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Presentation Title

Exploitative Priority Service

(with Eyal Winter)

Abstract

We analyze the implications of introducing priority service on customers' welfare. In monopoly markets, introducing priority service decreases the customers' surplus despite increasing the assignment efficiency: the monopolist extracts from customers a total payment higher than the total efficiency gain generated by the service and hence leaves customers worse off compared with the situation where no priority is offered at all. In duopoly markets with homogeneous customers the equilibrium price and customers' welfare coincide with the monopoly outcome where this monopolist faces half of the market. With heterogeneous customers priority can improve the aggregated customers' welfare, yet in equilibrium service providers extract a very substantial part of the gains of the improved allocation. Our conclusion is that priority service erects barriers to competition that are embedded in the nature of the service provided, with the victims of these barriers primarily being agents with low willingness or low ability to pay for the priority.

Keywords

Priority pricing, queuing, consumer surplus.

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