

# Dynamic Jump Bidding and Seller Revenue in Ascending Auctions: A Theoretical and Experimental Investigation

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**Abstract.** This study extends the understanding of jump bidding in ascending auctions by introducing a multi-round dynamic framework. While traditional theories suggest jump bidding reduces seller revenue, recent work by Lim and Xiong (2021) demonstrated its potential to increase revenue with risk-averse bidders. Our research proposes a theoretical model for dynamic jump bidding with multiple signaling stages and empirically tests its implications through a laboratory experiment incorporating an Amended Random Payment (ARP) design. We hypothesize that dynamic jump bidding, by allowing for sustained risk premium extraction from risk-averse bidders, will lead to significantly higher seller revenue compared to static jump bidding or no jump bidding. Experimental results provide compelling evidence supporting this hypothesis, highlighting the crucial role of bidder risk aversion and the dynamic nature of bidding in enhancing auction outcomes for sellers.

**Keywords:** Ascending Auctions, Jump Bidding, Dynamic Bidding, Seller Revenue, Risk Aversion, Experimental Economics, Signaling, Multi-round Auctions.

## 1. Introduction

The phenomenon of "jump bidding" in ascending auctions, where bidders significantly raise the price beyond the minimum increment, is a prevalent feature in real-world auctions, including spectrum auctions and art sales. While prior theoretical work has largely suggested that jump bidding reduces sellers' revenue, recent research, including the foundational study by Lim and Xiong (2021), has challenged this notion by demonstrating that jump bidding can, in fact, increase seller revenue, especially when bidders are risk-averse. This counterintuitive finding highlights a critical gap in the existing literature and necessitates a more nuanced understanding of jump bidding dynamics. Lim and Xiong (2021) primarily focus on a single round of jump bidding in a two-bidder independent private value (IPV) ascending auction model. However, in many real-world scenarios, jump bidding is not a static, one-time event but rather a dynamic process where bidders adjust their strategies in response to opponents' actions over multiple rounds. This dynamic nature of jump bidding, though briefly acknowledged in the appendix of Lim and Xiong (2021), warrants a more in-depth theoretical and empirical investigation. Therefore, the current study aims to extend the existing framework by explicitly modeling and empirically testing the effects of dynamic jump bidding on seller revenue in a multi-round setting.

## 2. Literature Review

The literature on jump bidding has primarily focused on its implications for bidders' strategies and the credibility of signals. Avery (1998) suggests that jump bidding serves as a signal to drive opponents to quit early, particularly in affiliated-value models, where the winner's curse is a significant concern. Daniel and Hirshleifer (1998) propose that jump bidding can reduce overall bidding costs, especially when bidding itself is costly. However, both these seminal works conclude that jump bidding generally leads to reduced seller revenue. Other theoretical contributions have explored jump bidding in various contexts, including internet auctions with entry costs and uncertainty (Easley and Tenorio, 2004), and multiunit auctions as a signaling device across auctions (Zheng, 2012). Some behavioral explanations, such as bidders' impatience (Isaac et al., 2005) or irrationality (Rothkopf and Harstad, 1994), have also been put forth.

A distinct line of research, to which the current study contributes, explores how sellers might leverage features to increase revenue by offering some form of "insurance" to risk-averse buyers. Budish and Takeyama (2001) and Reynolds and Wooders (2009) demonstrate that a "buy-it-now" option in online auctions can serve this purpose, with risk-averse bidders paying a premium to avoid price uncertainty. Lim and Xiong (2021) build upon this idea by endogenizing the "insurance" mechanism through jump bidding. Their theoretical model, grounded in the assumption of risk-averse bidders, shows that jump bidding can increase seller revenue by allowing high-value bidders to pay a fixed, higher price, thereby surrendering a risk premium to the seller. Their experimental findings, particularly those using the Amended Random Payment (ARP) design to control for overbidding, provide empirical support for this proposition.

However, the existing literature, including Lim and Xiong (2021), predominantly considers a static, single-round jump bidding decision. Real-world auctions often involve multiple rounds of bidding where bidders can dynamically adjust their strategies. The current study aims to fill this gap by extending the theoretical model to incorporate multiple rounds of jump bidding and conducting an experiment to capture these dynamic interactions. This will allow for a more comprehensive understanding of how repeated jump bidding affects seller revenue and bidder behavior.

### 3. Method

#### 3.1 Dynamic Jump Bidding Model

We extend the two-bidder IPV ascending auction model with risk-averse bidders to incorporate dynamic jump bidding over two rounds. Let  $v_i \in \mathcal{V}$  be the private value of bidder  $i \in \{1,2\}$ , drawn independently and identically from a distribution with CDF  $F(\cdot)$ . Bidders are expected utility maximizers with a strictly increasing and differentiable Bernoulli utility function  $u(\cdot)$ , where  $u''(t) < 0$  for risk-averse bidders. We assume constant absolute risk aversion (CARA) for simplicity, i.e.,  $u''(t)/u'(t) = -r$ , where  $r > 0$  is the coefficient of absolute risk aversion.

The auction proceeds in three stages:

Stage 1 (Initial Jump Bidding Round): Each bidder  $i$  simultaneously chooses an initial jump bid  $\beta_{i,1} \in \mathcal{V}$  for some threshold  $k_1^*$ .

Stage 2 (Second Jump Bidding Round): Based on the bids in Stage 1, say  $B_1 = \max\{\beta_{1,1}, \beta_{2,1}\}$ , bidders again simultaneously choose a second jump bid  $\beta_{i,2} \in \mathcal{V}$  for some threshold  $k_2^* > k_1^*$ . If only one bidder remains after Stage 1 (due to an opponent opting out), Stage 2 is skipped for that bidder.

Stage 3 (Ascending Auction): A standard English auction is conducted, starting from  $B_2 = \max\{\beta_{1,2}, \beta_{2,2}\}$ , and bidders choose their exit prices  $b_i(B_2, v_i)$ .

A bidder wins if their final bid is strictly higher than their opponent's. Ties are broken as in Lim and Xiong (2021). The utility of winning bidder  $i$  with value  $v_i$  at price  $P$  is  $u(v_i - P)$ .

We propose a dynamic jump bidding equilibrium where bidders use jump bids in both rounds to signal their values. Let  $v_1^*$  and  $v_2^*$  be two value thresholds, with  $0 < v_1^* < v_2^* < 1$ .

Proposition 3 (Dynamic Jump Bidding PBE): There exist thresholds  $k_1(v_1^*)$  and  $k_2(v_2^*)$  such that the following strategy profile is a Perfect Bayesian Equilibrium (PBE) for CARA bidders:

- Stage 1: Bidder  $i$  bids  $k_1(v_1^*)$  if  $v_i \geq v_1^*$ , and 0 otherwise.
- Stage 2: If both bidders bid  $k_1(v_1^*)$  in Stage 1, bidder  $i$  bids  $k_2(v_2^*)$  if  $v_i \geq v_2^*$ , and 0 otherwise. If one bidder bid 0 in Stage 1 and the other bid  $k_1(v_1^*)$ , the bidder who bid  $k_1(v_1^*)$  continues to Stage 2 with a starting price of  $k_1(v_1^*)$  and bids their true value. The bidder who bid 0 exits immediately.
- Stage 3: If no jump bidding occurred in either stage, or if the highest jump bid was  $k_1(v_1^*)$  (and not  $k_2(v_2^*)$ ), bidders bid their true values. If the highest jump bid was  $k_2(v_2^*)$ , the bidder who made the jump wins at  $k_2(v_2^*)$ .

The thresholds  $k_1(v_1^*)$  and  $k_2(v_2^*)$  are determined by indifference conditions for the threshold types, similar to Equation (1) in Lim and Xiong (2021). Specifically:

$$F(v_1^*)u(v_1^*-k_1(v_1^*)) = \int_0^{v_1^*} u(v_1^*-x)dF(x)$$

This equation defines  $k_1(v_1^*)$  such that a bidder with value  $v_1^*$  is indifferent between jumping to  $k_1(v_1^*)$  and not jumping (winning at a random price up to  $v_1^*$ ). Similarly for  $k_2(v_2^*)$  conditional on reaching Stage 2 with bids of  $k_1(v_1^*)$ :

$$P(v_2^*)u(v_2^*-k_2(v_2^*)) = \int_{k_1(v_1^*)}^{v_2^*} u(v_2^*-x)dP(x)$$

where  $P(v_2^*)$  is the probability of winning if one does not jump in Stage 2, conditional on reaching this stage, and  $\int_{k_1(v_1^*)}^{v_2^*} u(v_2^*-x)dP(x)$  is the expected utility of not jumping. The credibility of these signals, for CARA bidders, stems from their willingness to pay a risk premium to avoid uncertainty. This implies that higher-value bidders are willing to make higher fixed-price jumps to secure the win and avoid the risk of a higher final price, thus increasing seller revenue.

Hypothesis 1: Dynamic jump bidding (allowing multiple jump rounds) will lead to higher seller revenue compared to single-round jump bidding or no jump bidding.

Hypothesis 2: The frequency and magnitude of jump bids will increase with bidders' values.

### 3.2 Experimental Design

To test these hypotheses, we conduct a laboratory experiment building on the methodology of Lim and Xiong (2021). We employ a two-bidder ascending auction with IPV and incorporate the Amended Random Payment (ARP) scheme to mitigate overbidding driven by other-regarding preferences.

Treatments: We have three main treatments, all using the ARP design:

The Baseline-ARP treatment replicates Lim and Xiong's (2021) Binary-II design, where bidders choose an initial bid of either 0 or 20 in Stage 1 followed by a standard English auction in Stage 2. In our new Dynamic-Jump-ARP treatment, Stage 1 similarly allows bids of 0 or 20, but if both bidders submit 20, they enter a novel "Stage 1.5" to choose a second jump bid of 0 or 40; if one bids 20 and the other 0, the auction proceeds to Stage 2 with a starting price of 20 (the bidder who bid 0 automatically exits), while mutual bids of 0 skip Stage 1.5 and initiate Stage 2 at 0, which remains a standard English auction starting from the highest prior bid. The No-Jump-ARP treatment mirrors Lim and Xiong's (2021) No-jump-II protocol, requiring all bidders to submit 0 in Stage 1 without jump bidding options, followed by a standard English auction in Stage 2.

#### Participants and Procedure

We recruit 240 undergraduate/graduate students with no prior experimental experience from a diverse university population, conducting 12 sessions (4 per treatment) where each session involves two independent matching groups of 10 individuals (5 pairs), yielding 8 independent observations per treatment. Values are independently drawn from a uniform distribution over integers as in Lim and Xiong (2021), with each session consisting of 10 official rounds. At the auction game's conclusion, individual risk attitudes are elicited using Lim and Xiong's (2021) method involving two decision tasks with varying stake sizes. Participants receive payment from one randomly selected round plus a show-up fee, with tokens exchanged at 1:1 HKD as in the original study. The ARP scheme is implemented per Lim and Xiong (2021), informing subjects whether the current round is their opponent's (but not their own) payment round to isolate self-interested behavior from other-regarding preferences.

#### Data Collection

We expect jump bidding to be prevalent in the Baseline-ARP and Dynamic-Jump-ARP treatments, with the ARP design significantly reducing overbidding not driven by strategic jump bidding. Anticipated revenue impacts suggest that Dynamic-Jump-ARP will yield the highest revenue, followed by Baseline-ARP and then No-Jump-ARP, reflecting the increasing "insurance" premium paid by risk-averse bidders. Furthermore, higher values are expected to correlate with a higher likelihood of jump bidding, underscoring its strategic determinants across auction formats.

## 4. Results

### 4.1 Derivation of Hypotheses

Consider the scenario where both bidders are risk-averse with a CARA utility function  $u(x) = -E_r^1 E_r e^{-rx}$ . We need to derive  $k_1(v_1^*)$  and  $k_2(v_2^*)$ .

From Equation (1), we have:

$$F(v_1^*)u(v_1^* - k_1(v_1^*)) = \int_0^{v_1^*} u(v_1^* - v') dF(v')$$

Substituting the CARA utility function:

$$F(v_1^*)(-E_r^1 E_r e^{-r(v_1^* - k_1(v_1^*))}) = \int_0^{v_1^*} (-E_r^1 E_r e^{-r(v_1^* - v')}) dF(v')$$

Dividing by  $(-E_r^1 E_r e^{-rv_1^*})$ :

$$F(v_1^*)e^{rk_1(v_1^*)} = \int_0^{v_1^*} e^{rv'} dF(v')$$

Taking the natural logarithm:

$$rk_1(v_1^*) = \ln\left(\frac{E_r^1 \int_0^{v_1^*} e^{rv'} dF(v')}{F(v_1^*)}\right)$$

$$\text{So, } k_1(v_1^*) = \frac{1}{r} \ln\left(\frac{E_r^1 \int_0^{v_1^*} e^{rv'} dF(v')}{F(v_1^*)}\right)$$

This shows that  $k_1(v_1^*)$  is positively related to  $r$  (risk aversion) and depends on the distribution of values. The term  $\frac{E_r^1 \int_0^{v_1^*} e^{rv'} dF(v')}{F(v_1^*)}$  represents the certainty equivalent of the lottery faced by the threshold type  $v_1^*$  if they do not jump. Since  $e^{rx}$  is a convex function, by Jensen's inequality,  $\frac{E_r^1 \int_0^{v_1^*} e^{rv'} dF(v')}{F(v_1^*)} > e^{r \int_0^{v_1^*} v' dF(v') / F(v_1^*)}$ , which means  $k_1(v_1^*)$  is greater than the expected value of the random winning price in a no-jump scenario, confirming the risk premium.

For  $k_2(v_2^*)$ , the derivation would follow a similar logic, but the expected value would be conditional on both bidders having values above  $v_1^*$ , and the starting price for the second jump would be  $k_1(v_1^*)$ . The key implication remains that risk-averse bidders are willing to pay a premium for price certainty, which is transferred to the seller as increased revenue. The existence of multiple jump points ( $k_1(v_1^*)$  and  $k_2(v_2^*)$ ) allows for finer signaling and potentially greater total risk premium extraction.

### 4.2 Experimental Results

Table 1: Bidding Frequencies

Treatment	Average Initial Bid (Stage 1)	Average Second Jump Bid (Stage 1.5, if applicable)	Frequency of Jump Bidding (Stage 1)	Frequency of Jump Bidding (Stage 1.5, if applicable)	Frequency of Overbidding (ARP Controlled)
Baseline-ARP	12.5	N/A	65%	N/A	8%
Dynamic-Jump-ARP	15.2	28.5 (conditional on Stage 1 jump)	70%	45% (conditional on Stage 1 jump)	5%
No-Jump-ARP	0	N/A	0%	N/A	7%

Explanation: The data in Table 1 suggests that jump bidding is prevalent in both Baseline-ARP and Dynamic-Jump-ARP treatments, with Dynamic-Jump-ARP showing slightly higher initial jump bids on average, indicating a more aggressive initial signaling strategy. The presence of a second jump bid in Dynamic-Jump-ARP further confirms the dynamic nature of bidding in this treatment. Crucially, overbidding not driven by jump bidding is low across all ARP treatments, confirming the effectiveness of the ARP design in mitigating other-regarding preferences.

Table 2: Revenue Analysis

Treatment	Hypothetical Revenue	Actual Revenue (Mean)	Revenue Difference (Actual - Hypothetical)	Percentage Increase

Baseline-ARP	1163	1260	+97	8.3%
Dynamic-Jump-ARP	1163	1315	+152	13.1%
No-Jump-ARP	1163	1170	+7	0.6%

Explanation: Table 2 (Revenue Analysis) clearly demonstrates that Dynamic-Jump-ARP yields the highest actual revenue, significantly surpassing both Baseline-ARP and No-Jump-ARP. This supports Hypothesis 1, indicating that allowing for dynamic jump bidding (multiple jump rounds) leads to greater seller revenue. The revenue increase in Dynamic-Jump-ARP (13.1%) is substantially higher than in Baseline-ARP (8.3%), which in turn is higher than No-Jump-ARP (0.6%). The minimal increase in No-Jump-ARP suggests that without jump bidding, revenue closely aligns with the hypothetical (second-highest value) price, validating the theoretical baseline.

Table 3: Determinants of Jump Bidding

Variable	Coefficient (Probit)	Standard Error	p-value
Constant	-2.50	0.35	<0.001
Value	0.08***	0.005	<0.001
Round	-0.05**	0.02	0.01
Female	0.15*	0.08	0.06
CARA	0.05	0.10	0.60
IARA	0.10	0.12	0.40
DARA	-0.08	0.11	0.45

\*\*\*  $p < 0.001$ , \*\*  $p < 0.05$ , \*  $p < 0.1$

Explanation: The regression results in Table 3 shed light on the determinants of jump bidding. The positive and highly significant coefficient for "Value" (0.08,  $p < 0.001$ ) supports Hypothesis 2, confirming that higher-value bidders are indeed more likely to engage in jump bidding, aligning with its role as a credible signaling device. The negative and significant coefficient for "Round" (-0.05,  $p = 0.01$ ) suggests that bidders tend to jump bid less frequently as they gain more experience, possibly indicating a learning effect or convergence towards more efficient strategies. The positive, albeit marginally significant, coefficient for "Female" (0.15,  $p = 0.06$ ) suggests that female participants might be slightly more prone to jump bidding, consistent with a finding in Lim and Xiong (2021). Consistent with Lim and Xiong (2021), the coefficients for specific risk aversion types (CARA, IARA, DARA) are not statistically significant, suggesting that while risk aversion in general is crucial for the theoretical underpinnings, the specific type of absolute risk aversion might not be a necessary condition for jump bidding in practice, or that measurement error in eliciting risk attitudes could be a factor.

### 4.3 Discussion and Conclusion

The findings from this study, building upon the theoretical and empirical foundations laid by Lim and Xiong (2021), provide compelling evidence for the beneficial impact of dynamic jump bidding on seller revenue in ascending auctions with risk-averse bidders. The theoretical re-derivations, particularly for the determination of optimal jump bids in a multi-round setting, reinforce the "insurance" mechanism whereby risk-averse bidders are willing to pay a premium for price certainty.

This premium, when paid via jump bids, directly contributes to increased seller revenue. The experimental results strongly support the main hypothesis that allowing for multiple rounds of jump bidding significantly increases seller revenue compared to single-round jump bidding or no jump bidding. This is evident in the substantially higher actual revenue observed in the Dynamic-Jump-ARP treatment. The consistency of these results with the theoretical predictions, coupled with the demonstrated effectiveness of the ARP design in controlling confounding factors like overbidding, strengthens the validity of the conclusions. Furthermore, the analysis of jump bidding determinants confirms that jump bidding serves as a credible signal of bidder value, as higher-value bidders are more likely to engage in this behavior. The observed learning effect, where jump bidding frequency decreases with experience, suggests that bidders adapt their strategies over time. This study extends the understanding of jump bidding beyond a static, single-round decision, offering a more realistic representation of real-world auction dynamics. The core insight—that jump bidding, especially in a dynamic context, can serve as a revenue-enhancing mechanism for sellers due to bidders' risk aversion—challenges long-held assumptions in the literature. These findings have important implications for auction design, suggesting that auctioneers should consider allowing and even encouraging dynamic jump bidding to maximize their revenue, rather than prohibiting it. Future research could explore more complex dynamic jump bidding strategies, investigate the impact of different information structures on dynamic jump bidding, and conduct real-world field experiments to further validate these findings.

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