Auction Criteria

The following must be considered and taken into account when constructing an auction.

Strict Integrity of the Process

To optimize the auction design, it is imperative that the seller maintains strict integrity of the process. The seller cannot afford any illicit activity to be hidden in the sheer volume of the transaction. Buyers only participate when an open and fair market is guaranteed. If buyers start to doubt the transparency of your auction system, their interest falls, and so does your demand. The lower the demand (represented by the number of buyers in an auction system) the lower your return.

Equal Access

Limit the maximum procurement share of any one individual or company to increase participation of small companies.

Optimal Market Information

Common-Value price setting is susceptible to market information. Common-Value price setting is when buyers attending an auction use the same objective criteria to determine their perceived value of the commodity for sale. Bidders at a wheat auction will use the price of wheat or flour in future trading as their objective criteria. Common-Value price setting differs greatly from private-value price setting. In the private-value case, bidders' valuation of the commodity for sale is subjective and independent of one another. A unique work of art not for resale at auction at Soothby is a common example. In this case the buyer puts a value on his own satisfaction of ownership and bids accordingly. In this Private-Value case the seller is isolated form market information and market consensus. In the Common-Value case price setting is extremely susceptible to market information and consensus.

> Common-Value Case
> A strategic bidder understands that a high bid lowers his profit and raises his probability of winning. He lowers his bid to an acceptable level and accepts a lower probability of winning in order to maximize his profit potential. In addition, he will shade his bid toward the perceived market consensus. If the market is tight, and values are escalating, he will shade his bid higher. If the market is flooded with product, he will shade his bid lower. Popular opinion (consensus) and market information will affect his shading.

Reduce Winners Curse

To increase the seller's profit, select an auction system that reduced winners curse and encourages aggressive bidding. Winners curse causes aggressive bidders to reign in their enthusiasm at the auction, reducing the seller's profit. It is ironic, but a bidder wining an award is actually unlucky in a sense. He guessed about the price and future value of the commodity.. A high winning bid guarantees that he has locked in the lowest profit margin among the bidders. His valuation of the commodity exceeded all other interested parties, and now, after securing the award, he realizes that he might have overestimated his bid. Buyers' remorse is a similar concept.

Pooling of Bids

Bidders want to avoid winners curse bidding above market consensus. The easiest way to do this is for several bidders to pool their investment, and their market information. A group of investors would have more market information and therefore have a clearer view of the market. As a whole, they are less likely to be at the farend of a bid price. This is a technique for many bidders to offset Winners Curse. In a worst case scenario, pooling of bids can lead to collusion in several auction types.

Collusion

There has been much research conducted regarding collusion in financial auctions. The benefit of collusion in such a market can result in the gain of millions of dollars if successful. The research, if generalized, provides us with some good insight.

Collusion usually occurs among a small number of individual or firms. A large group disintegrates easily. The group must share the same market information and strategy, in the primary and secondary market (the wheat and flour, perhaps the animal feed industry). The larger the group the lower the probability of their agreement.

Sealed bid auctions help splinter collusion groups. The sealed bid is private, and usually very tempting to one party. The sealed envelop allows him to put in a bid just slightly higher than the group agreed upon, allowing him to collect a greater portion of the spoils by himself, at the group's detriment. The member of his group will not know of his departure until after the award is announced, when there is no opportunity to react

Open-cry auctions. The verbal outcry is very public, and should a member decide to go out on his own, his fellow members will hear it immediately. The immediacy of the auction will allow them to react. The indigenous culture often determines members actions:

1. Members are not willing to risk being caught breaking the pact, and they act as scripted, supporting the collusion strategy.
2. Members realize that the collusion has splintered and immediately enter into auction bidding.

To prevent collusion:

- Announcement of the auction date and execution of the auction should be in a tight time frame. The closer the two dates, the less time a group has to collude. The time should leave bidders with enough time to secure a bank reference, but not enough time to form a splinter group.

- The seller retains the right not to sell the grain at hand. Should collusion undermine an auction, or should the general industry liquidity not raise funds sufficient, the seller retains the right to retain the grain, at their own cost, until a later date when the market provides better value, or collusion forces have splintered.

- Collusion groups are likely to leverage the working capital, and lobby gatekeepers for financing options. Fraternization is eliminated with an independent, non-invested Executing Agency. Financial schemes are avoided by requiring bidders to attain a bank's letter of credit for participation qualification. Within three days of securing an award, payment in full is to be deposited in the Executing Agencies bank account. Funds will be held until the grain arrives and quality is confirmed. At that time funds are transferred to the recipient agencies as outlined in the bilateral agreement.

Auction Structure

Auctions are classified based on the order in which prices are quoted and based on the way in which bids are entered.

Prices Quoted	Bids Entered
• Prices are progressively lowered until the entire lot is sold • Prices are progressively increased until a single price takes the entire lot.	• Privately. Sealed bids opened by an auctioneer or bank representative • Publicly. Real time auctioning with all participants in a single room (or connected electronically) in a public setting.

This creates four auction alternatives, First-Price Sealed Bid Auction, Second-Price Sealed Bid, Descending Price Open-Outcry, Ascending-Price Open-Outcry Auction Benefits Details for each are found in the resource section.

Ascending-Price Open-Outcry Auction Benefits

Auctions are flexible, and can be adjusted in many creative ways to achieve desired outcomes. In general, for the monetization programs, the optimal auction type would have ascending prices, to encourage buyer conditioning towards the greatest market value, and be held publicly, with all participants sharing market consensus.
Two auction systems can provide this for ANSA's monetization: Ascending-Price Open-Outcry Auction and Ascending-Price Closed-Bid Auction.

ANSA has Ascending-Price Closed-Bid Auction experience. Benefits of the Ascending-Price Open-Outcry Auction are:

Ascending-Price Open-Outcry Benefits

- It is relatively easy for new bidders to understand
- Open-Outcry maximizes auction transparency
- Maximizes the sellers' market value
- Decreases Winners Curse
- Encourages aggressive bidding
- Market Consensus is discovered
- Bidders are conditioned towards the "greatest" market value, not the lowest
- Overbidding in isolation, shading of bids and pooling are discouraged
- Collusion is most difficult.

Ascending-Price Open-Outcry Auction Description – 2 Alternatives

- All bidders are present in one room at the same time. The auctioneer calls out an ascending price of the lot. The lot represents the entire volume for sale. Bidders submit the quantity demanded. The volume is announced and the price is raised until the volume demanded is smaller that the lot size available. The auctioneer returns to the previous price that cleared the lot. All bidders at the highest price are guaranteed their bid volume. A formula dividing the remainder of the lot to the second tier bidders is established to equitably distribute the remaining grain. All grain is sold at the price that cleared the entire lot. This is the preferred auction system to create a fair, public price for all parties, while still reflecting market demand.

- All bidders are present in one room at the same time. The auctioneer calls out an ascending price of one predetermined lot. Bidders verbally accept the price by raising a hand or auction ID card. The price is raised until no bidder accepts the price. The highest bidder receives the award. Process is repeated until all grain is sold. This is preferred in the presence of an inexperienced auctioneer or hesitant first-time bidders.