

## **Leveling the Auction Playing Field** **by Eliane Dotson, Old World Auctions**

The earliest report of an auction was around 500 B.C., when annual auctions of women for marriage were held in Babylon, according to Herodotus. Auctions have come a long way since then, with everything imaginable available for auction, and internet auctions gaining in popularity. Researchers have found that auctions are the best format for selling an item when the value of the item is uncertain. This makes auctions particularly suitable for antiques, which are often rare and difficult to value. Due to the competitive nature of the auction market, both sellers and buyers must identify optimal strategies for maximizing their success.

### **Strategies for sellers**

One of the most important strategies for all sellers is to provide as much information as possible on the item up for sale. This decreases the risk for buyers to participate in the sale and results in a higher realized value. Since each potential buyer must assess the value of the item on his or her own, giving full and complete information on an auction item encourages more buyers to participate in the bidding activity.

Another factor for sellers to consider is whether to start with a high or low starting price. Traditionally, high starting prices create a higher perceived value due to the psychological principle known as "anchoring." This principle is common in decision-making where an initial piece of information is used to make subsequent judgments. However, some researchers have found that using a strategy of a low starting price can actually lead to a higher realized price.

A research study by Adam Galinsky and J. Keith Murnighan, both from the Kellogg School of Management, and Gilliam Ku, from the London Business School, found evidence of a reverse anchoring effect with auctions with low starting prices. With auctions of both common goods and one-of-a-kind items, low opening bids encouraged more bidders to participate. In addition, lower prices caused bidders to invest more time and money into the auction, increasing their overall commitment. This total boost in traffic produced two results: bidders perceived a higher value of the item based on the number of bids it received; and of course the more bids the item received, the higher the price went.

Therefore with items for which there is interest from numerous buyers, a low starting price may be the best strategy. And for very specialized items that would have a smaller customer base, adopting a high starting price will likely lead to a better result.

### **Strategies for buyers**

Once the seller has selected a strategy, it is up to the buyer to optimize his or her own strategy. There are several key factors that play a role in the buyer's auction

strategy. First a buyer must determine his or her risk tolerance. This is determined by how critical it is that the buyer win the item, as well as how important it is that the buyer avoid the "winner's curse," which occurs when the buyer pays more than the true value of the item. Of course determining the value of the item is another key factor. A buyer must do his or her homework, because information advantages often lead to the best returns in an auction environment. The third factor that must be considered is whether the buyer intends to keep the item or resell it at a later date. A buyer turned seller must anticipate the additional costs of selling while still maintaining a level of profit.

Once the buyer has ascertained his or her risk tolerance, the value of the item, and possible resale opportunities, he or she can identify a suitable bidding strategy. There are two common bidding strategies that can discourage competition. The first is known as "squatting," in which a bidder bids early and often, continually responding to competition by placing higher bids. The keys to this strategy are to respond to competitive bids quickly and to bid aggressively, as simply bidding the minimum invites competition. Another strategy is called "jump bidding," in which a bidder suddenly places a bid much higher than the current bidding activity requires. In a live auction setting, this aggressive strategy enables a bidder to communicate his or her strong interest in an item to competitors. As a result, the competitors may assume that the bidder values the item more than they do, and drop out of the bidding. This strategy can also be used in a timed, online auction by placing a high maximum bid. Competitors who try to place bids will find themselves immediately outbid over and over again, which may discourage them from placing further bids.

Although sniping is another bidding strategy, it won't be discussed here as it is not an option through our auction format. With Old World Auctions, bids placed at the last minute (or the last second!) simply extend the length of the auction so that other bidders have the chance to place a competitive bid.

Regardless of your bidding strategy, there are two fundamentals that lead to more successful bids. When possible, look for low trafficked items, as lower traffic leads to lower prices. And second, spend time researching what an item is worth, and then bid the value you are willing to pay. (See our October newsletter article on "Establishing Auction Estimates" for how we value maps.) If you win the item, you'll know that you haven't overpaid, and if you lose, you won't suffer the winner's curse by paying more than the item is worth to you.