our knowledge, no previous study has replicated the findings of Gneezy et al. (2010) in a different field and further examined the impact of charitable giving, when the treatment is combined together with price suggestion.

Our paper is also related to several recent papers examining the power of suggestion and the role of learning from others' behavior in charitable giving. Edwards and List (2014) conducted a field experiment of university fundraising campaign and found that potential donors are significantly responsive to the treatment of a donation amount suggestion. Some recent papers also found that potential donors are positively influenced by other donors' contribution (Shang and Croson, 2009) and their belief about it (Croson, Handy and Shang, 2009). Martin and Randal (2008) conducted a field experiment at an art gallery where they placed a transparent box for donation collection and manipulated the initial contents in the box. Consistent with the previous studies, they found that the propensity to donate and willingness to donate depend upon the contents in the donation box, which implies that people learn from others (previous donors) about the type of behavior that is appropriate in a given situation.

To summarize our main findings, we first find that PWYW, when combined with charitable giving and a suggested price, yields net revenue as large as that under the fixed price scheme. We do not know whether the profitability of PWYW persists in the long run; however, our findings show its possibility as a successful business strategy, at least as an event-type promotion. Second, we find that consumers under PWYW with charitable giving are responsive to a suggested price and seek to learn from others, implying that consumers face a degree of uncertainty regarding how to behave in this unfamiliar situation.<sup>2</sup> Therefore, they might prefer following external references rather than exploiting the opportunity to maximize their self-interest. Lastly, we find that under PWYW, consumers' sensitivity to charitable giving and a suggested price is salient even with the condition of anonymity.

<sup>1</sup> We chose 50% donation for comparison with the results from Gneezy et al. (2010). We also wanted to check the viability of PWYW as a business model, even in the very short run; obviously, with 100% donation, there is no revenue to the shop.

<sup>2</sup> One theoretical interpretation about suggested price or others' behavior is that they play a role of social information. If so, our findings are supportive of conformity theory, which according to Shang and Croson (2009) suggests that social information is more effective in "ambiguous" situations.

Consumers do not reduce their payments when no other consumers are around, implying that the role of implicit social pressure is not significant.

The remainder of this paper is as follows. Section 2 explains our field experimental design and implementation. Section 3 presents the results of a comparison of revenue across different pricing schemes; we also present a simple model of consumer choice under PWYW and discuss its implications for our results. Section 4 concludes.

## 2. Experimental design and implementation

The field experiments were conducted for five days in November 2012. On each day, we implemented a different pricing scheme during business hours from 7:00 a.m. to midnight: FP on November 12 (Monday), FP + C on 13 (Tuesday), PWYW on 15 (Thursday), PWYW + C on 19 (Monday), and PWYW + CS on 21 (Wednesday). We avoided weekends and attempted not to use different pricing schemes on consecutive days, to prevent possible contamination between treatments. We did not control for the day of the week because we found no particular pattern over time from aggregate sales data before the experimental period. We obtained the original receipts for all consumers, giving us all information available on receipts, such as the time of purchase, the items purchased, cashier identity, and total payment. The only demographic information on consumers is gender as manually recorded on the receipt by the cashier.

The experimental pricing schemes were applied to six beverage items (the best-selling menus in the shop). Their normal prices are KRW 2300, 3000, or 3900 (KRW 1000  $\approx$  USD 1).<sup>3</sup> The shop sells a lot more in addition to these experimental items, allowing us to examine whether special pricing on certain items affects sales of other items. The experiments were not advertised in advance. At the opening time on each day, we put an advertisement in the window of the shop. However, we noticed that almost all consumers come into the shop without recognizing special pricing, indicating that selection should not be a major issue and consumers are comparable across treatments. In fact, we find no significant difference in the number of consumers by treatment. Once consumers come inside, they are again reminded of "today's special prices" using a small poster on the cashier's desk. When charitable giving is involved, we displayed the charity's official banner to describe its purpose.<sup>4</sup>

One might be concerned about the possibility that some customers visited the shop multiple times during our experiment weeks. For example, customers who visited the shop on the day when PWYW was implemented could visit again on the day when PWYW + C was implemented. In such cases, any change in the customer's behavior at the second visit could reflect not only the treatment effect of PWYW + C, but also the carry-over effect from the previous treatment, PWYW.<sup>5</sup> Unfortunately, we cannot identify individual customers in our data, so it is impossible to identify repeated customers. We attempt to address this concern by

<sup>3</sup> The six items are Americano (3000 KRW), Drip coffee with or without sugar (both 2300 KRW), Café Mocha (3900 KRW), Caramel macchiato (3900 KRW), and Vanilla latte (3900 KRW). 1000 KRW is approximately 1 USD. The first item, Americano, accounts for 55.8% of total number of items sold during the experiment weeks.

<sup>4</sup> The charity is a local social welfare center, authorized by the city of Seoul, providing various social services mainly for the disadvantaged (the disabled, elderly or children in poor households). The charity does not have any political or religious orientation. The charity was not selected by the experimenter but by the owner of the coffee shop, who is a regular donor for the organization.

<sup>5</sup> We appreciate an anonymous referee for raising this issue. Since there are customers who visited only once and experienced one treatment only and those who visited multiple times and experienced multiple treatments. In this sense, there are both between- and within-subjects comparisons in our analysis.

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