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Management Insights

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Customer-Driven Misconduct: How Competition Corrupts Business Practices (p. 1725)

[Victor Manuel Bennett](#), [Lamar Pierce](#), [Jason A. Snyder](#),
[Michael W. Toffel](#)

When is a good thing a bad thing? Competitors who fight for customers may cut corners in order to get their business. Competition among firms yields many benefits but can also encourage firms to engage in corrupt or unethical activities. The authors suggest that competition can lead organizations to provide services that customers demand but that violate government regulations, especially when price competition is restricted. Using 28 million vehicle emissions tests from more than 11,000 facilities, the authors show that increased competition is associated with greater inspection leniency, a service quality attribute that customers value but that is illegal and socially costly. Firms with more competitors pass customer vehicles at higher rates and are more likely to lose customers whom they fail, suggesting that competition intensifies pressure on facilities to provide illegal leniency. The authors also show that, at least in markets in which pricing is restricted, firms use corrupt and unethical practices as an entry strategy. The insight for management: Highly competitive environments may create perverse incentives along legal and ethical lines.

Measuring the Effect of Queues on Customer Purchases (p. 1743)

[Yina Lu](#), [Andrés Musalem](#), [Marcelo Olivares](#),
[Ariel Schilkrut](#)

How does the size of queues affect sales? The authors conduct an empirical study to analyze how waiting in line in the context of a retail store affects customers' purchasing behavior. The authors collected data at a deli counter via video recognition technology over a period of nine months and cross-referenced it with point-of-sales data. They find that waiting in line has an escalating effect on purchases; longer lines

are dramatically more discouraging than shorter ones. Interestingly, customers appear to focus mostly on the length of the queue, without adjusting enough for the speed at which the line moves—despite the fact that a single queue generally provides better service. An implication of this finding is that pooling multiple queues into a single queue may increase the length of the queue observed by customers and thereby lead to lower revenues, even though service is better. The authors also find that bargain-hunting customers are more willing to wait in lines; thus, the service strategy also has price implications. The insight for management: Those developing service strategies in services with queues must consider consumer psychology as well as operational efficiency.

How Do Firm Financial Conditions Affect Product Quality and Pricing? (p. 1764)

[Gordon Phillips](#), [Giorgo Sertsios](#)

The authors analyze the interaction of firm product quality and pricing decisions with financial distress and bankruptcy in the airline industry. They consider an airline's choices of quality and price as dynamic decisions that trade off current cash flows for future revenue. They examine how mishandled baggage, on-time performance, and pricing are related to financial distress and bankruptcy, controlling for the endogeneity of financial distress and bankruptcy. They find that an airline's quality decisions are differentially affected by financial distress and bankruptcy. Product quality decreases when airlines are in financial distress, consistent with financial distress reducing a firm's incentive to invest in quality. In contrast, during bankruptcy product quality increases relative to financial distress. In addition, the authors find that firms price more aggressively when in financial distress consistent with firms' trying to increase short-term market share and revenues. The insight for management: A firm's financial conditions may directly affect the quality and pricing of its services.

The Emergence of Opinion Leaders in a Networked Online Community: A Dyadic Model with Time Dynamics and a Heuristic for Fast Estimation (p. 1783)

[Yingda Lu, Kinshuk Jerath, Param Vir Singh](#)

Online ratings, rankings, and reviews are prevalent on many retail sites. Do different opinions carry more or less weight with prospective buyers? The authors study the drivers of the emergence of “opinion leaders” in a networked community where users establish links to others, indicating their “trust” for the link receiver’s opinion. This leads to the formation of a network, with some individuals becoming the opinion leaders. The authors find that, in the Epinions network, both the widely studied “preferential attachment” effect based on the existing number of links to an opinion giver and the number and quality of reviews written are significant drivers of new incoming trust links to a reviewer. However, over time the influence of the opinion leaders fades. The insight for management: The design of online review communities should consider the important influence of quality and quantity of opinions provided by opinion leaders.

Designing Buyback Contracts for Irrational But Predictable Newsvendors (p. 1800)

[Michael Becker-Peth, Elena Katok, Ulrich W. Thonemann](#)

In the face of uncertainty, are supply chain managers rational? One of the main assumptions in research on designing supply contracts is that decision makers act in a way that maximizes their expected profit. The authors conduct a number of laboratory experiments that demonstrate that this assumption does not hold. Specifically, faced with uncertain demand, decision makers place orders that systematically deviate from the expected profit-maximizing levels. The insight for management: One must account for tastes; a behavioral model better explains contracting outcomes than contracts designed using the standard rational optimization model.

Price Competition Under Mixed Multinomial Logit Demand Functions (p. 1817)

[Margaret Aksoy-Pierson, Gad Allon, Awi Federgruen](#)

How do competitive markets perform when customers can be segmented? The authors estimate the performance of a market that is partitioned into a finite set of market segments. They characterize the equilibrium behavior of this class of market models. The insight for management: Modeling approaches can lead to a better understanding of the performance in equilibrium conditions of segmented markets.

Alleviating the Patient’s Price of Privacy Through a Partially Observable Waiting List (p. 1836)

[Burhaneddin Sandıkçı, Lisa M. Maillart, Andrew J. Schaefer, Mark S. Roberts](#)

What is the price of patient privacy in the case of a liver donation waiting list? In the United States, end-stage liver disease patients join a waiting list and then make accept/reject decisions for transplantation as deceased-donor organs are offered to them over time. These decisions are largely influenced by the patient’s prospect for future offers, which can be ascertained most accurately by knowing the entire composition of the waiting list. Under the current transplantation system, however, the United Network for Organ Sharing (UNOS), in an effort to strike a balance between privacy and transparency, publishes only an aggregated version of the waiting list. It is not clear whether the published information is good enough (compared with perfect information) to help patients make optimal decisions that maximize their individual life expectancies. The authors compare, in a clinically driven numerical study, the results with perfect and imperfect information. They assess the quality of the published imperfect information as measured by a patient’s so-called price of privacy, measured in the opportunity loss in expected life days due to a lack of perfect waiting list information. The insight for management: The currently published partial information is nearly sufficient to eliminate this loss, resulting in a negligible price of privacy and supporting current UNOS practice.

What Are Investors Willing to Pay to Customize Their Investment Product? (p. 1855)

[Dennis Vrecko, Thomas Langer](#)

Even though buy-and-hold (B&H) investment strategies can take the risk tolerance of an investor into account by specifying a suitable stock proportion, the outcome profiles of B&H strategies are restricted to a specific class of return distributions. For investors with particular risk preferences, further customization should thus provide additional value. The authors investigate the strength of preference for such customized distributions and draw conclusions about the demand for personalized investment products. In two experimental studies, 256 participants could adjust the return distribution of an initially chosen B&H investment by using an interactive software program. The authors also surveyed real investors at an investors fair to compare their preferences with those of the main pool of student subjects. The insight for management: Most investors make extensive use of the customization option, and many are willing to pay a substantial fee for this additional flexibility.

Consideration Set Formation with Multiproduct Firms: The Case of Within-Firm and Across-Firm Evaluation Costs (p. 1871)

Lin Liu, Anthony Dukes

How many firms and how many products should be considered in evaluating potential suppliers? The authors evaluate a situation in which firms carry multiple products and consumers incur evaluation costs not only across firms but also within firms. Consumers judiciously decide the number of firms to include in their consideration sets as well as how many products from those firms. This decision depends on the relative trade-offs of evaluating an additional product and whether it is from a firm already included in the consideration set or from an entirely new firm. The composition of consumers' consideration set affects how firms compete in prices and in the number of products to offer. The authors find that firm differentiation can reduce firms' product lines and that within-firm evaluation costs have either a positive or a negative effect on firms' prices. The insight for management: Within-firm evaluation costs and across-firm evaluation costs are different constructs; the number of products that firms offer in equilibrium can exceed the socially optimal level if within-firm evaluation costs are significant.

Do Hedge Funds Outperform Stocks and Bonds? (p. 1887)

Turan G. Bali, Stephen J. Brown, K. Ozgur Demirtas

Hedge funds' extensive use of derivatives, short selling, and leverage and their dynamic trading strategies create significant nonnormalities in their return distributions. Hence, the traditional performance measures fail to provide an accurate characterization of the relative strength of hedge fund portfolios. The authors set out to determine which hedge fund strategies outperform the U.S. equity and/or bond markets. The insight for management: The long/short equity hedge and emerging markets hedge fund strategies outperform the U.S. equity market, and the long/short equity hedge, multistrategy, managed futures, and

global macro hedge fund strategies dominate the U.S. Treasury market.

Mixed Bundling in Two-Sided Markets in the Presence of Installed Base Effects (p. 1904)

Yong Chao, Timothy Derdenger

How does bundling affect prices in a market where there is an established installed base, such as video games? The authors determine that mixed bundling causes prices to fall on both sides of the market. They find that mixed bundling acts as a price discrimination tool segmenting the market more efficiently. Interestingly, as a by-product of this price discrimination, the two sides are better coordinated, and social welfare is enhanced. The authors test these theoretical predictions in the video game console market. The insight for management: Bundling and price discrimination has market efficiency creating potential in two-sided markets with an installed base.

Implications of Hyperbolic Discounting for Optimal Pricing and Scheduling of Unpleasant Services That Generate Future Benefits (p. 1927)

Erica L. Plambeck, Qiong Wang

Why do so many people have gym memberships that they never use? People tend to lack the self-control to undergo an unpleasant service that would generate future benefits; no pain, but no gain. Planning in advance, people may naively overestimate their self-control and join the gym with all good intentions. How does such behavior affect optimal pricing? The authors show that the welfare-maximizing usage fee and the revenue-maximizing usage fee decrease with customers' lack of self-control. Charging for a subscription, in addition to or instead of per-use fees, increases revenue, especially when subscribers are naive. If customers are heterogeneous in their self-control and naiveté, priority scheduling can dramatically increase welfare and revenue. The insight for management: Optimally, gym memberships (and the like) are inexpensive because they are sold to people who underuse them.