

# Welfare Impact of Grey Market: Consumer's Perspective

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## Abstract:

*This paper analyses the welfare impact of the grey market on the consumers. A survey has been conducted on the people in the age group of 20-30 in order to identify the application of the economics definition of consumer surplus in real life and on that basis, we have analyzed whether the grey market is a boon or bane to the consumer. The whole paper is divided into three sections. The first section deals with the introductory part with the conceptual framework of the grey market and how the grey market is different from other forms of the market. Section -2, deals with the advantages and disadvantages of the grey market. Section -3 deals with the main concern of the paper i.e. what welfare means to consumer and how the grey market increases the welfare of the consumers. Accounting implication of the grey market on the manufacturer and the authorized dealers has not been analyzed.*

**Keywords:** consumer surplus, consumer, survey, welfare, greymarket

## I. Introduction

Since the mid 1980s there has been a growing interest in grey market, also known as parallel import. Grey market (parallel import) is the market where the product is bought and sold outside the manufacturer's authorized trading channel. For example, if the store owner bought the product from an unauthorized channel than it is said that the product is sold in grey market.

Grey market is also known as parallel import as the seller who is importing and selling the product through unauthorized channel is not permitted by the producer to sell the product in the designated market and as the product is being imported product therefore is considered parallel to the genuine import.

Does the grey market which sells genuine product through unauthorized dealers really increases the welfare of the consumers or is it a false reality (assumption) of this market? No doubt, that the products which are being sold through the grey market are generally less in price but do these product provides value for money to the consumers? The paper tries to find answers of these questions.

## II. Conceptual framework of Grey Market

### A. Grey market is different from other forms of market

There are other forms of market which are often confused with the grey market. The reason may lies in the very origin of the market. But this market is far from these types of market in product quality.

Grey market is different from black market, because in the black market those goods are imported which are legally restricted but in case of grey market the goods are not legally restricted but they are sold outside the normal distribution channel. For example, imports of fire arms are legally restricted in some countries and such imports constitute black market.

Grey market should not be confused with counterfeit market as well. The counterfeit products generally have fake company logos and brands. In the case of goods, it results in patent infringement and trade mark infringement.

Thus, grey market goods are "legal (different from black) and genuine (different from counterfeit) goods" which are sold outside the normal distribution channels by the sellers, having no relationship with the manufacturer of the good.

### B. Many Shades of Grey Market

There are many types of business activities exist which represent different shades of grey market i.e.

- 1) Goods produced in a country for export which is then imported back into the country without the authorization of the trademark owner. For example, If US manufacturer is exporting good A to India and if that good is imported back into India without the US manufacturer's permission then it is a grey market.
- 2) Unauthorized import competing with domestically produced goods.  
For example, if Coca Cola is producing Coca cola for US and Mexico which are different in taste and Mexican Coca Cola sold in US and liked by US consumers then it will be competition for US Coca cola market.
- 3) Unauthorized imports competing with authorized imports.

For example, a manufacturer from US exports some product to AB Ltd of India. AB Ltd is the authorized dealer of the US manufacturer. The same product is sold by YZ Ltd but it is not the authorized dealer than YZ will be a competitor of the AB Ltd.

The most common type of grey market is the sale of imported goods (brought by small import companies or individual not authorized by the manufacturer) which would otherwise be more expensive in the country they are imported to. In other words, the most prevalent form of the grey market is the importation of goods whose price rises sharply when they are imported through the authorized channel of the manufacturer.

### C. *Reasons for Grey Market:*

According to Krechevsky, the reasons for existence of grey market are as follows:

- 1) *Price discrimination in different countries:* Prices of the goods bearing identical trademarks are generally sold at different prices in different countries which give rise to arbitrage. And thus give incentive for the development of grey market. For example- Electronics are cheaper in Singapore as compared to India and therefore being imported to India by unauthorized dealers, giving rise to parallel import.
- 2) *Scarcity driven market:* Grey market arises when the authorized sellers are unable to synchronize demand and supply in various markets. For example, when iPhone was first launched, there were shortages in the UK, so people were bought iPhone from other markets. But Scarcity driven grey market is an aberration.
- 3) *Global nature of marketing:* As the world turns into global village, the marketing is not restricted to the country boundaries only. So, marketers have been able to do marketing on a world wide scale, thereby, taking commercial advantage of global operational differences, similarities and opportunities in order to meet global objective. For example: Before launching iPhone-5 in India, Indian people were aware of it because of the global nature of the marketing.
- 4) *Improved communication among markets:* With the development in the technology the access of the marketer to consumers has increased. For example:-Various auction sites such as e-bay have provided seller a platform to access different consumers across different countries.
- 5) *Fluctuation in Exchange rate:* Exchange rates are subject to changes according to economic conditions of the countries. Therefore exchange rate volatility creates profit opportunities for the sellers and thus give rise to a new form of market known as grey market. For example, the strong dollar had provided an opportunity with grey market to bring Caterpillar's equipment into US at lower prices than domestically produced goods.
- 6) *Ease with each product moves across nations:* With the globalization, there has been substantial reduction in barrier to trades such as import tariff, custom duty which lead to an easy movement of goods across nations.
- 7) *Excess inventory:* It can be other source of parallel import as when an authorized dealer cannot sell its inventory to consumers, it may move the left over items to unauthorized dealer. For example, in the high-fashion apparel market, an authorized dealer has incentive to maintain excess inventory as it can move the excess inventory to the unauthorized dealers and still make the profit as the margins are significantly high.

### *Negative and Positive Impact of Grey Market*

As there is two face of a coin, thus the grey markets also have some positive and negative effects on different constituents of distribution channel. On one hand, grey market leads to the dilution of exclusivity, reduction in manufacturer's profit, creates free riding problem. On the other hand, Grey market c

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creates new customer base in existing market, give wide choice to the consumer and helps in exploring the new market.

### III. Grey market's effect on consumers

The product which is being manufactured in the market is produced to sell in the market. Consumers are the main root of the market. Generally the consumer market is divided into three parts:-

- 1) Consumers stay with Authorized Version as they place more value to warranty and services that comes from authorized dealer.

- 2) Consumer switches to parallel import as they place little value to warranty, taste and advantages provided with the product.
- 3) New segment that would not have purchased the product before.

*A. What Does Welfare Actually Mean for the Consumer?*

Welfare means “Are the consumers better off?” by the market activity. *Welfare in economics* means that the consumer is able to purchase the goods at the price which is less than what he is ready to pay for the product. Therefore, the welfare of the consumer increases if he accesses the goods at the cheaper price, which is one of the reasons of the origin of the grey market.

Different types of consumers define welfare differently. An empirical study was conducted on 200 people of the age group 20-30. This gives interesting results over the definition of the welfare and gives a base to the paper that welfare for individual does not always mean buying the product at lesser price rather sometimes to have that product at whatever be the price. Also, this helps us to reach the conclusion that the other form of market i.e. the grey market could also increase the welfare of the consumers.

The result of the survey is as follows:

- In case of high- end luxurious products which have not been launched in the country yet, 22% of the consumers were of the opinion that they would be willing to pay higher price only when the maximum margin is 20% .
- In case of products where the warranty does not matter at all (*viz.* pen drives, text books etc) more than 85% would be willing to buy the product at lesser price.
- In case where the warranty is provided in the regular market, consumers are more concerned about the price of the same product being offered in various different markets at the same time.
- If the same product is available in the regular market with warranty and also in grey market but with no warranty and at comparatively lower price with marginal difference, then, more than 80% were of the opinion that they would be willing to buy the product with warranty.
- On the other hand, if the product is available in the regular market with warranty and in the grey market at comparatively lower price with no warranty, but the difference in price is quite high, then ,60-70% consumers desired to purchase the product from the grey market.
- If the product is available in both the markets with warranty then consumers will be more concerned about the terms of warranty and the price difference. 40% would have preference for the terms of warranty whereas 60% would go for the cheaper product available.
- In case of apparels generally no warranty is provided by the seller, in this case around 40% were of the opinion they would prefer the brand name and purchase from the authorized dealer whereas the rest were willing to purchase the same from the unauthorized dealer, if available at lower price.

Thus, various interesting facts were drawn from the survey such as different consumers have different meaning of welfare in their

minds. For some, price was not the matter of concern at all instead the only concern was the availability of the product. This

generally happened in the case of the product which satisfied the status recognition need of the consumer. For example, when I

Phone-5 was not launched in India, grey market raises its price to 1 lakh rupees as there were some set of consumers who were

willing to pay any price to get the I phone-5. There were also some set of consumers who desired to get the product at lower price.

This mainly happens in case of textbooks, pen drives and there is some set of consumers who value the branded goods and thus, are

willing to pay higher price for such goods. There is also some set of consumers for whom there is a trade off between price

difference and the terms of warranty in the normal market and the grey market.

*B. Whether the Grey Market is the Boon or Bane to the Consumers?*

Grey market is a boon to consumers as it made available products to those consumers who are only concerned about its availability. They are not concerned about the price that they are paying. In the survey, we have seen that in case of products like textbooks, grey market made available such products at lower price and thus increases the consumers

welfare as warranty also does not matter at all in this case. Moreover, grey market gives wide choice to the consumer. For example: Cadbury is producing Dairy milk chocolate of different taste in India and China. If the chocolate, produced in China is imported in India and creates its own customer base, then the customer will enjoy wide variety of chocolate produced by the same company.

The existence of grey market helps in combating the monopoly power of manufacturer and dealers, who in the absence of grey market can charge any price from the customer. This happens because the grey market gives consumer scope to have the trade off between price difference and the terms of warranty as there is always some set of consumers who value lower price more than the warranty available.

#### *C. Role of Government in Grey Market*

Government has not taken stringent action against the development of grey market. It need to regulate the grey market where it creates unhealthy competition and unnecessarily raises the price of the products, which are essential for the survival, for example, Grey marketer takes the advantages of lax state laws regarding the distribution of prescription drugs. Pharmaceutical companies sell almost all of their products to a few large distributors, which control the major sales to hospitals and pharmacies. However, there are hundreds of small distributors that purchase drugs from one another like any other traded commodity, with the hope of buying low and selling high. When shortages occur, they offer the drugs for sale to hospital pharmacists at prices that can be 100 times or more than retail.

#### *D. Conclusion*

Grey market increases the welfare of the consumer as it made available the genuine products to the consumers and give wide choice to the consumer. Grey market caters the need of different kind of consumers and also helps the consumer to save the part of their money which is going to be spent on unnecessary warranty given by the authorized dealers but we need to regulate the grey market in case of the essential products where it raises its prices and results in unhealthy competition in the market.

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