

Privacy, price discrimination, and the seeds of capitalism's destruction

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October 28, 2015

Main thesis:

- technology is leading to fundamental changes in our society
- those changes are even more fundamental than generally perceived, threatening the incentives that have made the market system as dynamic as it has been
- price discrimination, facilitated by erosion of privacy, has a key but underappreciated role in these developments

Some preliminary caveats:

- presentation is US-centric, although main points should have wide applicability
- these are personal views, and some are yet to be documented (a paper on this topic will be available soon)

Lessons from the past:

- 19th century railroads presented a similarly fundamental challenge to the market economy
- price discrimination was the basic cause of complaints
- railroad price discrimination led to the first substantial US federal government intervention in the conduct of the economy
- expect that similar reaction will lead even US business interests to call for regulation on how information is used

More lessons from the past:

- US regulation of railroads led to an inefficient and sclerotic system
- almost complete deregulation (Staggers Act, 1980) (enabled by the rise of partially competing transportation technologies) produced a dramatic improvement
- quality of regulation may become main determinant of how successful an economy is

Lessons from the present:

Two recent (September 2015) events that attracted wide public notice:

- rise in US price of generic drug, Daraprim, from \$13.50 to \$750 per tablet
- VW emissions tests fraud

They point to a future dominated by search for choke points, and by cheating (or, in more polite terms, obfuscation).

Lessons from the present (cont'd):

Positive sides to these developments (only slightly in jest):

- solution to problem of jobs: we will all be busy cheating each other and detecting cheating
- reason this is less of a joke than it might seem: there are theories that human intelligence developed precisely for those purposes, as in small social groups of early *Homo sapiens* there were high rewards for successful but hidden cheating, and incentives to detect such behavior
- important form of human cheating involves self-deception: 75% of the people are above average,

Modern economy:

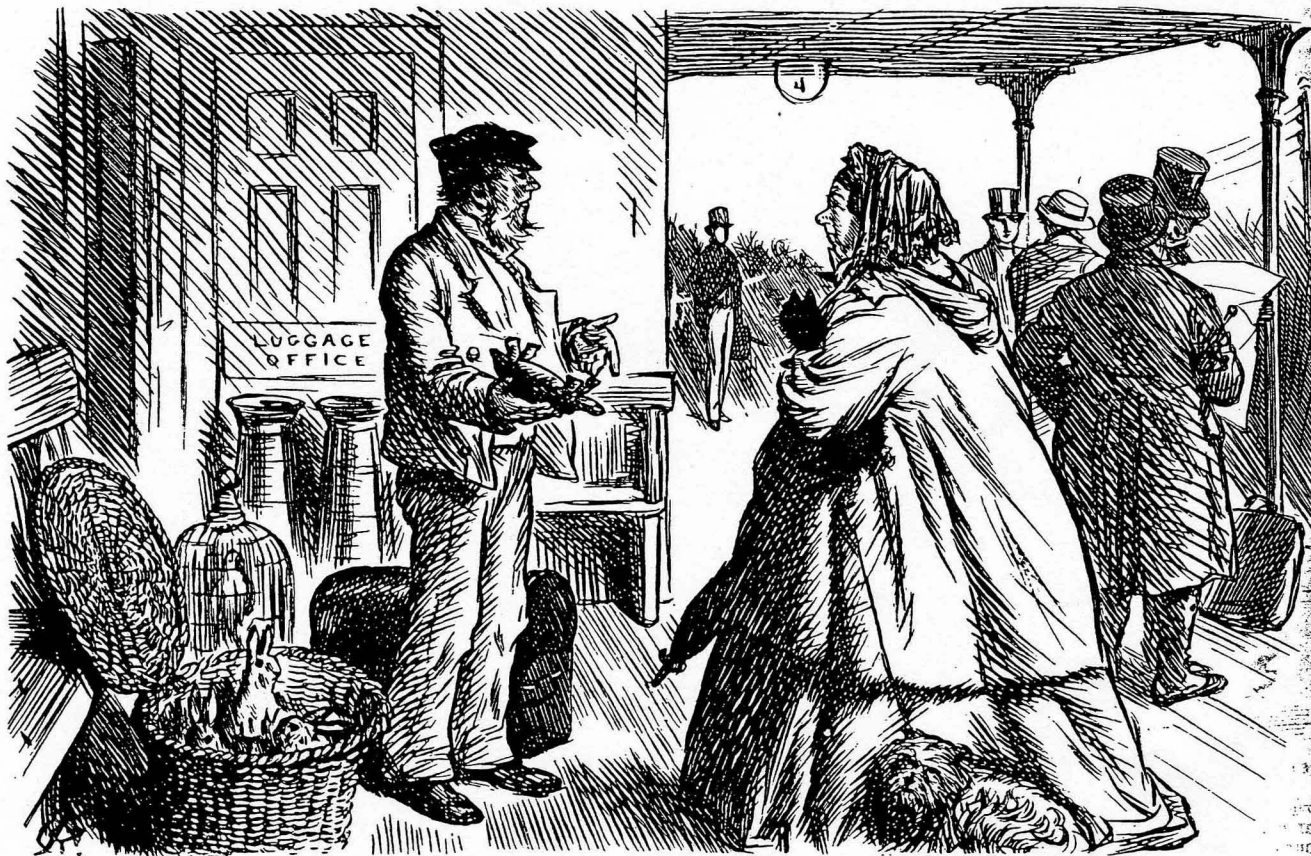
- based on dominance of the market and of corporations
- both are recent creations, and almost surely crucial to the dramatic shift to rapid growth and wealth of the last 200 years
- market disliked by both the public and corporations
- erosion of market principle by price discrimination (individual prices eliminate the basic market mechanism of a single price, which forces sellers to compete just on quality and price)

Modern economy (cont'd):

- too much attention paid to the obvious dangers from new monopolies that seem to be arising (platform providers such as Google, Facebook, Apple)
- too little attention paid to all the other actors who are able to use Big Data, analytics, ..., to create barriers to competition and extract value
- possible sign of the decline of market economy: paradox of high corporate profits, low interest rates, and low entrepreneurial activity

Price discrimination:

- very important role in economy
- role understood intuitively even by ancient policy makers, way before the theory was developed by the French econo-engineers of the 1840s
- never-ending quest to reconcile economic incentives to price discriminate with public concern about fairness



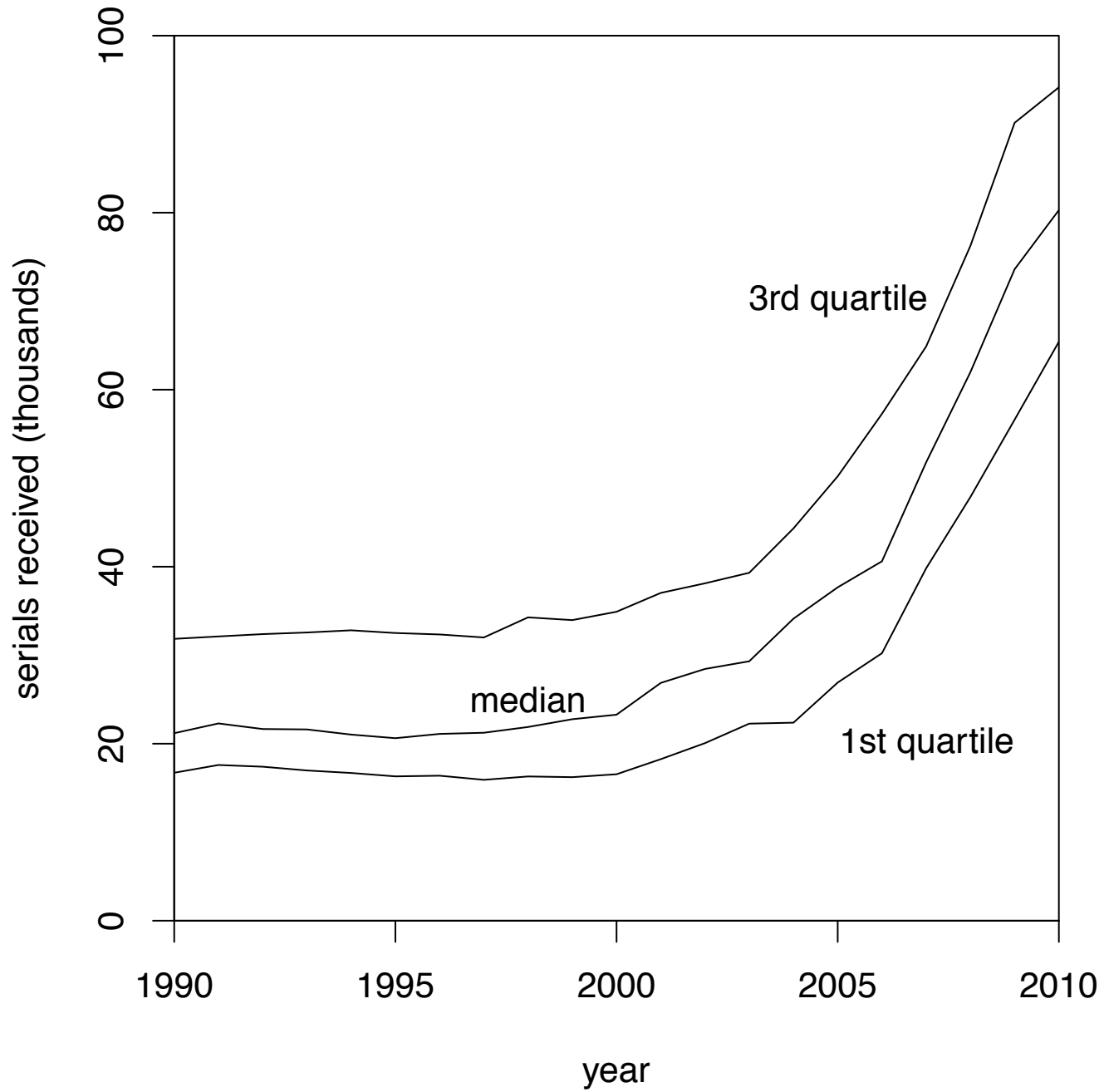
ZOOLOGY.

Railway Porter (to Old Lady travelling with a Menagerie of Pets). "STATION MASTER SAY, MUM, AS CATS IS 'DOGS,' AND RABBITS IS 'DOGS,' AND SO 'S PARROTS; BUT THIS ERE 'TORTIS' IS A INSECT, SO THERE AIN'T NO CHARGE FOR IT!"

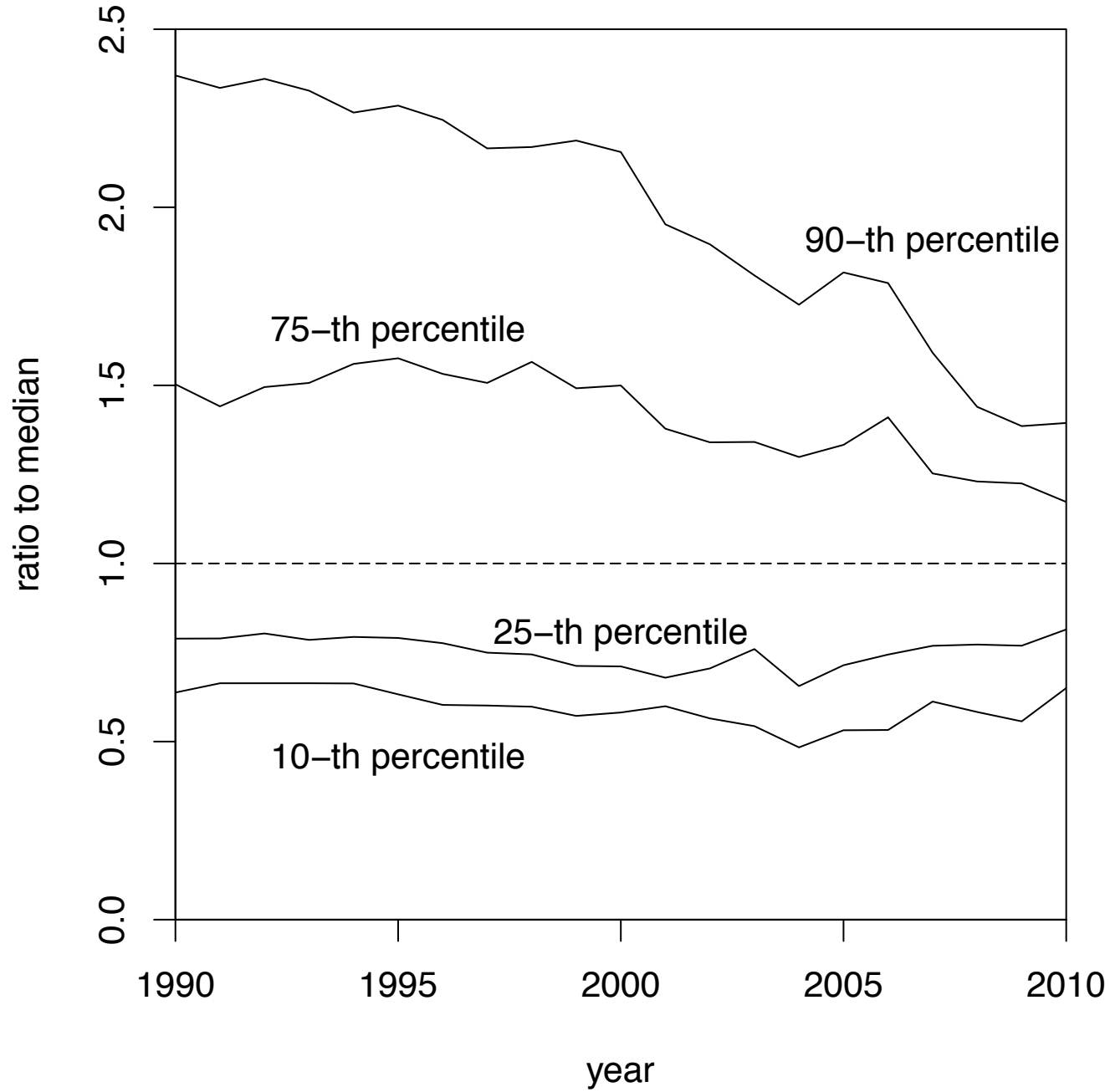
Price discrimination dangers:

- price discrimination usually increases output
- can shift benefits to either consumers or producers
- most fundamental danger not being discussed yet:
undermining the incentives that drive the current
economy

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Fundamental danger:

- secure system of property rights very important for economic development
- price discrimination taken to its extreme is equivalent to abolition of rule of law, and letting many mafias run free
- decreases ordinary economic rewards, and also offends human sense of fairness, and breaks down the trust that is vital to efficient markets

Conclusions:

- great promise for further economic progress
- great danger to the basic incentives that drive our current system, danger of slipping into a few form of feudalism
- regulation on use of information and on pricing likely to increase, even in US
- good regulation very tricky, no simple solutions

More information, papers, etc.:

<http://www.dtc.umn.edu/~odlyzko/>

or just google/bing “odlyzko”