

Quality Uncertainty and Bundling

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Abstract: Bundling is the practice of selling certain products together rather than individually. Bundling is sometimes associated with the exercise of market power, as with "block booking" of motion pictures. Bundling also seems to be a means by which buyers and sellers can moderate the effects of exogenous uncertainty, and so its use may be motivated in certain cases even though monopoly power is absent. For example, bundling may discourage selective rejection of items below average in quality, and this may be desirable if it is costly for buyers to inspect prior to purchase or if it is costly or impossible for sellers to resell rejected items. We specify a model in which bundling can be an efficient means of moderating the effects of uncertainty. We also report results of double auction trading in which bundling emerges naturally; bundles are preferred when they offer an efficiency advantage.