CSC304 Lecture 9

Mechanism Design with Money: More VCG examples; greedy approximation of VCG; sponsored search

VCG Recap

- $f(\tilde{v}) = a^* = \text{argmax}_{a \in A} \sum_i \tilde{v}_i(a)$
  - Choose the allocation maximizing *reported* welfare

- $p_i(\tilde{v}) = \left[\max_a \sum_{j \neq i} \tilde{v}_j(a)\right] - \left[\sum_{j \neq i} \tilde{v}_j(a^*)\right]$
  - Each agent pays the loss to others due to her presence

- Four properties
  - Strategyproofness
  - Individual rationality (IR)
  - No payments to agents
  - Welfare maximization

Seller as Agent

- Seller (S) wants to sell his car (c) to buyer (B)

- Seller has a value for his own car: $v_S(c)$
  - Individual rationality for the seller mandates that seller must get revenue at least $v_S(c)$

- Idea: Add seller as another agent, and make his values part of the welfare calculations!

Seller as Agent

$v_S(c) = 3$

$v_B(c) = 5$

- What if…
  - We give the car to buyer when $v_B(c) > v_S(c)$ and
  - Buyer pays seller $v_B(c)$: Not strategyproof for buyer!
  - Buyer pays seller $v_S(c)$: Not strategyproof for seller!

What would VCG do?

$v_S(c) = 3$

$v_B(c) = 5$

- Allocation?
  - Buyer gets the car (welfare = 5)
- Payment?
  - Buyer pays: $3 - 0 = 3$
  - Seller pays: $0 - 5 = -5$

Mechanism takes \$3 from buyer, and gives \$5 to the seller!

- Need external subsidy

Problems with VCG

- Difficult to understand
  - Need to reason about what welfare maximizing allocation in agent i's absence
- Does not care about revenue
  - Although we can lower bound its revenue
- With sellers as agents, need subsidy
  - With no subsidy, cannot get the other three properties
- Might be NP-hard to compute

Single-Minded Bidders

- Combinatorial auction for a set of m items S
- Each agent i has two private values (v_i, S_i)
  - $S_i \subseteq S$ is the set of desired items
  - When given a bundle of items A_i, agent has value v_i if $S_i \subseteq A_i$ and 0 otherwise
  - "Single-minded"
- Welfare-maximizing allocation
  - Agent i either gets S_i or nothing
  - Find a subset of players with the highest total value such that their desired sets are disjoint

Single-Minded Bidders

- Weighted Independent Set (WIS) problem
  - Given a graph with weights on nodes, find an independent set of nodes with the maximum weight
  - Known to be NP-hard
- Easy to reduce our problem to WIS
  - Not even $O(m^{0.5-\epsilon})$ approximation of welfare unless $NP \subseteq ZPP$
- Luckily, there's a simple, $\sqrt{m}$-approximation greedy algorithm

Greedy Algorithm

- Input: (v_i, S_i) for each agent i
- Output: Agents with mutually independent S_i

- Greedy Algorithm:
  - Sort the agents in a specific order (we'll see).
  - Relabel them as $1,2,\ldots,n$ in this order.
  - $W \leftarrow \emptyset$
  - For $i = 1,\ldots,n$:
    - If $S_i \cap S_j = \emptyset$ for every $j \in W$, then $W \leftarrow W \cup \{i\}$
  - Give agents in W their desired items.

Greedy Algorithm

- Sort by what?

- We want to satisfy agents with higher values.
  - $v_1 \geq v_2 \geq \cdots \geq v_n \Rightarrow m$-approximation ☹

- But we don't want to exhaust too many items.
  - $\frac{v_1}{|S_1|} \geq \frac{v_2}{|S_2|} \geq \cdots \frac{v_n}{|S_n|} \Rightarrow m$-approximation ☹

- $\sqrt{m}$-approximation : $\frac{v_1}{\sqrt{|S_1|}} \geq \frac{v_2}{\sqrt{|S_2|}} \geq \cdots \frac{v_n}{\sqrt{|S_n|}}$?

[Lehmann et al. 2011]

Proof of Approximation

- Definitions
  - OPT = Agents satisfied by the optimal algorithm
  - W = Agents satisfied by the greedy algorithm
  - For $i \in W$,
$$OPT_i = \{j \in OPT, j \geq i : S_i \cap S_j \neq \emptyset\}$$
- Claim 1: $OPT \subseteq \bigcup_{i \in W} OPT_i$
- Claim 2: It is enough to show that $\forall i \in W$
$$\sqrt{m} \cdot v_i \geq \Sigma_{j \in OPT_i} v_j$$
- Observation: For $j \in OPT_i$, $v_j \leq v_i \cdot \frac{\sqrt{|S_j|}}{\sqrt{|S_i|}}$

Proof of Approximation

- Summing over all $j \in OPT_i$:

$$\Sigma_{j \in OPT_i} v_j \le \frac{v_i}{\sqrt{|S_i|}} \cdot \Sigma_{j \in OPT_i} \sqrt{|S_j|}$$

- Using Cauchy-Schwarz ($\Sigma_i x_i y_i \le \sqrt{\Sigma_i x_i^2} \cdot \sqrt{\Sigma_i y_i^2}$)

$$\Sigma_{j \in OPT_i} \sqrt{|S_j| \cdot 1} \le \sqrt{|OPT_i|} \cdot \sqrt{\Sigma_{j \in OPT_i} |S_j|}$$

$$\le \sqrt{|S_i|} \cdot \sqrt{m}$$

Strategyproofness

- Agent i pays $p_i = v_{j^*} \cdot \sqrt{\frac{|S_i|}{|S_{j^*}|}}$
  - j^* is the smallest index $j > i$ such that $S_j \cap S_i \neq \emptyset$ and $S_j \cap S_k = \emptyset$ for all $k < j, k \neq i$
- How do I interpret j^* and p_i?
  - j^* = agent such that if agent i reports a value $\tilde{v}_i$ low enough to fall below j^* in the ordering, she stops winning. Otherwise, she wins.
  - p_i = lowest value i can report and still win

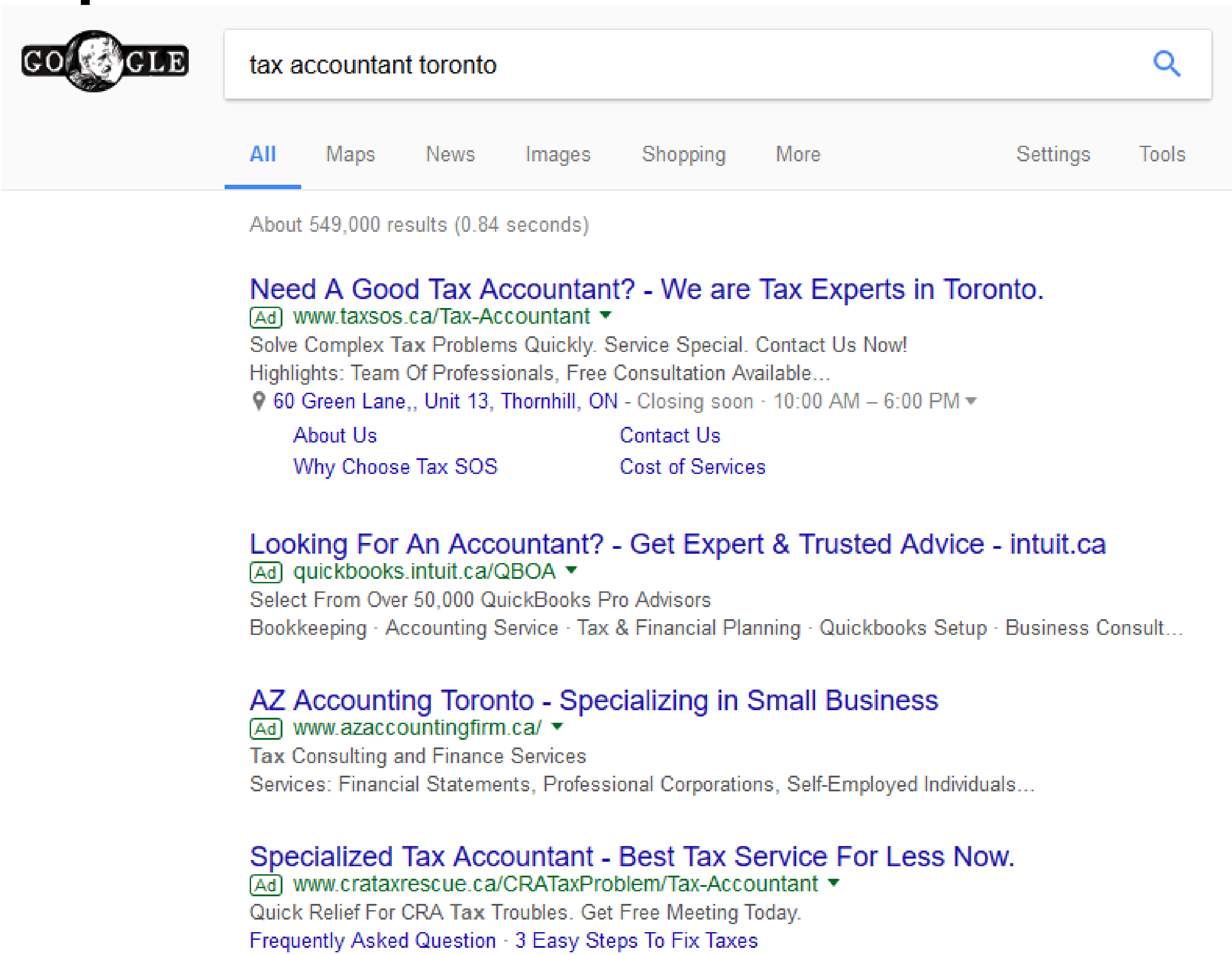
Strategyproofness

- Critical payment
  - Charge each agent the lowest value they can report and still win
- Monotonic allocation
  - If agent i wins when reporting (v_i, S_i), she must win when reporting $v_i' \geq v_i$ and $S_i' \subseteq S_i$.
  - Greedy allocation rule satisfies this.
- Theorem: Critical payment + monotonic allocation rule imply strategyproofness.

Moral

- VCG can sometimes be too difficult to implement
  - May look into approximately maximizing welfare
  - As long as the allocation rule is monotone, we can charge critical payments to achieve strategyproofness
  - Note: approximation is needed for computational reasons
- Later in mechanism design without money…
  - We will not be able to use payments to achieve strategyproofness
  - Hence, we will need to approximate welfare just to get strategyproofness, even without any computational restrictions

Sponsored Search Auctions



Sponsored Search Auctions

- A search engine receives a query
- There are k advertisement slots
  - "Clickthrough rates" : $c_1 \geq c_2 \geq \cdots \geq c_k \geq c_{k+1} = 0$

For convenience

- There are n advertisers (bidders)
  - Bidder i derives value v_i ***<u>per click</u>***
  - Value to bidder i for slot j = $v_i \cdot c_j$
  - Without loss of generality, $v_1 \geq v_2 \geq \cdots \geq v_n$
- Question:
  - Who gets which slot, and how much do they pay?

Sponsored Search : VCG

- VCG
  - Maximize welfare:
    - bidder j gets slot j for $1 \leq j \leq k$, other bidders get nothing
  - Payment of bidder j?

- Increase in social welfare to others if j abstains
  - Bidders $j+1$ through "$k+1$" get upgraded by one slot
  - Payment of bidder j = $\sum_{i=j+1}^{k+1} v_i \cdot (c_{i-1} - c_i)$
  - Payment of bidder j ***<u>per click</u>*** = $\sum_{i=j+1}^{k+1} v_i \cdot \frac{c_{i-1} - c_i}{c_j}$

Sponsored Search : VCG

- What if all the clickthrough rates are same?
  - $c_1 = c_2 = \cdots = c_k > c_{k+1} = 0$
- Payment of bidder j ***per click***
  - $\sum_{i=j+1}^{k+1} v_i \cdot \frac{c_{i-1} - c_i}{c_j} = v_{k+1}$
- Bidders 1 through k pay the value of bidder $k+1$
  - Familiar? VCG for k identical items

Sponsored Search : GSP

- Generalized Second Price Auction (GSP)
  - For $1 \leq j \leq k$, bidder j gets slot j and pays the value of bidder $j+1$ ***per click***
  - Other bidders get nothing and pay nothing

- Natural extension of the "second price" idea
  - We considered this before for two identical slots
  - Not strategyproof
  - In fact, truth-telling may not even be a Nash equilibrium ☹

Sponsored Search : GSP

- But there is a good Nash equilibrium that…
  - realizes the VCG outcome, i.e., maximizes welfare, and
  - generates as much revenue as VCG ☺ [Edelman et al. 2007]

- Even the worst Nash equilibrium…
  - gives 1.282-approximation to welfare ($PoA \leq 1.282$) and
  - generates at least half of the revenue of VCG
    [Caragiannis et al. 2011, Dutting et al. 2011, Lucier et al. 2012]

- So if the players achieve an equilibrium, things aren't so bad.

VCG vs GSP

- VCG
  - Truthful revelation is a dominant strategy, so there’s a higher confidence that players will reveal truthfully and the theoretical welfare/revenue guarantees will hold
  - But it is difficult to convey and understand
- GSP
  - Need to rely on players reaching a Nash equilibrium
  - But has good welfare and revenue guarantees and is easy to convey and understand
- Industry is split on this issue too!

From Theory to Reality

- Value is proportional to clickthrough rate?
  - Could it be that users clicking on the 2nd slot are more likely buyers than those clicking on the 1st slot?
- Misaligned values of advertisers and ad engines?
  - An advertiser having a high value for a slot does not necessarily mean their ad is appropriate for the slot
- Market competition?
  - What if there are other ad engines deploying other mechanisms and advertisers are strategic about which ad engines to participate in?