

# Experimental economics, summary paper



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Summary of the Article The Article How Auctions Work for Wine and Art written by Orley Ashenfelter discusses the particular behavior of English auctions in regards to the movement of wines and arts. The behavior of price in these auction settings at times fail to follow the basic laws of prices. The article describes empirical regularities that have been observed in auction markets of these two items. In the English auction system there is a mechanism known as a reserve price. The reserve price is the minimum price the bidders have to reach for the sale to occur. The people bidding do not know the reserve price. Another rule is that the seller cannot bid on himself to avoid prices going up artificially. This practice is unethical and illegal. “ No auction house that values its reputation – and the long run profits its reputation secures – would systematically engage in this practice” (Ashenfelter). The fact that reserve prices are kept secret is considered by many an illogical tactic. This occurs because the most dominant strategy used is to bid up in regards to the true valuation of the object which makes the optimal reserve price identical irrelevant of the reserve price being known or kept a secret. Another variable that must be considered in the English auction system is buy-in rates. Sometimes buy-in rates are high despite the fact that the reserve price is also high. These types of sellers are looking to maximize their profit both in terms of final price and buy-in revenues. Auctions that are able to get a lot of bidders to buy-in generate greater profits than places with few bidders participating in the game. Low turnout of bidders is an undesirable marketplace. When this occurs many sellers prefer to take their items off the market temporarily to protect themselves against collusion from the buyers in an attempt to depress the price. The highest bidding in an auction is only accepted if the bid ends up

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exceeding the reserve price. Main Findings of Article One of the main findings of the article is that revealing information tends to remove uncertainty and makes low bidders more aggressive. This action puts upward pressure on the bidding of others; a behavior which is in the best interest of the seller. Description of Result Interesting to Me A finding that I found interesting is the fact that secrecy about reserve prices do not matter that much to the buyer. The buyers are more interested in the fact that they have to outbid the rest of the players. The reserve price in theory is supposed to protect the seller from getting offers that are too low for the item being auctioned. If something is worth \$50, 000, getting an offer for '\$10, 000 is an offer that would lead to a loss in the sale of the item. As far as the impact of the reserve price, the bidder is not going to stop a bidding war if the person wants an item because of the existence of a low reserve price. Discussion Question What would happen if you ran two auctions: one with known reserve prices and one with hidden reserves prices? Which of the two auctions do you think will result in higher final prices? Work Cited Page Ashernfelter, O. " How Auction Works for Fine Arts." The Journal of Economic Perspective Summer 1989: 23-36.