Pricing the Right to Renege in Search Markets: Evidence from Trucking *

Richard Faltings †

Job Market Paper | July 2, 2024

Full draft is subject to confidentiality review until July 25, 2024 and will be made publicly available thereafter.

Click here for the latest version.

Abstract

In many search markets, advance contracts allow one party to renege against a penalty, granting them the option to keep searching for alternatives. This paper studies the efficiency of such arrangements in the trucking industry, leveraging novel data from an online freight auction platform. Reneging is widespread on the platform and more likely at low prices, suggesting opportunistic behavior on the side of the carriers. A dynamic model of the carrier search process rationalizes these patterns and links the platform's cancellation penalty to the search and bidding behavior of the carrier's. Using estimates of the model, I simulate counterfactual cancellation schedules with both increasing and uniform penalties. The findings suggest that increasing the current reputational penalty reduces both firm profits and overall welfare, as the burden of reduced flexibility is shifted to the platform through the bids. Additionally, I explore a switch to pecuniary penalties—common in the travel industry—which give the platform an additional revenue stream. I show that these can increase firm profits at the cost of overall welfare.

*I thank Eugenio Miravete, Dan Ackerberg, Nick Buchholz, and Victoria Marone for their execllent mentorship and advice. I am also grateful to Bob Town, Jorge Balat, Jackson Dorsey, Andrey Ordin, John Asker, Michael Dickstein, Amanda Starc, Volker Nocke, Bob Miller, Brett Hollenbeck, Steve Cicala, Andrey Fradkin, Andre Veiga, Felipe Brugues, Claudia Allende, Yeşim Orhun, Lauri Kytömaa, Hayden Parsley, and participants at the UT Austin IO workshop for helpful comments and discussions. This research was made possible with data from an anonymous company. I wish to thank JL, ACZ, FK, and numerous others at the company for their invaluable support on the project. No financial compensation was provided for this research. The company's review of the paper was limited to ensuring the protection of proprietary information.

†The University of Texas at Austin. Email: richard.faltings@utexas.edu