Simple and Optimal Mechanism in Efficiency and Equality Trade-off

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Mechanism Design

Single objective

• Profit
  • Myerson optimal mechanism

• Social welfare
  • Vickrey-Clarke-Groves mechanism

......
Public Resource Allocation

Public Resource
- Supply-demand imbalance
- Heterogeneous agents

Multi-objective mechanism design
- Efficiency
- Fairness

A good mechanism in practice
✓ Easy implementation
Efficiency

Social
  Social welfare maximization

Individual
  Market equilibrium
Fairness

Fairness defined based on utility

Fairness defined based on allocation (non utility-based)
Utility-based Fairness

• Envy-free: everyone likes his more than others
• Egalitarian: same utility for everyone
• Proportional fairness: utility proportional to contribution
• Max-min: always maximize the minimum utility
Opportunity Fairness (non utility-based)

• Defined only on allocation (independent of utility)
• Lottery
Problem 1: Vehicle License Allocation
(Chen, Qi, Wang WINE’17)
(Chen, Qi, Wang & Wang ‘22)

Background: many big cities started the vehicle licenses control due to the terrible traffic and air quality problem.
In each time period, only a small number of plates can be allocated to the potential car buyers.
Vehicle licenses allocation is a tough problem
Efficiency
Current Mechanism 1: Auction

- Representative: Shanghai (1994-2013.3), Singapore (1990-now)
- Pros: efficiency
- Cons: low affordability, unfair for poor

**Figure:** Singapore’s Auction ($92100 in 2013)
Equality
Current Mechanism 2: Lottery

Representative: Beijing (2010-now), Guiyang (2011-now)

- Pros: fairness
- Cons: low efficiency and winning probability, no value exploration

**Figure:** Winning Probability in Beijing’s Lottery (0.501% in June, 2016)
Beijing’s Data

Waiting time: over 30 years!
Make a Balance

Efficiency & Equality (fairness)
Current Mechanism 3: Reserve-price Lottery

Representative City: Shanghai (2013.4-now)
Pros: easy implementation (winners in lottery pay the reserve price)
Cons: hard to set price, no exploration, inefficiency
Current Mechanism 4: Simultaneous Auction and Lottery

• Representative City: Guangzhou, Hangzhou, Shenzhen...

• Each player chooses either auction or lottery first.
  • Pros: consider both fairness and efficiency
  • Cons: hard to compute the equilibrium, untruthful
Which one is optimal?

- Auction
- Lottery
- Reserve-price Lottery
- Simultaneous Auction and Lottery
Key Result

First auction then lottery (AtL), is the best choice!

✓ Efficiency
✓ Equality
✓ Easy implementation
The Problem

• How to optimally allocate k homogeneous goods to n (> k) unit-demand players with efficiency & equality trade-off?
The Model

• k homogeneous goods, n unit-demand players;

• Suppose w.l.o.g. \( v_1 \geq v_2 \geq \cdots \geq v_n \) are the true private values;

• No need random & independent assumption on values;

• Maximizing efficiency while guaranteeing certain level of equality;

• Pre-computed probabilities \( q_1, q_2, \ldots, q_n \) before knowing values;

• As simple as possible.
Start with Two-group Mechanism

**Step 1** The government determines an integer number
\[ k \in [0, K], \text{ a ratio } \gamma \in \left[ 1, \frac{N}{K} \right]. \]

**Step 2** Highest \( k \gamma \) bids will be allocated \( k \) licenses via lottery (Lottery I);
\( K - k \) licenses allocated to remaining \( N - k \gamma \) players by lottery (Lottery II).

\[
\begin{array}{cccc}
V_1 & V_2 & \cdots & V_{\gamma k} \\
V_{\gamma k+1} & \cdots & V_N
\end{array}
\]

Lottery I: \( k \) licenses       Lottery II: \( K-k \) licenses
Two-group Framework

**MECHANISM 1: Two-Group Framework**

1. The government determines an integer number $n_1 \in [0, n]$, a ratio $t_1 \in \left[\frac{k}{n}, \min\{\frac{k}{n_1}, 1\}\right]$.
2. Every player $i$ submits a bid $b_i \geq 0$.
3. Highest $n_1$ bidders will be allocated with probability $t_1$ (Group I); The other $n - n_1$ players will be allocated the remaining goods with probability $\frac{k-n_1 t_1}{n-n_1}$ (Group II).
4. Only winners of Group I pay $p = \frac{n t_1 - k}{(n-n_1) t_1} \cdot b(n_1 + 1)$; others pay $p = 0$.

**Theorem**

*This mechanism is incentive compatible and ex-post individual rational.*
Efficiency Measure

**Efficiency** is defined as the social welfare:

\[ Z(q) = \sum_{i=1}^{n} q_i v_i \]

The efficiency of our mechanism is

\[ Z(n_1, t_1) = t_1 \sum_{i=1}^{n_1} v_i + \frac{k - n_1 t_1}{n - n_1} \sum_{i=n_1+1}^{n} v_i \]
Equality

**Equality** is defined by Gini coefficient [Corrado, 1936]

\[ \eta(q) = 1 - G(q) \]

The equality of our mechanism is

\[ \eta(n_1, t_1) = \frac{n(k - n_1 t_1) + n_1 k}{nk} \]

- Gini index: \( G = A/(A+B) \)
- Equality = 1 - G
A Unified Framework

Proposition

By choosing different parameters $k$ and $\gamma$, our mechanism either includes the existing mechanisms as special cases or outperforms them.

- **Auction**: $n_1 = k$, $t_1 = 1$,
- **Lottery**: $t_1 = \frac{k}{n}$ (or $n_1 = 0$),
- **Reserved-price Lottery**: Setting $n_1 = n_p$, $t_1 = \frac{k}{n_p}$
- **Simultaneous Auction and Lottery**: Setting $n_1 = \ell$, $t_1 = 1$
How to compute optimal mechanism under the framework?
Math Formula of optimal two-group mechanism

Let $v_1 \geq v_2 \geq \cdots \geq v_N$ be the true private values. Our problem is to solve the following programming:

$$\max_{n_1, t_1} \quad Z(n_1, t_1) = t_1 \sum_{i=1}^{n_1} v_i + \frac{k - n_1 t_1}{n - n_1} \sum_{i=n_1+1}^{n} v_i$$

s.t. \quad \eta(n_1, t_1) = \frac{n(k - n_1 t_1) + n_1 k}{nk} \geq c,$$

$$\frac{k}{n} \leq t_1 \leq \frac{n}{n},$$

$$1 \leq n_1 \leq n,$$

$$n_1 t_1 \leq k.$$

where $c \in [0, 1]$ is a pre-determined constant to measure the least required equality.
Challenges

Determine $n_1$, $t_1$

before knowing any information about the values $v_i$
Slight change, Big difference

Suppose $n = 6$, $k = 3$, and $\eta(k, \gamma) \geq c = 5/6$, then:

- $(v_1, v_2, v_3, v_4, v_5, v_6) = (4, 3.5, 3, 1, 0.8, 0.6)$, then the optimal mechanism is with $n_1 = 3$ and $t_1 = 2/3$.

- If $(v_1, v_2, v_3, v_4, v_5, v_6) = (5, 3.5, 3, 1, 0.8, 0.6)$, then the optimal mechanism is with $n_1 = 1$ and $t_1 = 1$.

- If $(v_1, v_2, v_3, v_4, v_5, v_6) = (4, 3.5, 3, 3, 0.8, 0.6)$, then the optimal mechanism is with $n_1 = 4$ and $t_1 = 5/8$. 
Main Result: Optimal mechanism
(Chen, Qi, Wang & Wang Recent work)

Theorem (1)

If $\Delta_i \geq \Delta_{i+1}, \ \forall \ i = 0, \ldots, n - 1$, where $\Delta_i := v_i - v_{i+1}$, then $\forall c$, the optimal $n_1, t_1$ can be computed quickly with $n_1 = \frac{nk(1-c)}{n-k}$, $t_1 = 1$ (i.e., Auction then Lottery).

Figure: pyramid-shaped value lead to decreasing spacing
Main Result: Optimal mechanism

Theorem (2)

If $\Delta_i \geq \Delta_{i+1}$, $\forall \ i \leq \frac{n-1}{2}$, $\Delta_i \geq \Delta_{n-i}$, $\forall \ i \leq \frac{n}{2}$, and $n \geq 2k$, then $\forall c$, the optimal $n_1, t_1$ can be computed quickly with $n_1 = \frac{nk(1-c)}{n-k}$, $t_1 = 1$ (i.e., Auction then Lottery).

Figure: olive-shaped value negatively skewed spacing
Random Values
(Chen, Qi & Wang WINE’17)

• Assume players’ values $v$ are i.i.d. from $F(f)$
Random Values

Assume players’ values $v$ are i.i.d. from $F(f)$

Theorem

If the probability density function $f(\cdot)$ is non-increasing, then every Pareto optimal mechanism is Auction then Lottery.

Theorem

If $f(\cdot)$ satisfies $f(F^{-1}(x)) \geq f(F^{-1}(1 - x))$, $\forall x \in [0, 1/2]$, and $f(F^{-1}(1 - x))$ is non-decreasing about $x \in [0, 1/2]$, then every Pareto optimal mechanism is Auction then Lottery.
Main Result

Surprisingly!

For all the common distributions, the optimal mechanism is:

$$\gamma = 1, k = \frac{NK(1-c)}{N-K}$$ (first auction, then lottery!)

**THEORETICAL** Classic distributions: Normal, Uniform, Exponential

**EMPIRICAL** Power law relationship (economic and empirical study): Log-normal, Power-law, Truncated normal, gamma

- Semi-distribution free!
- No need to know any information about the distribution
Key Ideas

efficiency with fairness constraint ⇐ mean difference ⇐ spacing ⇐ pdf
information
Procedure of Our Optimal Mechanism

Government
- Decide License Num K, fairness level $c$
- Calculate $k = \frac{NK(1-c)}{N-K}$
- Announce winners, payment $p = \frac{N-K}{N-k}v^{(k+1)}$

Time Line
- Auction Day-1
- Auction Day

Players
- Register
- Submit bids

Distribution Free
- Truthful Bidding
Good?

Mechanism “Auction then Lottery” is always Pareto optimal when:
1. there are two group of probabilities;
2. the values $v_i$ satisfy some natural conditions.

What about its **general performance**?
Benchmark: The real optimal solution

- Values $v_1 \geq v_2 \geq \cdots \geq v_n$ can be any case;
- The allocation probabilities can be mutually different.

$$\max_q Z(q, v) := \sum_{i=1}^{n} q_i v_i \quad (1a)$$

$$\text{s.t.} \quad \frac{1}{nk} \left( \sum_{i=1}^{n} (2i - 1)q_i \right) \geq c, \quad (1b)$$

$$\sum_{i=1}^{n} q_i = k, \quad (1c)$$

$$1 \geq q_1 \geq q_2 \geq \cdots \geq q_n \geq 0. \quad (1d)$$
Approximation Ratio

- For any given equality level $c$;
- Denote $q^{al}$ as the allocation probabilities of AtL mechanism with $t_1 = 1, n_1 = \frac{nk(1-c)}{n-k}$;

$$\text{Approximation Ratio} := \min_{v \in V} \frac{Z(q^{al}, v)}{\max_{q \in Q} Z(q, v)} = \min_{v \in V} \min_{q \in Q} \frac{Z(q^{al}, v)}{Z(q, v)}$$

Note: $\min_{v \in V} \min_{q \in Q} \frac{Z(q^{al}, v)}{Z(q, v)} = \min_{q \in Q} \min_{v \in V} \frac{Z(q^{al}, v)}{Z(q, v)}$
Main Result: Approximate Optimality
(Chen, Qi, Wang & Wang Recent work)

Theorem

For every $c$, using mechanism AtL can always guarantee at least $\frac{3}{4}$ of the optimal social welfare, i.e.,

$$\text{Approximation ratio} = \min_{v \in V_1} \frac{Z(q^{al}, v)}{\max_{q \in Q} Z(q, v)} \geq \frac{3}{4}$$
Better Approximation at Certain Conditions

Theorem

If $\Delta_1 \geq \Delta_2 \cdots \geq \Delta_{n-1}$, then $\forall c$, the efficiency of mechanism AtL

$$Z(q^a_l, v) \geq \max_{q \in \mathcal{Q}} Z(q, v) - v_1, \forall v \in V$$
Better Approximation at Certain Conditions

**Theorem**

If $\Delta_1 \geq \Delta_2 \cdots \geq \Delta_{n-1}$, then $\forall c$, the efficiency of mechanism AtL

$$Z(q^{al}, v) \geq \max_{q \in Q} Z(q, v) - v_1, \forall v \in V$$

**Theorem**

If $\exists s \geq \frac{n}{2}$ s.t. $\Delta_1 \geq \Delta_2 \geq \cdots \geq \Delta_s$, $\Delta_s \leq \Delta_{s+1} \leq \cdots \leq \Delta_n$ and $\Delta_{s-i} \geq \Delta_{s+i}, \forall i \leq \min\{s, n - s\}$, then $\forall c$, the efficiency of mechanism AtL

$$Z(q^{al}, v) \geq (1 - \frac{k}{n}) \max_{q \in Q} Z(q, v) - 3\nu_{max}, \forall v \in V$$
Simulation: Comparison under distribution

(a) Efficiency Under $\ln N(9.6228, 0.2129)$, $n = 400000$, $k = 8000$

<table>
<thead>
<tr>
<th></th>
<th>$Z_{al}$</th>
<th>$\mathcal{E}_{opt}$</th>
<th>Gap</th>
</tr>
</thead>
<tbody>
<tr>
<td>$c = 0.3$</td>
<td>183618004</td>
<td>183624500</td>
<td>0.0035%</td>
</tr>
<tr>
<td>$c = 0.5$</td>
<td>168916563</td>
<td>168925666</td>
<td>0.0054%</td>
</tr>
<tr>
<td>$c = 0.8$</td>
<td>144402231</td>
<td>144406293</td>
<td>0.0028%</td>
</tr>
<tr>
<td>$c = 0.9$</td>
<td>135013621</td>
<td>135017294</td>
<td>0.0027%</td>
</tr>
</tbody>
</table>

**Table:** Comparison Under Different Distributions
Comparison under distribution

<table>
<thead>
<tr>
<th>c</th>
<th>$Z_{al}$</th>
<th>$Z_{opt}$</th>
<th>Gap</th>
</tr>
</thead>
<tbody>
<tr>
<td>0.3</td>
<td>253859011</td>
<td>253867192</td>
<td>0.0032%</td>
</tr>
<tr>
<td>0.5</td>
<td>224153384</td>
<td>224171696</td>
<td>0.0082%</td>
</tr>
<tr>
<td>0.8</td>
<td>175932376</td>
<td>175941577</td>
<td>0.0052%</td>
</tr>
<tr>
<td>0.9</td>
<td>158118046</td>
<td>158134262</td>
<td>0.0103%</td>
</tr>
</tbody>
</table>

Table: Comparison Under Different Distributions

(a) Efficiency Under $TN(16802, 8184^2)$
Comparison under distribution

<table>
<thead>
<tr>
<th></th>
<th>Z_{al}</th>
<th>Z_{opt}</th>
<th>Gap</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>c = 0.3</strong></td>
<td>539854494</td>
<td>540019060</td>
<td>0.0305%</td>
</tr>
<tr>
<td><strong>c = 0.5</strong></td>
<td>445652648</td>
<td>445745078</td>
<td>0.0207%</td>
</tr>
<tr>
<td><strong>c = 0.8</strong></td>
<td>282866045</td>
<td>282921361</td>
<td>0.0196%</td>
</tr>
<tr>
<td><strong>c = 0.9</strong></td>
<td>217811469</td>
<td>217853933</td>
<td>0.0195%</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th></th>
<th>Z_{al}</th>
<th>Z_{opt}</th>
<th>Gap</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>c = 0.3</strong></td>
<td>213797147</td>
<td>213799878</td>
<td>0.0013%</td>
</tr>
<tr>
<td><strong>c = 0.5</strong></td>
<td>191117159</td>
<td>191119972</td>
<td>0.0015%</td>
</tr>
<tr>
<td><strong>c = 0.8</strong></td>
<td>157096389</td>
<td>157096481</td>
<td>0.0000%</td>
</tr>
<tr>
<td><strong>c = 0.9</strong></td>
<td>145754486</td>
<td>145755179</td>
<td>0.0005%</td>
</tr>
</tbody>
</table>

Table: Comparison Under Different Distributions
Comparison under different values

<table>
<thead>
<tr>
<th>n</th>
<th>k</th>
<th>c</th>
<th>Max Gap</th>
<th>Min Gap</th>
<th>Average Gap</th>
</tr>
</thead>
<tbody>
<tr>
<td>10000, k = 100, c = 0.9, $\mathcal{U}(0, 1)$</td>
<td>0.396%</td>
<td>0.091%</td>
<td>0.147%</td>
<td></td>
<td></td>
</tr>
<tr>
<td>10000, k = 100, c = 0.5, $\mathcal{U}(0, 1)$</td>
<td>1.302%</td>
<td>0.333%</td>
<td>0.477%</td>
<td></td>
<td></td>
</tr>
<tr>
<td>10000, k = 100, c = 0.3, $\mathcal{U}(0, 1)$</td>
<td>1.125%</td>
<td>0.411%</td>
<td>0.560%</td>
<td></td>
<td></td>
</tr>
<tr>
<td>10000, k = 200, c = 0.5, $\mathcal{U}(0, 1)$</td>
<td>0.889%</td>
<td>0.013%</td>
<td>0.016%</td>
<td></td>
<td></td>
</tr>
<tr>
<td>10000, k = 400, c = 0.5, $\mathcal{U}(0, 1)$</td>
<td>0.941%</td>
<td>0.053%</td>
<td>0.197%</td>
<td></td>
<td></td>
</tr>
<tr>
<td>10000, k = 800, c = 0.5, $\mathcal{U}(0, 1)$</td>
<td>0.939%</td>
<td>0.060%</td>
<td>0.195%</td>
<td></td>
<td></td>
</tr>
<tr>
<td>10000, k = 1600, c = 0.5, $\mathcal{U}(0, 1)$</td>
<td>0.687%</td>
<td>0.013%</td>
<td>0.144%</td>
<td></td>
<td></td>
</tr>
<tr>
<td>10000, k = 3200, c = 0.5, $\mathcal{U}(0, 1)$</td>
<td>0.543%</td>
<td>0.013%</td>
<td>0.110%</td>
<td></td>
<td></td>
</tr>
<tr>
<td>10000, k = 1000, c = 0.5, $\ln \mathcal{N}(0, 1)$</td>
<td>0.041%</td>
<td>0.035%</td>
<td>0.038%</td>
<td></td>
<td></td>
</tr>
<tr>
<td>10000, k = 1000, c = 0.5, $\ln \mathcal{N}(0, 0.5)$</td>
<td>0.032%</td>
<td>0.030%</td>
<td>0.031%</td>
<td></td>
<td></td>
</tr>
<tr>
<td>10000, k = 1000, c = 0.5, $\ln \mathcal{N}(0, 0.25)$</td>
<td>0.026%</td>
<td>0.020%</td>
<td>0.022%</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Table: Comparison for 1000 times
Comparison under different values

<table>
<thead>
<tr>
<th>n=1000, k=100, c=0.5</th>
<th>$Z_{al}$</th>
<th>$Z_{opt}$</th>
<th>Gap</th>
</tr>
</thead>
<tbody>
<tr>
<td>half $U(0, 1)$, half $U(10, 11)$</td>
<td>834.772</td>
<td>1048.980</td>
<td>20.421%</td>
</tr>
<tr>
<td>half $U(1, 2)$, half $U(9, 10)$</td>
<td>782.468</td>
<td>948.834</td>
<td>17.534%</td>
</tr>
<tr>
<td>half $U(2, 3)$, half $U(8, 9)$</td>
<td>730.829</td>
<td>850.529</td>
<td>14.074%</td>
</tr>
<tr>
<td>half $U(3, 4)$, half $U(7, 8)$</td>
<td>677.608</td>
<td>750.389</td>
<td>9.699%</td>
</tr>
<tr>
<td>half $U(4, 5)$, half $U(6, 7)$</td>
<td>626.154</td>
<td>650.201</td>
<td>3.698%</td>
</tr>
<tr>
<td>All $U(5, 6)$</td>
<td>575.894</td>
<td>575.895</td>
<td>0.193%</td>
</tr>
</tbody>
</table>

Table: Comparison with Two Value clusters
Problem 2: Public Housing
(Zhou, Qi, Wang, Wang WINE’17)

Private house is hardly affordable for most residents.

**Figure:** Median house price to annual income
Public Housing in Hong Kong

Low income households are willing to live in public housing, with very low rents.

- In Hong Kong, 44.7% of the population (3.3 million people) are living in public houses.
- About 20,000 applications per year.
- Over 250,000 applications are still waiting.
- Average idle waiting time is more than 5 years.
Current Allocation Rules

- Lottery (e.g., New York)
  - single lottery
  - repeated lottery
- Waitlist (e.g., Hong Kong)
Current Waitlist System in Hong Kong

*Question*: Will it be better if allowing other deferral number?
Objective

Previous research has shown that lottery is outcome equivalent to waitlist with specific parameter (deferral number).

Our objective: optimize the waitlist mechanism under several metrics (idle waiting time, social welfare, etc)
Our Work

We investigate a unified waitlist mechanism where agents could have various numbers of deferral chances, and derives the optimal choice.

- consider agents’ optimal strategies
- characterize the equilibrium state
Agent’s Problem

Assume agents are affected by the aggregate actions of all other agents, and each agent actually faces a Markov Decision Process.

\( \tau \): idle waiting time in equilibrium state.

- **State space:** \( S = \{- \lceil \tau \rceil - 1, - \lceil \tau \rceil, \ldots, -1, 0, 1, \ldots, k\} \).
- **Action set:** for \( s < 0 \), \{wait\}; for \( s \geq 0 \), \{Accept, Reject\}.
- **Transition:**
  - for \( s < k \), matches if choosing ‘Accept’, and goes to state \( s + 1 \) otherwise;
  - for \( s = k \), matches if choosing ‘Accept’ and goes back to state \(- \lceil \tau \rceil\) with probability \( \lceil \tau \rceil + 1 - \tau \) and state \(- \lceil \tau \rceil - 1\) with probability \( \tau - \lceil \tau \rceil \) otherwise.
Agent’s Strategy

\( V(s) \): value of state \( s \)
\( A_s \): action set at state \( s \)
\( s_a \): state after acting \( a \) at state \( s \).

For an agent with outside option \( \alpha \),

\[
V_\alpha(s) = \delta \cdot \mathbb{E}_v \left[ \max_{a \in A_s} \{(v - \alpha)1_{\text{matched}} + V(s_a)(1 - 1_{\text{matched}})\} \right].
\]

- state value
- utility if accept the offer
- utility if stay to next period

Optimal Strategy: Based on a threshold on the outside option
Evaluation Metrics

- Idle waiting time $\tau_k$.
  - number of periods taken from the bottom position to the top position.
  - smaller is better

- Match value $v_k(\alpha)$:
  \[
  v_k(\alpha) = \frac{1}{\pi_k(\alpha)} [Pr(\text{matches } v_H \text{ house}) + v_L \cdot Pr(\text{matches } v_L \text{ house})].
  \]

  - $\pi_k(\alpha)$: probability that an agent with outside option $\alpha$ matches
  - shows whether the matched agents receive their desirable houses
  - larger is better
Evaluation Metrics

- Match distribution $F_k(\alpha)$:

$$F_k(\alpha) = \frac{1}{\mu} \int_0^\alpha \pi_k(\beta)f(\beta)d\beta.$$ 

-評估了多少低收入家庭從公營住宅獲益
  - 更高更好

- 社會福利 $W_k$:

$$W_k = \frac{1}{\mu} \mathbb{E}_\pi[u_k(\alpha)],$$

- $u_k(\alpha) = \pi_k(\alpha)(\nu_k(\alpha) - \alpha)$ 是一個代理的期望收益
  - 更高更好
Main Result

Under the same waiting time, we can gain 10% of the social welfare by increasing the deferral number from 2 to 5.
A pandemic adds **capacity restrictions** to shops, gyms, schools, and public spaces such as parks and beaches, which seem limitless under normal circumstances.
We want to achieve an intermediate outcome between these contrasting scenarios.
We want to develop market-based mechanisms to achieve a middle-ground between these opposing outcomes.

Price Public Goods to Match Supply and Demand

Everyone receives their most preferred bundle of goods under the set prices
The classical fisher market model

• Set budget constraints for agents, capacity constraints for resources
• Find the equilibrium price set, under which each agent buys the optimal bundle of goods.
• Each agent’s budget is fully used and each good with positive price is sold out.
Agents maximize their utilities subject to budget constraints

\[ u_{i1} > u_{i2} > u_{i3} \]

\[ \begin{align*}
  u_i x_i &= u_{i1} x_{i1} + u_{i2} x_{i2} + u_{i3} x_{i3} \\
  w_i &\geq 0
\end{align*} \]

\[ \text{Individual Optimization Problem:} \]

\[ \max_{x_i} \sum_{j} u_{ij} x_{ij} \]

\[ \text{s.t.} \quad p^T x_i \leq w_i \]

\[ x_i \geq 0 \]

\[ M = \text{Total Number of Goods} \]
Classical Fisher Markets provide a framework to derive prices through a centralized optimization problem.

Social Optimization Problem:

\[
\begin{align*}
\max_{\mathbf{x}_i, \forall i \in [N]} & \quad \sum_i w_i \log \left( \sum_j u_{ij} x_{ij} \right) \\
\text{s.t.} & \quad \sum_i x_{ij} = \bar{s}_j, \forall j \in [M] \\
\end{align*}
\]

Budget Weighted Log Utility

Capacity Constraints

\[ x_{ij} \geq 0, \forall i, j \]

\[ p_j : \text{Price of Good } j = \text{Dual Variable of Constraint } j \]

- \( u_{ij} \) : Preference of Agent \( i \) for one unit of good \( j \)
- \( x_{ij} \) : Quantity of good \( j \) purchased by person \( i \)
- \( p_j \) : Price of Good \( j \)
- \( w_i \) : Budget of Agent \( i \)
- \( \bar{s}_j \) : Capacity of Good \( j \)
The optimality conditions of the social and individual optimization problems are equivalent

**Individual Optimization Problem:**

\[
\max_{\mathbf{x}_i} \sum_j u_{ij} x_{ij} \\
\text{s.t.} \quad \mathbf{p}^T \mathbf{x}_i \leq w_i \\
\mathbf{x}_i \geq 0
\]

**Social Optimization Problem:**

\[
\max_{\mathbf{x}_i, \forall i \in [N]} \sum_i w_i \log \left( \sum_j u_{ij} x_{ij} \right) \\
\text{s.t.} \quad \sum_i x_{ij} = \bar{s}_j, \forall j \in [M] \\
\mathbf{x}_{ij} \geq 0, \forall i, j
\]

\( p_j \) : Price of Good \( j \) = Dual Variable of Constraint \( j \)
However, Fisher markets do not account for additional constraints, e.g., **knapsack constraints**, that commonly arise in public goods allocation problems.

On a given day, I would like to go to one park, one library and one coffee shop.
A potential allocation in Fisher markets may be...

Set of All Parks, Libraries and Coffee Shops in a Neighborhood
A potential allocation in Fisher markets may be...

Set of All Parks, Libraries and Coffee Shops in a Neighborhood

3 coffee shops
Fisher fails

What’s next?
We extend the Fisher market framework to account for additional linear constraints.

Existing generalizations of Fisher markets are limited to spending constraints of buyers and earning constraints of sellers.
Application

Supply side
  • Purchasing limits
  • E.g., House, car plate

Demand side
  • Course selection, covid-19 public resource allocation
Fisher markets with additional linear constraints have different properties from classical Fisher markets.

1. Market Equilibrium may not exist

2. Market Equilibrium may not be unique

3. People do not purchase goods with maximum bang-per-buck

Individual Optimization Problem:

\[
\begin{align*}
\text{max} & \quad \sum_{j} u_{ij} x_{ij} \\
\text{s.t.} & \quad p^{T} x_{i} \leq w_{i} \\
& \quad A_{t}^{(i)} x_{i} \leq b_{it}, \forall t \in T_{i} \\
& \quad x_{i} \geq 0
\end{align*}
\]
We show that under mild conditions the equilibrium exists and characterize the optimal solution of IOP.

Individual Optimization Problem:

\[
\text{IOP} \\
\max_{\mathbf{x}_i} \sum_j u_{ij} x_{ij} \\
\text{s.t. } p^T \mathbf{x}_i \leq w_i \\
A^{(i)}_t x_i \leq b_{it}, \forall t \in T_i \\
x_i \geq 0
\]

Theorem 1. People purchase goods in the descending order of their virtual products’ bang-per-buck ratios.

Theorem 2. Market Equilibrium may not be Unique, and even not convex!
Definition 3. (Virtual Product). A virtual product is characterized by its two endpoints $A = (u_{ij1}, p_{j1})$ and $B = (u_{ij2}, p_{j2})$ with a slope $\theta_{j1,j2} = \frac{p_{j2} - p_{j1}}{u_{ij2} - u_{ij1}}$. Then its bang-per-buck $= \frac{1}{\theta_{j1,j2}} = \frac{u_{ij2} - u_{ij1}}{p_{j2} - p_{j1}}$.

Fig. 2. The enclosed region represents the convex hull corresponding to the solution set $S_t$. The vertices on the lower frontier (in bold) correspond to the goods and the segments correspond to virtual products. The figure on the right shows that any optimal solution must lie on the lower frontier of the convex hull, as indicated by the point $C$. 
Theorem 2. Given a price vector $p \in \mathbb{R}_\geq^m$, agent $i$ can obtain an optimal solution $x_i^* \in \mathbb{R}^m$ of IOP by mixing all virtual products from different types and spending their budget in the descending order of virtual products’ bang-per-buck. Furthermore, each agent $i$ can purchase at most one unit of each virtual product.

Note that when two virtual products have the same slope ties can be broken arbitrarily. Further, an immediate corollary follows, which answers the question of how many different goods an agent will purchase in each type.

Corollary 1. For any agent $i$, there exists an optimal solution $x_i^* \in \mathbb{R}^m$, such that $i$ purchases two different goods in at most one resource type. For all other resource types, agent $i$ buys at most one good.
We gave an example where the equilibrium price set is a curve in the 3-dimension space, which is not convex intuitively.

Proof. We consider a market with 4 agents and 4 products, with one knapsack constraint for goods 1-3 (and so we have a constraint $x_{i1} + x_{i2} + x_{i3} \leq 1$ for all $i$). Furthermore, since good 4 is not tied to any additional linear constraints, agents can purchase any amount of good 4 that is affordable. Next we consider the utility and budget values for each of the agents as well as the price and capacities for each of the goods as specified in Table A.4.

<table>
<thead>
<tr>
<th>Utility</th>
<th>Good 1</th>
<th>Good 2</th>
<th>Good 3</th>
<th>Good 4</th>
<th>Budget</th>
</tr>
</thead>
<tbody>
<tr>
<td>Buyer 1</td>
<td>2</td>
<td>0.0001</td>
<td>4</td>
<td>0.0001</td>
<td>2</td>
</tr>
<tr>
<td>Buyer 2</td>
<td>1</td>
<td>2</td>
<td>0.0001</td>
<td>0.0001</td>
<td>1.5</td>
</tr>
<tr>
<td>Buyer 3</td>
<td>0.0001</td>
<td>3</td>
<td>4</td>
<td>0.0001</td>
<td>2.5</td>
</tr>
<tr>
<td>Buyer 4</td>
<td>0.0001</td>
<td>0.0001</td>
<td>0.0001</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Supply</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td>1</td>
<td></td>
</tr>
</tbody>
</table>

| Price | $p_1 = 2 + \frac{2\eta - 1}{12\eta^2 + 1}$ | $p_2 = 2 - \frac{4\eta}{12\eta^2 + 1}$ | $p_3 = 2 + \frac{2\eta + 1}{12\eta^2 + 1}$ | $p_4 = 1$ |

Table A.4: Utilities and budgets of buyers as well as prices and capacities of goods in a four buyer, four good market to establish that the equilibrium price set may be non-convex.

We will now show that for all $\eta \in [-\frac{1}{24}, 0]$ that $(p_1, p_2, p_3, p_4)$ is an equilibrium price set to establish non-uniqueness and then establish this set is non-convex.
Can the Fisher Market social optimization problem with additional constraints be used to set equilibrium prices?

Individual Optimization Problem:  
\[
\text{IOP} \quad \max_{x_i} \sum_j u_{ij} x_{ij} \\
\text{s.t.} \quad p^T x_i \leq w_i \\
\quad \quad \quad \quad A^{(i)}_t x_i \leq b_{it}, \forall t \in T_i \\
\quad \quad \quad \quad x_i \geq 0
\]

Social Optimization Problem:  
\[
\text{SOP-I} \quad \max_{x_{ij}, \forall i \in [N]} \sum_i w_i \log \left( \sum_j u_{ij} x_{ij} \right) \\
\text{s.t.} \quad \sum_i x_{ij} = s_j, \forall j \in [M] \\
\quad \quad \quad \quad A^{(i)}_t x_i \leq b_{it}, \forall t \in T_i, \forall i \in [N] \\
\quad \quad \quad \quad x_{ij} \geq 0, \forall i, j
\]
**Theorem 4:** The dual variables of the capacity constraint of SOP-I may not be an equilibrium price.

**Individual Optimization Problem:**

\[
\text{IOP} \\
\max_{x_i} \sum_j u_{ij} x_{ij} \\
\text{s.t. } p^T x_i \leq w_i \\
A^{(i)}_t x_i \leq b_{it}, \forall t \in T_i \\
x_i \geq 0
\]

**Social Optimization Problem:**

\[
\text{SOP-I} \\
\max_{x_i, \forall i \in [N]} \sum_i w_i \log \left( \sum_j u_{ij} x_{ij} \right) \\
\text{s.t. } \sum_i x_{ij} = s_j, \forall j \in [M] \\
A^{(i)}_t x_i \leq b_{it}, \forall t \in T_i, \forall i \in [N] \\
x_{ij} \geq 0, \forall i, j
\]

Remark: It is an equilibrium if the constraints are homogeneous.
A robust approach to account for physical constraints in Fisher Markets can be achieved through Budget Perturbations

\[
\begin{align*}
\text{SOP-I} \\
\max_{x_i, \forall i \in [N]} & \sum_i w_i \log \left( \sum_j u_{ij} x_{ij} \right) \\
\text{s.t.} & \sum_i x_{ij} = \bar{s}_j, \forall j \in [M] \\
& A_{x}^{(i)} x_i \leq b_{it}, \forall t \in T_i, \forall i \in [N] \\
& x_{ij} \geq 0, \forall i, j
\end{align*}
\]
A robust approach to account for physical constraints in Fisher Markets can be achieved through Budget Perturbations.

**SOP-I**

\[
\max_{x_i, \forall i \in [N]} \sum_i w_i \log \left( \sum_j u_{ij} x_{ij} \right)
\]

s.t. \[ \sum_i x_{ij} = \bar{s}_j, \forall j \in [M] \]

\[ A_t^{(i)} x_i \leq b_{it}, \forall t \in T_i, \forall i \in [N] \]

\[ x_{ij} \geq 0, \forall i, j \]

**BP-SOP**

\[
\max_{x_i} \sum_i (w_i + \lambda_i) \log \left( \sum_j u_{ij} x_{ij} \right)
\]

s.t. \[ \sum_i x_{ij} = \bar{s}_j, \forall j \in [M] \]

\[ A_t^{(i)} x_i \leq b_{it}, \forall t \in T_i, \forall i \in [N] \]

\[ x_{ij} \geq 0, \forall i, j \]
Budget Perturbations allow more constrained agents, e.g., medical workers during a pandemic to have “higher priority” to get their goods.
Theorem 5: The dual variables of the capacity constraint of BP-SOP are the market equilibrium price iff \( \lambda_i = \sum_t r_{it} b_{it} \)

**Individual Optimization Problem:**

**IOP**

\[
\begin{align*}
\text{max}_{\mathbf{x}_i} & \quad \sum_j u_{ij} x_{ij} \\
\text{s.t.} & \quad p^T \mathbf{x}_i \leq w_i \\
& \quad A^{(i)}_t \mathbf{x}_i \leq b_{it}, \forall t \in T_i \\
& \quad \mathbf{x}_i \geq 0
\end{align*}
\]

\( p_j \): Price of Good \( j \) = Dual Variable of Constraint \( j \)

**Social Optimization Problem:**

**BP-SOP**

\[
\begin{align*}
\text{max}_{\mathbf{x}_i} & \quad \sum_i (w_i + \lambda_i) \log \left( \sum_j u_{ij} x_{ij} \right) \\
\text{s.t.} & \quad \sum_i x_{ij} = s_j, \forall j \in [M] \\
& \quad A^{(i)}_t \mathbf{x}_i \leq b_{it}, \forall t \in T_i, \forall i \in [N] \\
& \quad x_{ij} \geq 0, \forall i, j
\end{align*}
\]
To determine the perturbation constants we use a fixed-point iterative procedure.

Algorithm 1: Fixed Point Scheme

\[\text{Input} : \text{Tolerance } \epsilon, \text{ Function } G(\cdot) \text{ to calculate dual variables}\]
\[\text{Output: Budget Perturbation Parameters } \lambda\]
\[\lambda \leftarrow 0 ;\]
\[R \leftarrow G(\lambda) ;\]
\[q_i \leftarrow \sum_{t=1}^{i} r_t b_t, \forall i ;\]
\[\text{while } \|\lambda - q\|_2 > \epsilon \text{ do}\]
\[\lambda_i \leftarrow \sum_{t=1}^{i} r_t b_t, \forall i ;\]
\[R \leftarrow G(\lambda) ;\]
\[q_i \leftarrow \sum_{t=1}^{i} r_t b_t, \forall i ;\]
\[\text{end}\]
Methods to compute market equilibrium

Convex optimization
Tatonnement process
Primal-dual
Auction based approach
...

Centralized vs. distributed
Alternating Direction Methods (ADMs)

A new class of distributed tatonnement algorithms

Alternating Minimization Algorithm (AMA)
- Agents distributed solve their individual optimization problems at each iteration
- The step sizes of the price updates based on utilities

Alternating Direction Method of Multipliers (ADMM) Algorithm
- The step size is independent of utilities

Both algorithms $O(1/k)$ convergence rate for fisher market with homogeneous linear constraints
We design a market mechanism that derives market clearing prices while supporting additional constraints.

Set Prices that Clear the Market, i.e., all goods are sold, and all budgets are used.

Maximize a Social Objective while each person obtains their most preferred bundle of goods.
Thank you!