

Competition and Consumer Search

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Abstract

We study a growing market in which consumers must pay a cost to learn whether a firm's product is a good fit. Prices are publicly observed, but match quality is not. Consumers face repeated purchase opportunities that arrive as a Poisson process, and their match values are persistent. In equilibrium, firms initially offer the product for free and then randomize over the time at which they monetize by raising their price, with monetization occurring at an increasing rate as the market matures. This endogenous acceleration lowers consumers' outside option from re-entering search, amplifying firms' market power. Firms that monetize earlier become smaller, “niche” providers charging higher prices, whereas firms that monetize later achieve larger scale and charge lower (though rising) prices. We characterize the equilibrium dynamics and derive testable predictions for the joint evolution of prices, churn, and firm size.

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