The Economics of Professional Journal Pricing

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The problems of excessive inflation and price discrimination in journal pricing continue to plague libraries. In analyzing the causes of the current crisis, the authors review and evaluate previous contributions to the literature on journal pricing with particular emphasis on the three types of price discrimination practiced by journal publishers. The authors suggest that the monopoly power of commercial publishers, combined with a third-party payment system, are at the heart of the problem. They suggest solutions that involve providing appropriate incentives to journal users, adoption of more equitable pricing systems, and employing the potential monopoly purchasing power of library associations to lower prices.

After more than two decades of extraordinary inflation, professional journal prices continue to increase at rates several times as high as the American economy’s overall inflation rate and far higher than the rate of cost increase in the journal publishing industry. Academic economists, marketing researchers, librarians, and paid economic consultants have undertaken economic analyses of journal markets in order to explain the high rates of price increase and the great extent of price discrimination against libraries and United States buyers in general. Some of the researchers subsequently recommended solutions to library administrators, and many of their suggestions are sound and practical. However, a number of the studies are fraught with analytical errors and recommendations that were either economically illogical, impractical, or both. The authors intend to summarize the literature in this area, correct the analysis, and provide practical policy recommendations for library administrators based on what the application of economic principles really tells us about the journal market situation.

The Natural Monopoly Misconception

Several researchers have analyzed the academic journal industry and labeled it a natural monopoly. Despite the researchers’ claims, the academic journal industry is not a natural monopoly. A natural monopoly is an industry in which the cost structure is such that the average pro-

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duction cost per unit of the product continues to fall throughout as the firm's production increases (see figure 1). Therefore, one firm can produce the entire industry output more cheaply than having a group of competing firms. Because large firms usually have production cost advantages over small ones, it becomes difficult for small firms to compete and for new firms to enter the industry successfully.

The type of price discrimination practiced by journal publishers is perfectly legal because it is not aimed at putting anyone out of business or disadvantaging a particular group of buyer-resellers through a limited discounting program.

Public utilities, such as electric, natural gas, and local telephone firms, are the classic examples of natural monopolies. The existence of natural monopolies is the justification for federal, state, and local governments granting public utilities franchised monopolies on the grounds that having more than one local electric, water, telephone, or natural gas supplier would be uneconomical. Competition in these industries would require duplication of transport and connection facilities throughout the service area and would be unnecessarily costly. Hence, state and local governments grant monopoly franchises to utilities and then regulate their prices because there is no competition to keep the prices low.

Certainly there are economies of scale that cause the average cost of journal production to fall as output increases, mostly because of the high initial setup (i.e., first copy) or fixed costs. That is also true for the automobile industry, all of the other publishing industries, or any manufacturing industry for that matter. Typically, cost per unit will fall as the firm expands, but only up to a particular output level. Beyond that production level, per unit cost does not continue to fall and may eventually even increase. There is not a continuously declining cost curve that mandates that there can be only one efficient