

**AUCTIONS IN THE NETHERLANDS :
EXPERIENCES AND DEVELOPMENTS
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1. Introduction.

Auctions are a very important marketing institution in Dutch Horticulture. They are of some importance in other sectors of Dutch agriculture too. In this paper experiences with and developments in Dutch horticultural auctions will be analysed. Our analysis is placed in the framework of a discussion of auctions in general.

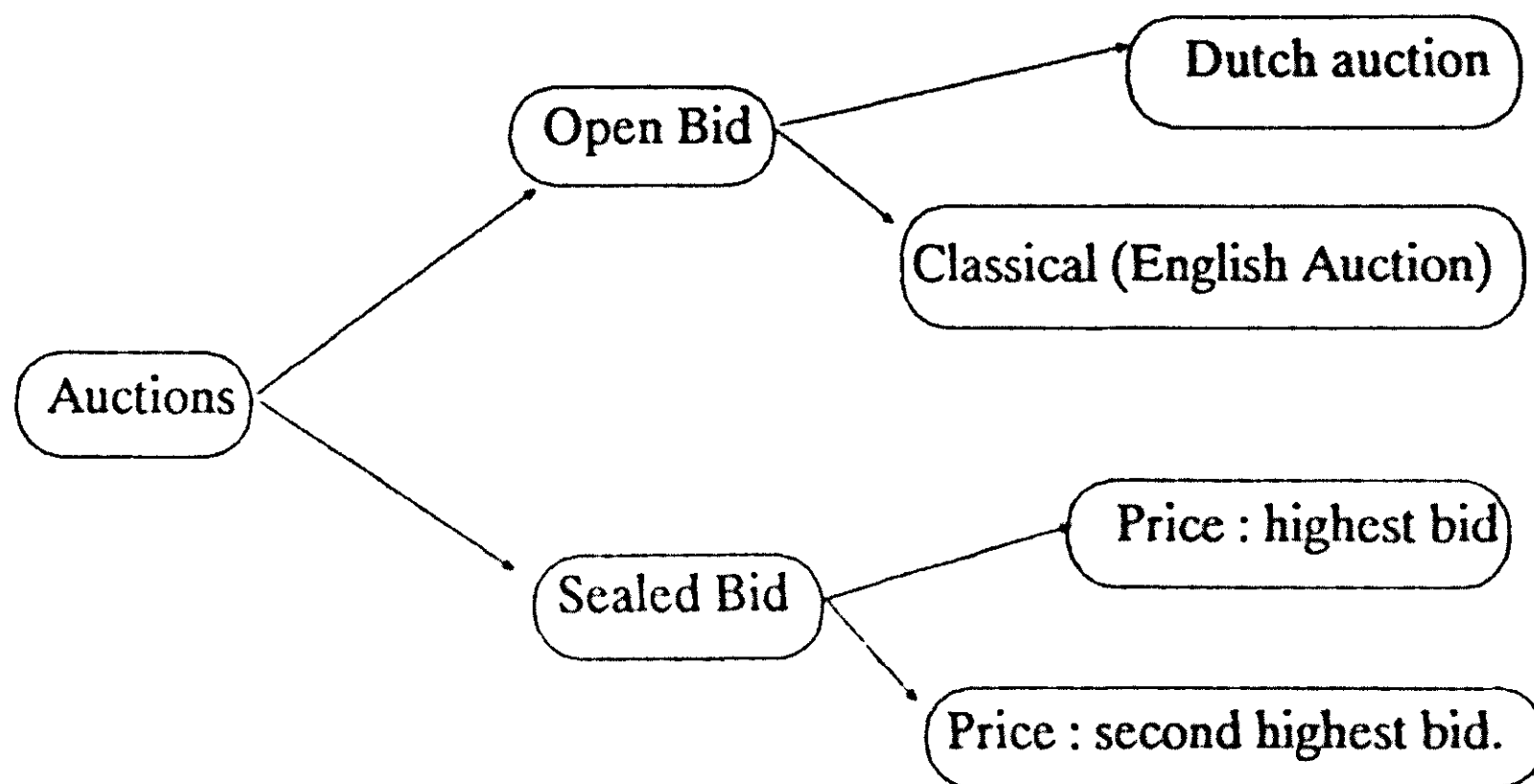
Hopefully this analysis of Dutch auctions is contributing to our knowledge about auctions as a marketing system in general.

2. Auctions as a price discovery institution.

2.1. Some general aspects of the price formation process.

Auctions are an intermediary between buyers and sellers. Their main objective is price discovery. In connection with price formation auctions fulfil also other marketing functions, like product assembly; products for sale are physically supplied to the auction. Being an important marketing institution in the marketing channel of fruit and vegetables and being a cooperative association, Dutch auctions have gradually assumed additional marketing functions.

Basically there are four ways of price formation by auctions (see for instance : Philips, 1988; Cassady, 1967; and Smith, 1989).



Auction systems in principle differ on two criteria. The first criterion is whether the price formation process is by open bidding or by sealed bidding. If buyers have perfect information on market supply and buyers are bidding on the basis of their reservation price, there does not seem any difference between open and sealed bidding. However, if this is not the case, bidding in the open in contrast to sealed bidding is providing additional market information to buyers during the buying process. Psychological aspects of the buying process are more important in open bidding, in particular in the English auction, than in sealed bidding. Sealed bidding will require a longer time period and organisational efforts per lot than open bidding. This difference is in particular important when a great many lots have to be sold in a short period of time, as happens to be the case marketing fresh produce.

At least from the theoretical point of view there is a fundamental difference between the classical English auction and the Dutch auction. In the English auction bidding starts from a low price and after a number of successive bids the ultimate highest bidder will purchase the product for sale. At Dutch auctions the bidding process starts from a high price and is lowered by means of a clock or by the auctioneer until the first and highest buyer purchases the lot.

At the English auction the highest bidder will pay a price which is marginally higher than the reservation price of the second highest bidder. At the Dutch auction a buyer will bid at his own reservation price, since he does not know the reservation price of his nearest competitor. As a result there will be a substantial difference between the highest bid at Dutch and English auctions when there is a large difference between the reservation price of the highest and second highest bidder. This point seems less relevant, when successively a great many lots of the same product are for sale in one auction session. In that case also buyers at Dutch auctions get some knowledge about the reservation prices of their competitors.

Dutch auctioning seems more efficient than the classical English auctioning since after one bid the lot is sold as against after a time consuming series of bids in the English auction.

The distinction between sealed bidding, wherein the highest bidder gets the lot for sale at his reservation price and sealed bidding, wherein the highest bidder gets the lot at the second highest reservation price is similar to the distinction between price formation by Dutch auction and by classical English auction. In the former case the buyer has to pay his reservation price, in the latter case he has to pay a marginally higher price than the second highest reservation price.

2.2. The effectiveness of the price formation process at auctions.

Some conditions have to be fulfilled in order to have an effective price formation process at an auction. In particular the following conditions seem important.

- Potential buyer should know the quality characteristics of the products for sale.

Potential buyers should know the properties of the product for sale (Clearly this does not imply that buyers know the utility, and the reservation price, attached to the product by competitive buyers). The

market should be transparent with respect to product quality. Product standardisation, sorting and grading are for that reason very important. It is a very important task of auctions to maximise product knowledge of potential buyers.

Product supply at Dutch horticultural auctions is graded and sorted either on the the basis EC-standards, of national standards or on the basis of standards of the auction.

The application of grading and sorting procedures has been enhanced by government measures. For instance, quality grading of fruit and vegetables to be exported was made compulsory in the Netherlands in 1938 by an Agricultural Export Act. Export grading rules were introduced and an Export Inspection Bureau for Horticultural Products was made responsible for controlling the system. Grading of vegetables was also necessary for a smooth operation of the minimum price scheme which has been introduced for vegetables at Dutch auctions in 1949.

Grading and sorting of flowers is more difficult. Nevertheless Dutch flower auctions have developed rules/ procedures with respect to sorting and grading of cut flowers and pot plants.

- Potential buyers must be interested to purchase at auctions.

When middlemen feel that auctions are an inferior type of market for buying a specific product, they will search for other ways of purchasing. For that reason auctions should offer in addition to effective price formation additional services to buyers.

At the start of Dutch auctions, wholesalers were not inclined to purchase at auctions, since they were suspicious about the price formation process at auctions. However they gradually developed a more favourable attitude towards the auction system. Attractive features of auctions to wholesalers are amongst others the possibility to purchase at one spot a complete assortment of fruit and vegetables, market

information for middlemen and facilities for middlemen to prepare and dispatch the purchased products to their clients.

- Auctions should have a substantial market share.

If auctions have a small market share, price formation at auctions might be suboptimal for various reasons. In that case a great many traders in the respective product do not participate in the price formation process at the auction. Also in that situation buyers at auctions will probably hesitate to bid their highest reservation price.

Dutch horticultural auctions were able to build up major market shares, of 70 % or more in the national market of fresh horticultural products. Various factors have enhanced this large market share :

a) members of co-operative auctions are compelled to sell their products through auctions; in fact all auctions are co-operatives having written into their regulations a compulsory auctioneering clause.

b) compulsory auctioneering was imposed by the Government from 1916 - 1918 and from 1933 - 1966. Afterwards this regulation stopped since compulsory auctioneering in the Netherlands was not compatible with an open EC market.

- There should be no collusion between buyers at auctions.

No collusion between buyers is necessary for price formation, which is in accordance with market demand and supply. A large number of buyers is helpful to prevent collusion between buyers. In order to attract more buyers Dutch auctions have merged into larger co-operatives.

- There should be geographic market transparency.

Effective price discovery requires market transparency between local and regional auctions of a country which sell the same product.

Prices at various auctions should be the same apart from price differences because of differences in quality and in marketing costs. For that reason there should be adequate exchange of information between auctions. In the Netherlands purchasers at different auction can communicate by telephone and inform each other about price development at their respective auction.

Electronic Data Interchange increase possibilities for geographic price transparency. Some auctions have connected their auction clocks, which makes it possible for a purchaser being physically at auction A to bid for products for sale auction B.

Also in order to optimize price formation geographically a product is sold at different auctions at the same hour of the day.

3. Cooperative structure of auctions.

Auctions in the Netherlands are cooperatives. In the introductory stage some auctions were private companies. However, only cooperative auctions have stayed in business. Cooperative auctions are democratic in character and the control remains in the hands of the growers themselves, who at their meetings elect their Executive Board out of their own membership. The day to day operations and the administration of the auction is in the hands of a managing board. A financial committee elected at meetings is supervising the policy, in particular the financial policies, of the Executive Board.

The auctions are financed by the deduction of an agreed percentage of the gross proceeds of the sale of produce, say 4 - 5 %. Also banker's loans, in particular of cooperative banks, are used for financing the operations of cooperative auctions.

Members of cooperative auctions are free in the quantity and quality of product they offer for sale, given some minimum conditions with respect

to product quality and package. Another element of a cooperative is that the executive board consists of growers, who might have not enough strategic and managerial capacities to run an auction become larger. Professional managers are needed to manage a co-operative auction. But at the same time it must be recognized that auctions are still the property of growers. Growers have to decide about the long term strategy of the co-operative auction, but they should be have according to the instructions of managers in operational matters and they should give room to professional managers in the preparation of the auction strategy.

Auction managers try to stimulate the production of new products and to improve product quality for sale at the auction by giving advice to growers and sometimes financial support to grow new products. They cannot compel members to produce specific quantities and qualities. Precise planning of market supply by auctions is impossible.

Amongst others since large food chains like to plan purchases of fresh produce in advance, they do not seem to be happy with the auction system. For that reason cooperative auctions are searching for special programmes to serve large clients better, like forward auctioneering of products.

Cooperative membership is based not only on economic reasoning but also on arguments of growers' solidarity. Economic arguments are gaining importance as compared to social arguments in growers' loyalty vis a vis their cooperative auction.

As the auctions were established, questions of policy and liaison arose which were not possible of solution on a parochial basis and the need for close collaboration in many matters was apparent. In 1917 a Central Bureau of Auctions was established, being a master organisation of all cooperative auctions of fruit and vegetables. It is in charge of general tasks which can best be performed in a uniform way by all auctions. Grading and packing were important tasks of this Bureau right from the beginning. Soon it got engaged also in advertising and sales promotion. It established a national Minimum price scheme. Minimum prices are fixed for a great number of products. Products which cannot be sold at the minimum price

are destroyed. Growers whose products are destroyed will be compensated by a certain percentage of the minimum price. The activities of the Bureau encompass also product development and product quality, market research, market development, promotion, market research and financial support.

Also cooperative flower auctions have set up a national organisation, which takes care of common interests of flower auctions. Because of a continuous process of amalgamation at present, auctions are getting bigger and are better placed to perform tasks which traditionally have been performed by the National master organisation.

An important characteristic of cooperative auction is that in principle they offer for sale the products of their members only. However, flower auctions accept for sale also product supply of non members. In this way the product assortment is broader/of better quality, which makes auctions more attractive to potential buyers. The counterargument is that additional supply of non members is decreasing auction prices.

A cooperative auction has not only the daily task of discovering market prices on short run, but has also the duty to maintain a profitable price level for the products in question on long run. Therefore cooperative auctions got engaged in other marketing activities besides price formation, which do not seem essential for an auction as such.

These additional marketing activities of Dutch auctions comprise the improvement of product quality and products assortment by grading schemes, research and advice to growers.

Advertising and sales promotion have become a standard activity of cooperative auctions in order to strengthen customer loyalty and create new markets. For instance, in 1991 fruit and vegetables auctions spent 23.4 million guilders on promotion, while total sales amounted to 4.3 billion guilders, i.e. 0.5% of total sales (Centraal Bureau van de Tuinbouwweilngen, 1992)

Logistical operations and marketing information are very important instruments of cooperative auctions in order to reinforce the competitive position of the market supply of their members. Cooperation with retail chains in marketing and promotional programs is increasingly important.

4. Auctions in relation to the type of product.

Different types of auctions are in use for different products. The English auction is used for example in the United States in selling cattle. In English auctions buyers will receive information about the market - like the interests of potential buyers - during the bidding process. For that reason products having unique features, like paintings, will often be sold by English auction. There is room for psychological tactics, in particular of the auctioneer, in the bidding process.

Sealed bidding is in use amongst others for tobacco. In that system prices are determined on the basis of individual expectations about market supply and demand.

The dutch auction is used when a great number of lots of a perishable product have to be sold in a short time, say in some hours. It is an efficient selling operation and it is supposed to realise the maximum reservation price of buyers. In the Netherlands it is used for the sale of fresh fruit and fresh vegetables, for fish and for eggs. In that case a great many lots of perishable product are sold during a short period of time.

While auctions are still the dominating marketing institution for fresh horticultural products in the Netherlands, they have lost importance for eggs. In case of eggs, product assortment is smaller than for fruit and vegetables. Also the assembling function has become less important in marketing eggs, since poultry farms have become larger.

5. The need for marketing management in marketing horticultural products is a challenge to Dutch horticultural auctions.

Horticultural auctions in the Netherland operate in dynamic markets. Consumers' wants and needs are changing. Consumers are more critical of producers, both with respect to products and production method. Retail chains have specific wishes with respect to the products to be delivered. They require specific services from suppliers, particularly in the field of logistics. At the supply side of the market much is changing too. New varieties are introduced and new competitors enter into the market. As a result horticultural marketing in the Netherlands has become more than selling a product at the best price. A marketing management policy, using all marketing instruments Product, Price, Promotion and Distribution is necessary. Horticultural auctions, being the most important marketing institution in marketing Dutch horticultural products, have to accommodate to these market changes. However, auctions are price discovery institutions and have a limited say about the marketing instruments product, promotion and distribution. But being a co-operative, they are responsible to market the products of their members in the best possible way. So auctions are extending their activities in the field of product policy, promotion, market information and logistical operations. Unfortunately they lack the institutional power to command the marketing instruments product, promotion and distribution.

Being a cooperative they leave it up to the member-growers to decide about the quantity and quality to be produced. Being an auction they do not interfere in the business of middlemen, being their clients. So they have to execute marketing management policies by advice to and deliberation with growers and middlemen. Actually auctions are developing new marketing propositions in terms of product quality, product assortment and services and try to get them introduced with growers and middlemen. Auctions have extended their activities in the field of promotion, quality control, new product development and logistical services.

Such programs are not always good enough. Special marketing programs with selected groups of members of the cooperative have to be set up in order to satisfy the wishes of important clients. Also cooperatives work together with wholesalers and retailers in special programs for the development of new markets and in special promotional programs. They

have introduced special marketing procedures to serve large buyers, like large food chains. Flower auctions have set up a brokerage operation for pot plants in addition to the auction operation. Vegetable auctions have introduced special auctions for future delivery, say one week ahead.

In this way Dutch horticultural auctions are developing themselves toward marketing institutions having a much broader scope than auctioneering as such. The important task of Dutch horticultural auctions is how to combine the price discovery task of the auction process with the marketing programming vis a vis product, price, promotion and distribution. The former task is specific for the auction. The latter, marketing programming, is a joint task of growers, auctions and middlemen together. But the auctions have to play a central role in this respect (Meulenberg, 1989)

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