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Article

Pay-What-You-Want Pricing - A structured review on drivers of prices paid by customers

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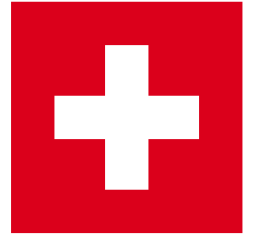
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Pay-What-You-Want Pricing

A structured review on drivers of prices paid by customers

Pay-What-You-Want (PWYW) pricing gives customers full control over a transaction price. It is a reasonable strategy to attract new customers, to offset low turnover periods, or for long-term application. The success and applicability of PWYW depends on various company-, customer-, and context-related factors, which will be discussed in this article.

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Customers increasingly demand empowerment and individualized products and services. More than ever, customers actively participate in activities, such as new product development and even pricing activities, which were previously regarded as solely companies' domain (van Doorn et al. 2010). Whereas the traditional fixed price model does not comprise any customer-seller interaction, participative pricing mechanisms offer customers different levels of participation in the price determination process (Hinz/Creusen 2009).

Pay-What-You-Want (PWYW), the strongest and most progressive form of participative pricing, gives customers full control over the transaction price (Kim/Natter/Spann 2009). In contrast to the traditional fixed price model, customers determine the price they are willing to pay. Sellers have to accept the payment even if it is zero (see Figure 1)

Practical Examples

Several practical examples underline the feasibility of PWYW, particularly for the service industry (see Table 1). These examples show that, despite the risk of customers exploiting their control by paying low prices or even not paying at all, PWYW can be a promising pricing mechanism.

PWYW examples can be found worldwide. For example, when the hotel chain Ibis opened in Germany in 1995, it used a PWYW promotion to attract new customers and create awareness (Frankfurter Allgemeine Sonntagszeitung 2008). Ibis used the same PWYW promotional applications in its hotels in Singapore (2009) and in India (2016) (see Figure 2). Regular prices for rooms at the Singapore Ibis start at 138 Singapore dollars. Average prices paid during the PWYW promotion ranged between 70 and 80 Singapore dollars. According to the marketing director at that time, the

pricing mechanism was initially intended to stimulate sales after the global financial crisis, however it also proved as a good way to measure customers' willingness-to-pay (Lovelock/Patterson/Wirtz 2015).

Another example illustrates the long-term applicability of PWYW. The guided walking tour agency Sandemans New Europe pursues a PWYW strategy since its foundation in 2003. Per year, it offers more than 1.5 million customers guided walking tours in 13 countries worldwide (Sandemans New Europe 2010).

However, there are also examples of PWYW failures. The dating platform Eve 'n' Adam which relied on PWYW had to shut down due to a lack of customers (Kim/Natter/Spann 2010a). The American restaurant Terra Bite Lounge stopped using PWYW, as it primarily attracted young customers who did not pay enough to cover the restaurant's expenses (NY Times 2010).

The success of a PWYW application is thus subject to different influences, which shall be introduced in the following sections.

Outcomes of PWYW

Prices Paid

PWYW is a pricing mechanism that, unlike voluntary donations or tips, aims at avoiding non-payment and maximizing profit. Prices paid refer to the monetary amounts customers voluntarily decide to pay in exchange for the product or service received. Research has shown that customers often pay more than zero and only a small number of customers pay very little when faced with PWYW.

Only occasionally are the prices paid higher than the market price, as in a deli, where the prices paid were 10 percent higher than the market price. Customers express their satisfaction by paying high prices (Kim/Natter/Spann 2009).

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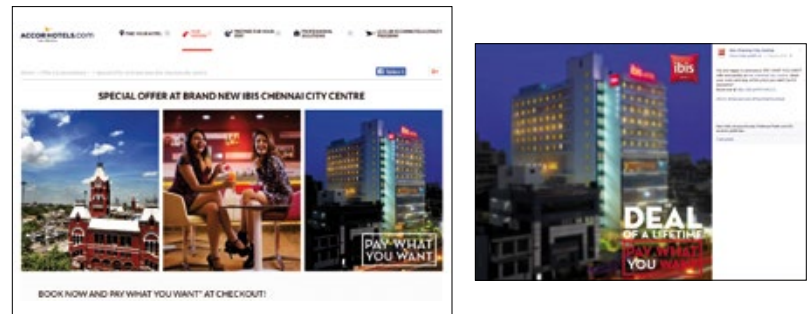
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Fig. 1: Differentiation between Fixed Price and PWYW

Source: Based closely on Kim/Natter/Spann 2009.

Fig. 2: Exemplary PWYW Promotion by Hotel Chain Ibis on the Corporate Homepage and on Facebook

Sources: Accorhotels Homepage 2016, Facebook Page Ibis Chennai City Centre 2016.

However, there is also evidence that customers may take advantage of PWYW and endeavor to obtain a good deal. A study in a cinema context reports that prices paid represented only 70 percent of the market prices. A reason for the low prices may be that customers generally perceive regular cinema ticket prices in Germany too high and unfair. In PWYW they thus have an incentive to pursue own economic benefits and to obtain a (fair) bargain (Kim/Natter/Spann 2009). A PWYW promotion by NH hotels lead to prices paid of only 40 percent of the market price. Prior awareness of the PWYW scheme influences price levels. Custo-

mers who were not aware of the PWYW mechanism paid on average substantially higher prices than those who were aware of the promotion. PWYW promotions might thus also attract customers, who seek to serve their own interest by paying low prices, and thus make a bargain (Gautier/van der Klaauw 2012).

Number of Units Sold

PWYW primarily increases the number of customers. The acquisition of (new) customers and, thus, the increased purchasing intensity increase the overall number of units sold. Conse-

quently, despite occasional lower prices paid, total turnover can nevertheless increase.

However, PWYW may not always be profitable. As Kim/Natter/Spann (2009) show, in two of three studies average prices paid decreased, by 19 percent (study 1) and 28 percent (study 2). In their first study, which was conducted in a buffet lunch context, the number of units sold simultaneously increased by 61 percent, resulting in a total increase of sales by 32 percent, thus indicating a profitable PWYW application. In contrast, in their second study (a cinema ticket context), sales volumes decreased by 30 per-

Table 1: Practical PWYW Examples

	Gastronomy	Hotel & Tourism	Music	Art & Culture	Online
Long-Term Implementation	<ul style="list-style-type: none"> • Wiener Deewan, AT • Berliner Weinerei, DE • Lentil As Anything, AU • Pay As You Please, IRL 	<ul style="list-style-type: none"> • Agilika Lodge, EG • Green Mobility at Maya Hotel, CH • Sandemans Free City Tours, EU 	<ul style="list-style-type: none"> • Cashmusic.org, USA • Moshpfit Tragedy Records, USA • Several Musicians, USA 	<ul style="list-style-type: none"> • Allwetterzoo Münster, DE • Several Museums, USA • Coeurage Theatre, USA 	<ul style="list-style-type: none"> • HumbleBundle.com • Genero.us • Studenten-forschung.de
Promotional Implementation	<ul style="list-style-type: none"> • Etrusca, DE • Little Bay, UK 	<ul style="list-style-type: none"> • Ibis, DE, SG, IND • NH Hotels, BE, NL • Skiing Pass, CH 	<ul style="list-style-type: none"> • Several Musicians, USA 	<ul style="list-style-type: none"> • Dallas Theater Center, USA • Zoologische Forschungsmuseum Alexander Koenig, DE 	

Source: Adapted from Kim/Natter/Spann 2010a.

cent. The combination of lower prices paid as well as less units sold during the PWYW application led to a total sales decrease by 50 percent. In their third study (a context of hot beverages), average prices paid increased by 10 percent. Despite a simultaneous reduction in sales volume by 6 percent, PWYW resulted in an increase in total sales by 3 percent. These results highlight that either prices paid or, alternatively, sales volume should increase to positively affect total sales under PWYW conditions.

Cross-Selling

The sale of products other than those offered under PWYW conditions could also increase. For example, a zoo in Germany reported a 2.5 times higher revenue during the PWYW campaign than in the previous year (Die Welt 2013). This revenue increase can be attributed to cross-selling effects. Due to increased numbers in visitors, not only tickets sales, but also sales of parking spaces and sales in the cafeteria of the zoo increased.

Relationship-Building

PWYW allows direct customer feedback on the perceived value of the of-

fered products or services (Spann/Skiera/Schäfers 2004). Customers thus often consider PWYW fairer than fixed pricing. This perception of a fair price mechanism may also contribute to a customer-friendly, positive reputation and an increase of more loyal customers. Further, after being exposed to PWYW, customers are more likely to spread positive word-of-mouth, or to feel more committed to sellers and willing to reciprocate their thoughtfulness (Kim/Natter/Spann 2010a; 2009).

Strategic Goals of PWYW

Promotion

PWYW increases the publicity a business receives and awareness among (new) customers due to its unconventional character (Kim/Natter/Spann 2010b). Applying PWYW is specifically suitable during low turnover periods to boost revenues. For example, the NH hotels in Belgium and the Netherlands tested PWYW on the weekend before Christmas, when there is usually little demand. Applying PWYW led to most of the participating NH hotels being fully booked, resulting in higher revenues than in the previous year (Gautier/van der Klaauw 2012).

Long-Term Strategy

PWYW can also be a successful strategy in the long term. A two-year field study at a restaurant in Vienna showed that the average prices paid declined slightly once PWYW had been applied for a longer period, but converged at a level that the restaurant deemed acceptable (Riener/Traxler 2012). In addition, as the number of customers, and thus sales volumes, increased, overall the PWYW implementation proved successful. However, if the prices paid are too low, informing customers that PWYW will become a fixed price if the seller's existence is jeopardized, leads to higher prices being paid (Mak et al. 2015).

Conceptual Framework

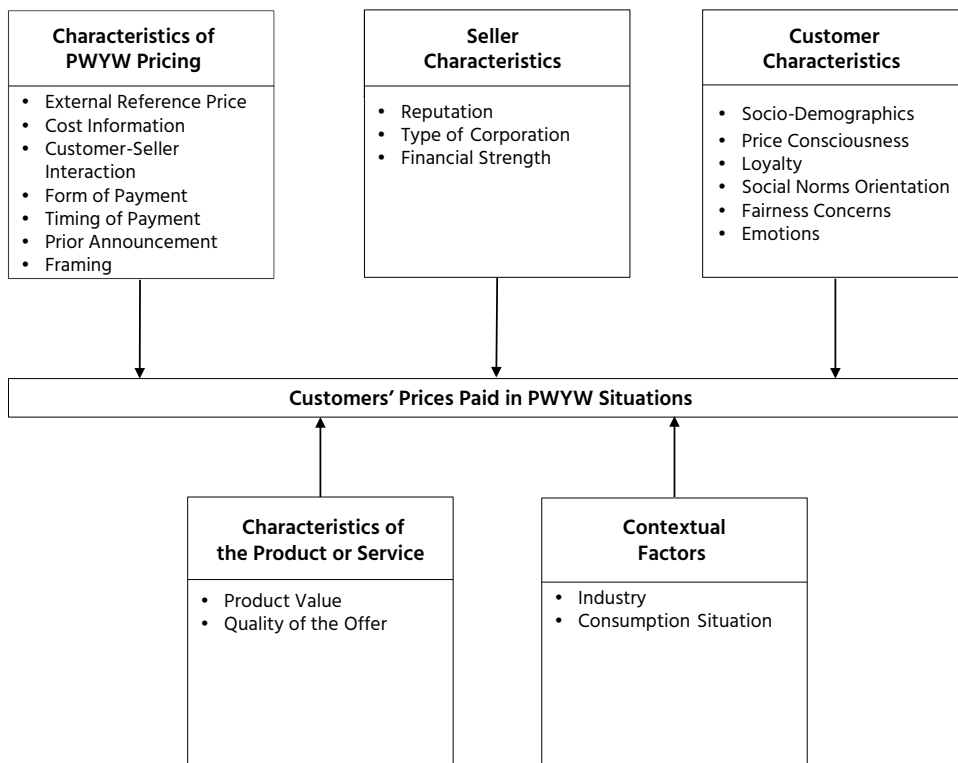
To successfully apply PWYW, practitioners must have profound knowledge of the factors that influence customers in their price-determination and, consequently, drive the prices that they eventually pay. However, to date, review articles on PWYW which provide a comprehensive overview of influencing factors are scarce. Kunter (2012) highlights the advantageousness of PWYW compared to fixed pricing, focusing on the procedural design options of PWYW applications. Since then, the main emphasis of the increasing number of empirical studies on PWYW has shifted to customer characteristics and motives as well as product and context specific success drivers. In our conceptual framework (Figure 3), which will be delineated in the following, we provide a review on important determinants of customers' prices paid in PWYW situations. However, it does not claim to be exhaustive.

Management Summary

PWYW is most suitable for the service industry with products or services of a rather low value.

PWYW can be a good promotional mechanism, as it attracts new customers, thus increases the number of units sold, and strengthens a seller's awareness and positive reputation.

The success of PWYW depends particularly on a specific design that accounts for sellers' and customer's individual characteristics, as well as contextual factors.

Fig. 3: Determinants of Customers' Prices Paid in PWYW Situations

Source: Authors' Own Compilation.

Characteristics of PWYW Pricing

External Reference Price

External reference prices serve as anchor points in PWYW situations. It has been shown that, customers set the prices they wish to pay close to a given external reference price (Kim/Natter/Spann 2009). As such, the provision of an external reference price can lower the risk of customers abusing their bargaining power in PWYW situations (Johnson/Cui 2013).

However, sellers should set external reference prices with care, as these do not always allow them to exploit the

full potential of customers' heterogeneous product valuation and willingness-to-pay (Isaac/Lightle/Norton 2015). When available, customers use minimum prices as an orientation when determining what they wish to pay and understand maximum prices, when available, as caps that they do not wish to exceed. Further, if the provided reference price is perceived as unfair, for example as too high, it has a negative effect on what customers wish to pay (Johnson/Cui 2013). Moreover, Johnson/Cui (2013) show for the context of concert tickets that PWYW with a suggested reference price, framed as the price others commonly pay, raised average prices paid (from \$43.77 to \$49.90).

Also a minimum price, framed as the price threshold participants' payments should exceed, raised average prices paid (from \$43.77 to \$47.00). However, the provision of a maximum price, framed as the price threshold participants' payments should not exceed, resulted in lower average prices paid (from \$43.77 to \$35.77). Similarly, the authors find that, the provision of both, minimum and maximum prices simultaneously, reduced average prices paid (from \$43.77 to \$32.11).

Cost Information

Providing cost information is another way of ensuring that customers have anchor points for their price determination. Normally, customers either have inadequate or no knowledge at all of the seller's costs, or do not take the full range of costs into account (Schons et al. 2014).

If sellers disclose their costs, customers can take these into consideration when determining the price they wish to pay. In fact, studies show that customers increase their prices paid in keeping with sellers' cost increases to ensure a fair exchange. However, this is only the case if customers perceive sellers' costs as legitimate (Schmidt/Spann/Zeithammer 2015; Jang/Chu 2012).

Customer-Seller Interaction

The level of interaction between customers and sellers during the consumption experience, or the payment phase, has a strong impact on the prices paid. Studies have revealed that these increase if customers interact directly and frequently with the seller (Kim/Kaufmann/Stegemann 2014). Conversely, customers pay lower prices in a PWYW situation if less customer-seller interaction characterizes the transaction.

Form of Payment

Customers' payments are higher if given personally to the seller (Kim/Kaufmann/Stegemann 2014). In contrast, if payment is made anonymously (Riener/Traxler 2012), customers tend to pay less.

Further, the payment mechanism – cash or card – might influence the prices customers choose to pay. Under fixed price conditions, customers' willingness-to-pay is higher if they pay with a credit card (Prelec/Simester 2001). This could possibly hold true in the context of PWYW.

Timing of Payment

Studies provide evidence that payment after consumption, or after testing an offer, leads to higher prices being paid. A possible explanation could be that the customers' uncertainties about the quality of the offer have been eliminated (Regner 2015; Weisstein/Kukar-Kinney/Monroe 2016). Consequently, payment after testing an offer also encourages new and risk-averse customers to make purchases, as they have minimized the risk of wrong investments (Egbert/Greiff/Xhangolli 2015).

Prior Announcement

Prior announcement of the application of PWYW might specifically attract price-conscious customers, or those wishing to bargain. Promotional campaigns of PWYW also attract customers tending to pay lower prices than the normal prices (Gautier/van der Klauw 2012). Sellers should therefore only announce the payment mechanism at their point-of-sale during its application period and not announce it beforehand.

Framing

Some studies reveal that the payments are higher if the price mechanism is called "Pay What It Is Worth to You" or "Pay What You Believe/s Fair" (Machado/Sinha 2012; Sleesman/Conlon 2016). An emphasis on the value of the offer thus influences the average prices paid positively.

price levels (Kim/Kaufmann/Stegemann 2014). A suitable example – omnipresent in many rural areas – are agricultural products, such as flowers or strawberries, offered at stalls, or that customers can harvested in a field. In a region in southern Germany, customers anonymously pay the amount due for their purchase in money boxes. Roughly 80 percent of customers pay the suggested prices. The higher the quality of the offer, and the more familiar customers are with the seller, the higher the prices paid (Süddeutsche Zeitung 2017).

PWYW does not only enable companies to increase awareness and attract new customers, but also addresses customers' individual product/service valuation.

Seller Characteristics

Reputation

Research shows a positive relationship between a seller's reputation as a family business and the prices customers choose to pay, while a large company's equally good reputation has no effect on

stated prices. The higher the quality of the offer, and the more familiar customers are with the seller, the higher the prices paid (Süddeutsche Zeitung 2017).

Type of Corporation

Studies on PWYW show that customers increasingly empathize with small, local family businesses rather than with large, anonymous, international corporations (Kim/Kaufmann/Stegemann 2014). Sellers who do not run a purely profit-oriented business, but pursue a social and ethical strategy, receive higher payments than those who pursue opposing strategies (Jung et al. 2014; Machado/Sinha 2012).

Financial Strength

Building on the above finding, customers might find low(er) prices paid justified, or feel less guilty when having paid low(er) prices, if they perceive a seller as financially sound or unsympathetic (Leon/Noguera/Tena-Sanchez 2012). One can thus presume that customers (unconsciously) decide which

Lessons Learned

1. Sellers should reflect on the suitability of PWYW, which depends on the type of business and goods/services on offer.
2. PWYW is suitable as a promotional strategy to offset low turnover periods.
3. Often PWYW lowers the prices paid by customers but increases the total sales volume owing to a larger customer base.

seller they wish to support by paying high(er) prices and which seller they do not wish to support, or even wish to actively harm by paying them low(er) prices (Gerpott 2016). Sellers should therefore be aware of their reputation, their social ties, and operating strategy before implementing PWYW.

Customer Characteristics

Socio-Demographics

Studies find a positive correlation between customers' age and the prices paid. Older customers tend to pay more. This might be related to the positive correlation between income and prices paid, as income and spending power generally increase with age (Kim/Kaufmann/Stegemann 2014; Kunter 2015).

Further, education and employment tend to influence the prices paid (Kim/Natter/Spann 2009; Riener/Traxler 2012). Highly educated customers might be more prone to engage in the cognitive processes required to determine the prices paid in a PWYW situation. These customers might also reflect more on the provided information, such as the cost information, and adjust their payments accordingly.

Price Consciousness

Commonly, price-conscious customers focus on getting a bargain, which means the prices they choose to pay are lower (Schons et al. 2014; Kim/Natter/Stegemann 2014). Thus, if sellers' customer base is very price-conscious, PWYW might not be an appropriate pricing mechanism.

Loyalty

Customers pursuing long-term relationships with sellers are willing to pay high

er prices for their products or services. This is primarily driven by their wish for the seller to remain in business (Schmidt/Spann/Zeithammer 2015). PWYW is thus particularly suitable for sellers with a loyal customer base.

Social Norms Orientation

Customers' orientation towards social norms triggers higher prices paid in PWYW situations. If customers do not pay appropriate prices, they face non-monetary costs. These include emotional sanctions, such as feelings of guilt and shame, as well as sanctions by others, such as social disapproval (Kunter 2015; Gneezy et al., 2012). Consequently, descriptive norms ('what others do') influence customers (Jang/Chu 2012). Sellers can take advantage of this by phrasing the external reference prices as descriptive norms.

Fairness Concerns

Customers tend to perceive the transaction as unfair if they know that others have purchased the same product at a lower price (Marett/Pearson/Moore 2012). Thus, in order to avoid an unfair transaction, customers will adjust their prices to those of fellow customers. Sellers should therefore avoid making a customer's payment amount visible to other customers, unless it is above the usual market price.

Emotions

Sometimes PWYW can also evoke negative reactions in customers. The perceived effort to determine the price may cause negative emotions such as guilt, frustration, and stress (Gerpott/Schneider 2016; Santana/Morwitz 2011). Sellers should thus closely monitor customers' reaction and feelings

towards PWYW. Asking for immediate customer feedback might help.

Characteristics of the Product or Service

Product Value

PWYW is particularly suitable for low value products and less so for high value products, such as holiday packages or hotel rooms. Absolute prices paid decrease relative to the product value. For example, in a restaurant/café setting, the payments compared to the product's value decrease in respect of products worth more than EUR 10 (Kim/Kaufmann/Stegemann 2014). The reason for this could be that as the product value increases, the increased savings potential replaces the influence of fairness considerations and social norms on

Main Propositions

1. PWYW is a promising pricing mechanism that can be applied in a wide range of sectors, such as gastronomy, hotel, art, and culture.
2. Achieving customer satisfaction is of the utmost importance as customers can reward or punish a seller directly via their prices paid.
3. PWYW allows sellers to exploit the full potential of customers' heterogeneous product/service valuation.
4. PWYW increases customers' likelihood of returning, of spreading positive word-of-mouth, and of feeling more committed to a seller.

pricing. Customers are thus more likely to exploit the PWYW mechanism if the product value increases (Leon/Noguera/Tena-Sánchez 2012).

Quality of the Offer

Sellers' commitment to PWYW serves as an indicator of quality for customers. If they experience inferior quality, they can pay less. In contrast, if customers perceive the quality of the product or service they enjoyed as high, the prices they pay increase (Weisstein/Kukar-Kinney/Monroe 2016).

Furthermore, customers who are uncertain about the quality of or their satisfaction with a product or service can

adapt their payments, so that the general risk for customers in a PWYW situation is lower than in traditional, fixed-price ones (Egbert/Greiff/Xhangolli 2015).

Thus, PWYW might be more difficult to implement in respect of new products. Since customers have not yet experienced them, they cannot assess their value (Gerpott 2016).

Contextual Factors

Industry

The success of PWYW is dependent on the industry in which it is applied. Research shows that this pricing mechanism is most suitable for industries with

low variable and low marginal costs, but with excess capacities (Kim/Natter/Spann 2010b). Practical examples of PWYW can be found in the gastronomy, museum, and hotel sectors, as well as in the music, and software sectors.

Consumption Situation

Finally, the consumption atmosphere influences the prices customers choose to pay. A positive atmosphere, in which customers feel comfortable, might lead to higher prices paid (Egbert/Greiff/Xhangolli 2015). In addition, it is assumed that customers are willing to pay more in hedonic consumption situations (Stegemann 2016).

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Conclusion


Applying PWYW bears various benefits for sellers (see Table 2 for an overview) and can thus be a promising pricing mechanism, in particular in the service industry. PWYW does not only enable companies to increase awareness and attract new customers, but also addresses customers' individual product/service valuation. Nevertheless, applying PWYW also bears some risk for sellers such as low payments and negative cognitive or affective customer reactions such as stress or shame. Thus, sellers should carefully design a suitable PWYW application compatible with their company. 

Table 2: Potential Effects of PWYW Application

	Potential Effects of PWYW Application	Exemplary Study
Potential Benefits	Innovative Corporate Image	Kim, Natter and Spann (2009)
	Enhanced Reputation	Gneezy et al. (2010)
	Positive Word-of-mouth	Kim, Natter, and Spann (2009)
	Acquisition of New Customers	Kim, Natter, and Spann (2010b)
	Consideration of Customers' Heterogeneous Product Valuation	Isaac, Lightle, and Norton (2015)
	Consideration of Customers' Heterogeneous Willingness-to-pay	Chandran and Morwitz (2005)
	Cross-Selling Effects	Kim, Natter, and Spann (2010b)
Potential Risks	Customers' Perceived Cognitive Effort (e.g. Complexity of Price Determination)	Gerpott and Schneider (2016)
	Customer's Negative Emotions (e.g. Shame)	Santana and Morwitz (2011)
	Lower Payment Amounts Compared to Fixed Price	Leon, Noguera, and Tena-Sanchez (2014)

Source: Authors' own Compilation.

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