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WIRTSCHAFTSTHEORETISCHES FORSCHUNGSSEMINAR

RESEARCH SEMINAR IN ECONOMIC THEORY

October 22, 2009

Institute for Advanced Studies
Stumpergasse 56, 1060 Wien
lecture room II, groundfloor (HSII)

4:00pm

Pieter Gautier,
University of Amsterdam:

“Directed search in the housing market”

Abstract printed on the next page

5:30pm

Sandro Shelegia,
University of Vienna:

“Multiproduct Pricing in Oligopoly”

Abstract printed on the next page

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<http://www.univie.ac.at/vwl/EconomicTheory.html>

NOTE: Participation of advanced students in this seminar is highly recommended.



Pieter Gautier,
University of Amsterdam:

“Directed search in the housing market”

In this paper, we present a model of the housing market. We construct our model with the following stylized facts in mind. First, sellers post asking prices, and buyers observe these announcements. Second, there is not a straightforward relationship between the asking price and the final sales price. Sometimes houses sell below the asking price, sometimes at the asking price, and sometimes above the asking price. Buyers sometimes make counteroffers below the asking price, but sometimes -- typically when the market is hot -- houses are sold by auction above the asking price. Our objective is to construct a tractable model that captures these features of the housing market.

Our model is one of directed search in the sense that sellers use the asking price to attract buyers. However, ours is not a standard directed search model in that we assume only limited commitment to the asking price. The specific form of commitment that we assume reflects the institutions of the U.S. housing market. Within a "selling period," buyers who view a house that is listed at a particular price can make offers on that house. A seller is, of course, free to reject any offer below her asking price, but she also has the option to accept such an offer. However, if the seller receives one or more bona fide offers to buy the house at her asking price (without contingencies), then she is committed to sell. If the seller receives only one such offer at the asking price, then she is committed to transfer the house to the buyer at that price. If the seller receives two or more legitimate offers at her asking price, then she cannot, of course, sell the house to more than one buyer. In this case, the remaining buyers can bid against each other to buy the house. In practice, this auction often takes the form of bids with escalator clauses.

Our description of the U.S. housing market is obviously stylized in the sense that there is sometimes ambiguity about what constitutes a bona fide offer at the asking price. For example, a seller can often reject a prospective buyer's offer at the asking price if the buyer's ability to secure a mortgage is in question. It is also important to emphasize that the institutional form of limited commitment to the asking price that we are ascribing to the U.S. housing market is not universal. For example, in the Netherlands, the asking price entails no legal commitment whatsoever. Nonetheless, since real estate agents have reputational concerns, asking prices do reflect some limited commitment there as well.

Given limited commitment, what determines the asking prices that sellers post and what role do they play? We begin with a basic version of our model in which all sellers have the same reservation price. After observing all the asking prices in the market, each buyer chooses a seller to visit. Upon visiting the seller, the buyer decides how much he likes her house; that is, he observes the realization of a match-specific random variable. This realization is the buyer's private information. Based on this realization -- and without knowing how many other buyers have visited this seller -- the buyer chooses among accepting the seller's asking price, making a counteroffer (and, if so, at what level), or simply walking away. The seller then assembles her offers, if any. If no buyer has offered to pay the asking price, the seller decides whether or not to accept her best counteroffer. If she has received one, and only one, offer at the asking price, then she sells the house at that price. If she has received multiple offers at the asking price, she then allows the buyers who made those offers to compete for the house via an ascending bid oral auction.

Then, we allow for heterogeneous sellers in terms of reservation prices (which is private information). In that case, the asking price can play a potential signaling role. Finally, we investigate the efficiency properties of the model.

with Jim Albrecht and Susan Vroman, both Georgetown University, Washington D.C.

Sandro Shelegia,
University of Vienna:

“Multiproduct Pricing in Oligopoly”

This paper proposes a two-good model of price competition where some consumers visit all the shops and others visit only one. We find that, in the Nash Equilibrium, the information frictions lead to price dispersion. When the goods are complements their prices will be negatively correlated so if one of them is priced high then the other one is at a discount. This finding is supported by the empirical observation that simultaneous price discounts of complements are infrequent. If the goods are substitutes then their prices will be uncorrelated, rationalizing the lack of evidence on their co-pricing. When selling complements, retailers earn higher profits than in the one-good model by discriminating consumers through taxing captives with high overall price tag and attracting shoppers by pricing one of the goods aggressively. This strategy does not yield additional profits for substitutes because captives will switch to buying only the aggressively-priced good.

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