

## Principle of First Copy Costs

(aka Economies of Scale)

The principle of first copy costs states that the cost of producing the first copy of something is much higher than the cost of the second or any subsequent copy. To illustrate, let's say you are a newspaper publisher and your daily cost of operation (cost of paying all your reporters, editors, salespeople, office staff, rent on building, depreciation on all your equipment, supplies, phones, other utilities, etc.) is \$6,000. This is your fixed cost. If you print only one copy of the newspaper, you will have to sell it for \$6,000 just to cover your fixed costs. If you print two copies, you will have to sell each for \$3,000; your average fixed cost per copy is cut in half. If you print 60,000 copies, your average fixed cost per copy is only 10 cents. Thus, your average fixed costs keep going down as these costs are spread over more and more copies.

When you print more copies, however, the costs of paper, ink, and distribution increase; these are your variable costs, because they vary according to the number of copies you print. The more copies you print, the more paper and ink you will need, although the price you pay for a roll of paper or a gallon of ink will go down because you can buy these materials in bulk and get big discounts. While your total cost for ink and paper will go up when printing more copies, your *average* variable cost for these will go down. This is known as economies of scale. The bigger the scale of your business, the more likely your costs will go down, either through your ability to demand greater discounts or because you are able to operate more efficiently beyond a certain point.

The more copies you print, the more your distribution costs will go up—both in total and on average. To illustrate this point, imagine that you publish only 1,000 copies of your newspaper. You could hire 10 youngsters to deliver 100 papers each after school and pay them a nickel for each paper delivered. Thus your average distribution cost is 5 cents per newspaper. But let's say you want to publish 50,000 newspapers. You would need to hire 500 youngsters,

and this would require you to develop a whole new layer of administration to recruit, train, and keep track of all these paper carriers. You would have to buy some trucks and hire drivers to get the newspapers out to these 500 carriers quickly every afternoon. You would also have to hire some bookkeepers to keep track of all the subscriptions and billing. So the average variable cost might increase from 5 cents to 15 cents per newspaper as you go from 1,000 to 50,000 in circulation.

Media companies, like any business, want to keep their expenses down, so they find the point at which the combination of their average fixed costs and their average variable costs are lowest. Beyond this point, distributing more copies only serves to increase unit costs and thus reduce profit. Newspaper, magazine, book, and recording companies each seek the point where their average total costs (the sum of average fixed costs plus average variable costs) are lowest.

On this principle of first copy costs, broadcast television and radio are different from the other media. They have no variable costs, only fixed costs. For example, with broadcast television there is no cost to the station for adding an additional viewer to the audience. Viewers pay for their own television receivers, and they pay for the electricity to run them. The station has no distribution costs other than the electricity for the broadcast signal, and the power used to broadcast a station's signal is the same whether 100 or 100,000 sets are tuned in. It is fixed. With no variable costs and with a very high first copy fixed cost, broadcast television stations keep dropping their average total costs with each additional audience member added. For this reason, the broadcast media (both radio and television) are strongly motivated, more than any other medium, to increase the size of their audiences.

### ***Direct and Indirect Costs***

Consumers of the mass media support the industry by paying both direct and indirect costs. When you write a check to your cable television provider for your monthly bill, you are paying money directly to a media company. That is a direct cost. Other examples of direct costs include paying admission to a movie or buying a magazine, book, recording, or computer software. When you buy hardware (TV set, VCR, computer, etc.) that is required to receive media messages, you are also contributing to direct costs.

In contrast, you also support the media indirectly. Let's say you spend \$5.00 for lunch at McDonald's. Some of that money (let's say \$1.00) will find its way into McDonald's advertising budget and is sent on to a television network. That \$1.00 of your lunch payment is an example of your indirect support of the media. The payment originated with you, but it did not go directly from you to a media company. Had you not bought lunch at McDon-

ald's, that \$1.00 would not have gone to the television network. Every time you buy an advertised product or service you are indirectly supporting the media.

The media of books, films, recordings, and computers are supported almost entirely by direct costs to the consumer. There are a few examples of ads being stuck in books or displayed before films or in computer programs, but the revenue from these ads is minor compared to direct costs. With magazines, newspapers, and now cable TV, the costs are split between direct (subscription or newsstand selling price) and indirect (advertising). With broadcast television and radio, there is no direct cost for exposure to a program, but there is a high cost for purchasing the means to receive a program, in addition to indirect costs in the guise of advertising.

The balance between direct and indirect support is shifting from direct to indirect payment. In the 1930s, 72% of media support was paid *directly* by consumers; by 1958, there was a 50%-50% split; now, about 75% is paid *indirectly* by consumers.