

Bundled Bidding

by

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It is often the case that two or more tenders may be issued simultaneously for related projects. For governments, these might be tenders for two aspects of a policy formation or implementation. For example, a local government parks project might involve a landscaping and paving aspect. Now sometimes, the tender is for and all in one provision of both tasks. Other times, it is for each separately. In either case, the tender or tenders is missing something of potential value. I will argue here that offering a bundled option may be a preferable third way.

It is perhaps easiest to see this by way of a very stylised example. Suppose that supplier A can provide both landscaping and paving. If it was undertaking both tasks, it would be able to do them both for \$200. However, if it was to do only one, that task alone would cost it \$150. (Yes, this is really stylised!) In effect, it is cheaper for A to provide both tasks together than separately. In economics, this is a situation where there are *economies of scope*.

There are two other potential suppliers. Supplier B is a landscape specialist and C is a paving specialist. Each of these *specialist* suppliers can do their respective task for \$125 a piece.

Finally, suppose that all suppliers reckon that the maximum budget for the parks project is \$300 and each has enough knowledge to know precisely who their competitors might be for any given tender.

Option 1 would be for the parks project to be split into two separate tenders. In this situation, A would bid for both projects, B would bid for the landscape project and C would bid for the paving job. In this situation, both B and C would be the low cost providers and could win their respective tenders for about \$149 each. This would result in a total expenditure of just under \$300.

Alternatively, for option 2, the parks project may be tendered as one job. In this case, only A would be able to bid for it and could get away with a total bid of \$300. Even if the other two got together, this would still be the outcome. So, from this perspective, there is little difference between options 1 and 2 although, in part, that is an artifact of my simple numbers. Change them a little and different outcomes result.

Now consider a third option. Option 3 would issue two tenders but allow one provider to engage in 'bundled bidding' for both jobs. This would allow supplier A (our generalist) to submit a bid like the following: "I can do the landscaping or paving job for \$150 a

piece but if I get both of them I can do the lot for \$249.” The other suppliers would still bid for their own jobs but each would know A would be engaging in a bundled bid and submit a price of \$125 each.

In the end, A’s bundled bid beats both of those options as the government would compare it to the best separated option totaling \$250 (\$125 from each of B and C). But the key point is that the entire expenditure is much lower. It is lower because the government is able to create competition between generalist and specialist providers and exploit each one’s strengths – in this case, A’s economies of scope and B and C’s gains from specialisation. Even had A’s costs been in excess of \$250 for both, making specialist provision better, Option 3 would reduce the cost of the parks project.

The moral of this story is that allowing for bundled bidding on related projects is superior to separate tenders or all-in-one deals. When you have many tasks of a single project, this is certainly the option worth considering.

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