An Analysis of Residential Auction Sale Prices and Quoted Guide Prices

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The majority of the literature concerned with residential auctions has examined whether houses sell at lower or higher prices in comparison with a private treaty negotiated sale. A number of studies have shown, both theoretically and empirically, that auctioned properties should not sell at a premium in comparison to private treaty sales. Mayer (1994) argues that as private sellers can wait longer they would receive a higher price from a more matched buyer. Mayer refers to the auction discount as the cost of liquidity. This argument is also presented by Adams, Kruger & Wyatt (1992). The majority of empirical studies have examined whether properties sell for more or less at auction using a hedonic modeling approach. The results support the theoretical work that argues for auctioned properties selling at a discount. These results are however to some degree influenced by the fact that most auctioned properties in the US involve foreclosures or bankruptcies, especially at the lower end of the market. This is highlighted in studies such as Allen & Swisher (2000) and Allen (2001) that both use Department of Housing and Urban Development (HUD) auction data in their analysis. Both studies find evidence to support the hypothesis that auctioned properties sell at discounts.

Ashenfelter & Genesove (1992) provides one of the few US studies to have evidence of an auction premium. The authors examined the condominium market in New Jersey. While not employing a hedonic model to the data, the use of condominium units allows for comparison of sale prices between identical units. The paper found evidence that properties that were sold at auction sold on average for 13% more than those properties that were subsequently sold privately. However, these results do not necessarily imply that auctioned properties sell for more than those properties that were never placed before an auction. All of the private sales examined in their paper were initially offered at auction and then subsequently sold. These results could be due to the nature and condition of the properties as well as other variables that play a more important role in the lower end of the housing market, such as the availability of finance to purchasers. Therefore, these findings are in line with other studies in the US that

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suggest that prices decline as the auction process progresses.

In other parts of the world, auctions are often used at the higher end of the market and represent the preferred method of sale for estate agents in this price bracket. Newell, MacFarlane, Lusht & Bulloch (1993) examined the Sydney housing market finding that the median price of properties sold at auction was 3.6% higher than properties sold by private treaty. While the authors did not adjust for quality differences in the sample, Lusht (1996) examined the Melbourne market and also found that auction properties sold at a premium. His study attempts to control for quality thorough the addition of a number of variables into the hedonic equation. Dotzour, Moorhead & Winkler (1998) also find that auctioned properties can sell for a premium. This study examined 5,344 transactions in Christchurch, New Zealand using a hedonic approach. A significant premium for auctioned properties was observed in two of the four submarkets. The authors noted that these areas contained those with above average house prices, while the areas in which no discernable differences were observed are those with below average house prices.

This paper addresses a number of key issues, extending the existing literature to have examined auctions in a real estate context and builds upon preliminary work undertaken by the authors, Stevenson & Young (2004). This paper used a sample of 1,993 residential sales in Dublin, Ireland comprising of both private treaty and auctioned properties. The dataset analyzed contained not only the sale price but also the guide price for each property. As is the case with Australia, properties sold at auction in Ireland tend to be at the premium end of the market, thereby displaying a key difference with the US case. The auction mechanism generally used is an English auction, although sealed bids are sometimes employed. The analysis showed that over the period 1997-2001 auctioned properties sold on average for higher premiums than private treaty sales and that higher numbers of auctioned properties sold at high premiums. A significant difference in the premium over guide prices was observed for auctioned properties. In comparison, private treaty sale prices were insignificantly different from the quoted guide. The paper shows that 94.1% of auctioned properties sold in excess of the guide with an average degree of underpricing of 26%. Indeed, over 50% of the auctioned properties sold for more than 20% in excess of the guide. In comparison, the corresponding figure for private treaty sales was 10%.

The authors argue that the results are due to two primary issues. The first relates to the strong upward movement in the Dublin housing market during the period under examination. This is particularly so due to the evidence that a speculative bubble was present in the market during the late nineties. Due to the nature of auctions, these market conditions would encourage

speculative behavior at auctions. The second issue relates to the possibility that agents used different criteria in preparing the guide prices for auction, with some element of underpricing in order to help the marketing of the property. Therefore, while the speculative element is likely to have played an important role, the nature of the valuation process may build in a higher premium into properties sold at auction.

The current study extends this initial analysis using an expanded dataset of properties sold in Dublin during the period 2001-2004. The new dataset set includes expanded details of the properties allowing a more complete analysis of the properties concerned. The lack of detailed property specific data in the first study therefore prohibited the use of a hedonic framework. More importantly, the data includes details of the bidding process. Therefore in addition to the guide and sale price the analysis can model the actual bidding process. Details not only include the actual sequence of bids but through identification of the bidders it also allows us to incorporate the number of bidders into the analysis and individual bidder behavior. This should allow a thorough examination of how the nature of auctions impacts upon the bidding process and the final sale price. The period contained within the new sample has seen more stable price behavior in the Irish market in comparison to the previous work. This should also provide a clearer analysis of the role of the auction process. As already noted, the previous paper could not separate the impact of the sale mechanism from the speed of market movements. The data also includes information concerning any withdrawn properties and any subsequent sale. It also has details on the actual auctioneer and the date of the auction. It is intended that an analysis is undertaken to examine whether either of these two factors influences the premium of the sale price over the quoted guide.

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