

# Consumer generosity, tipping policy and service quality signaling

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## **Abstract**

Consumers' tipping behavior is generally guided by social norms and their tip amounts are usually related to service quality. Very often some consumers are uninformed about the service quality before consumption. In this paper, we study how consumer generosity affects firms' optimal policy and retail price, and how firms can signal their service quality to uninformed consumers. We denote a firm with high (low) service quality as H-type (L-type). We find that under complete information, it is optimal for the H-type to implement a tipping policy only if consumer generosity is relatively low. We also find that under incomplete information, a tipping policy and the complete information optimal price together can send signals for the H-type under a large parameter region. Moreover, we show that the H-type may even strategically choose to implement a tipping policy to signal its service quality, although it is better off with a non-tipping policy under complete information.

**Keywords:** *signaling strategy; service quality; game theory*

**Track:** Marketing Strategy & Theory