by Robert G. Picard

Rate Setting and Competition in Newspaper Advertising

Dearth of information on ad rates leaves newspapers at dangerous disadvantage.

Basic to the understanding of newspaper finances is an understanding of the role advertising plays in newspaper economics and how newspapers compete with each other and other media for advertising dollars.

The impact of advertising on newspaper financing, the ways newspapers determine their advertising rates, and how competition for advertising dollars affects the rates of competing newspapers have been virtually ignored and thus have placed newspaper managers at a severe disadvantage when dealing with advertiser representatives.

Despite the importance of advertising to the industry, the field has received little attention from industry organizations, and journalism and advertising publications and journalism schools and researchers have all but ignored the subject. In fact, during the last decade fewer than a half dozen articles seriously exploring advertising rates or reporting their impact on newspaper economics have appeared.

Even one of the few really excellent annual studies of newspaper finances, featuring composite medium and large daily newspapers, was ended by the industry publication *Editor and Publisher* in the early 1970s, leaving a gap in information that has gone unfilled. The American Newspaper Publishers Association has been active in seeking newspaper advertising data, but its information is not available in a widely distributed form.

These difficulties point out the need for further research and understanding about advertising from the journalist's standpoint, if individuals in the newspaper industry are to comprehend the importance of advertising, advertisers and the

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advertising departments of their enterprises.

Ad Expenditures

Expenditures for all commercial advertising have risen steadily in the past 20 years from $12 billion in 1960 to $55 billion in 1980, an increase of almost 458%. Expenditures for commercial newspaper advertising rose from $3.7 billion to $15.6 billion during the same period, an increase of slightly below 425%—not quite keeping pace with the total but still a healthy increase (See Table 1).

The percentage of total advertising dollars spent on newspaper advertising decreased slightly between 1960 and 1980, however, dropping from 30.7% to 28.5%, according to industry statistics.

"Newspapers have been by far the major outlet for advertising," reports an observer, who notes that newspapers have continued to remain a major advertising medium despite the decline in the total number of daily newspapers since World War II.[1]

Expenditures for local advertising have always exceeded national advertising in newspapers, but in the past 20 years the trend has been for national advertising to decline. In 1960, national advertising dollars accounted for 21% of the total commercial newspaper advertising expenditures, but by 1980 figure had shrunk to to 15%.

TABLE 1. Estimated Annual U.S. Advertising Expenditures 1960 to 1980 (in billions)

YEAR	Total Ad Expenditures	Total Newspaper Ad Expenditures	National Advertising	Local Advertising
1960	12.0	3.7	.78	2.9
1961	11.9	3.6	.74	2.9
1962	12.4	3.7	.73	2.9
1963	13.1	3.8	.70	3.1
1964	14.2	4.1	.73	3.4
1965	15.3	4.4	.78	3.6
1966	16.6	4.9	.78	4.0
1967	16.9	4.9	.85	4.1
1968	18.1	5.2	.89	4.3
1969	19.4	5.7	.94	4.8
1970	19.6	5.7	.89	4.8
1971	20.7	6.2	.99	5.2
1972	23.3	7.0	1.1	5.9
1973	25.1	7.6	1.1	6.5
1974	26.8	8.0	1.2	6.8
1975	28.2	8.4	1.2	7.2
1976	33.7	9.9	1.5	8.4
1977	37.9	11.1	1.7	9.5
1978	43.8	12.7	1.8	10.9
1979	49.7	14.6	2.1	13.5
1980*	54.8	15.6	2.3	13.3

Source: *Advertising Age*, prepared by McCann-Erickson, Inc.
*1980 figures provided by ANPA.

These figures do not necessarily mean that interest in advertising in newspapers had declined among national manufacturers and retailers. It has been noted that of the expenditures for local newspaper advertising, cooperative advertising programs between local retailers and manufacturers play a major role.[2] Such programs now bring more than $3 billion to the newspaper industry annually.[3] Because of this development, it may well be appropriate to consider the possibility that some of the funds spent by national advertisers have been shifted to the local advertisers. Of course, television and magazine advertising have also received increasing shares of the budgets of national advertisers.

Of total newspaper revenue, local advertising contributed more than half by the mid 1970s and national advertising accounted for less than 5%.

A study of newspaper budgets during the last three decades has shown that newspapers have grown more dependent on advertisers for revenue. Using a composite newspaper constructed for their study, with data from *Editor and Publisher* and confidential sources, the researchers found advertising to be the most important factor in newspaper financing. "In 1947, advertising contributed two-thirds of the revenue for our composite daily, but by 1965 the figure was nearer three-fourths," the researchers said.[4]

Many journalists lose sight of the fact that advertising not only contributes the majority of income to newspapers, but that it also accounts for the majority of the substance, or content, of the newspaper entity itself. ". . .Newspaper economics dictate that, to survive and make a profit, they [newspapers] must publish a paper that has a ratio of about 65 percent advertising to 35 percent news. Papers which substantially violate this ratio invite financial difficulty," says a newspaper publishing executive.[5]

This reality also results in advertisers "subsidizing" news—advertising revenue pays a disproportionate amount of the costs of publishing a newspaper, not just for the space and profit on the space used for advertising. Advertising contributes three-fourths of the revenue to papers but accounts for about two-thirds of space occupied within papers.

The importance of advertising revenue to newspapers makes advertiser dollars the mother's milk of journalism today, and no change in the situation appears likely in the future.

Newspaper and advertising economists predict that advertisers will continue to be attracted to newspapers as a primary outlet for commercial information. For the past several years increases in total newspaper advertising revenues have held steady at around 12% per annum and this figure is expected to hold true in 1981. A 16.2% increase in national advertising has been projected for the current year, with advertising revenue for newspapers expected to reach 27.4 billion dollars.[6]

Jon Udell, an economist at the University of Wisconsin who has devoted much of his research to newspapers, predicts they will remain important, experiencing increased circulation and advertising revenue because demand for consumer goods and increasing production capabilities will result in manufacturers increasing advertising expenditures in the decades to come. Newspapers, he says, will continue to attract a large share of those expenditures.[7]

How Rates Are Set

In marketing space to advertisers, newspaper managers must plan pricing strategies and set rates in much the same manner as producers of goods that will be marketed to the general public. Since advertising accounts for nearly three-quarters of newspaper income, one would assume that the pricing of advertising space would be of considerable importance to newspaper publishers and owners. But the opposite appears true, based on the little consideration it receives in industry publications and newspaper management materials.

Pricing strategies and rate setting are apparently not viewed with the same importance as in business and marketing circles, where admittedly—despite the acknowledged importance and study given to pricing policy—"most companies do not handle pricing well."[8]

In the newspaper industry, where the overt lack of interest in price strategy appears epidemic, pricing appears to be handled even worse. One observer noted charitably in 1956, "...rate setting is not as much an integral part of the over-all marketing strategy as it might be."[9] His admonition has not been heeded in the quarter century since that time, and the need for attention to be paid to rate setting has increased tremendously as newspapers have become more dependent on advertising revenue and competition for advertising dollars has grown.

The lack of concern about rates within the industry is reflected in, and perhaps is promoted by, the lack of concern about the issue in major newspaper management texts.

Leslie McClure's 1950 text, *Newspaper Advertising and Promotion,* widely regarded as a major work on the business side of newspaper operations, spends little time on the subject of rate setting, merely noting the influences on rates and providing an argument for differential rates.

Frank Rucker and Herbert Williams also virtually ignore the issue in their widely used and enduring text on newspaper operations, *Newspaper Organization and Management.* Although they acknowledge the importance of advertising and suggest ways to increase advertising sales, they do little more than McClure in the way of helping publishers or would-be publishers learn how to establish and maintain rates for advertising.

Economist Jon Udell's 1978 work on newspaper economics, *The Economics of the American Newspaper,* which was produced with the financial support of the American Newspaper Publishers Association,

was a long awaited and needed work on the economic side of publishing. Despite its importance it includes no significant discussion of rate structure or how rates should be set.

Udell, in fact, pays much more attention to circulation prices—as did McClure and Rucker and Williams—even though circulation revenue has much less impact on newspaper economics than advertising revenue, although it must be acknowledged that the size of the circulation does have an influence on advertising sales.

Publishers seeking substantive information to help them make rate-setting decisions are also left without help by such organizations as the Newspaper Advertising Bureau, American Newspaper Publishers Association and National Newspaper Publishers Association, which do not have publications on the subject and have not published journal articles that can be helpful to newspaper managers.

Because of the lack of information and studies on setting advertising rates, publishers must set and adjust their rates—apparently using intuition, adapting pricing strategies used by other industries, or blindly stumbling along with a let's-try-it-and-see strategy. In the nation's largest newspapers and newspaper chains, marketing and pricing strategies are gaining some consideration, however, and some firms now have departments which are beginning to analyze rates and make comparisons of rates in various markets among their other duties.

It is clear that there are numerous influences on the pricing of advertising space. John McKinney has observed that "Advertising rates are generally determined by considering the paper's total circulation, its expenses, and the rates charged by competing publications, if any exist."

Rucker and Williams concur that the accustomed standard has generally been circulation, but they add, "...the business public is beginning to realize that something more than paid subscribers determines the value of a newspaper as an advertising medium."[10]

The prestige of a paper, the quality of its circulation in terms of potential results for advertisers, the locations of readers, the service rendered by the paper and the local economy also plays a role in the setting of rates.

For the most part, strategies used in setting rates in the newspaper industry appear to take the forms of target-profit pricing and competition-oriented pricing or some combined variations of the two. Occasionally a demand-oriented policy may be selected, but the two dominant policies remain target-profit and competition-oriented pricing.

Target-profit pricing, of course, is the strategy of determining the price that will give a specific rate of return on total costs, based on estimated volumes of business. In competition-oriented pricing, prices are set with the greatest emphasis placed on competitors' prices, often after a review of what the going rate is for the product. Demand-oriented policy sets prices based on the perceptions and demand intensity of consumers.

In their basic strategies, newspapers have traditionally set different classes of advertisers. National advertisers usually pay higher rates than local advertisers, an occurrence not looked upon favorably by national advertisers. Newspapers also set different rates based on services rendered to the advertiser, placement and the amount of advertising space purchased during a year.

James Ferguson studied the rate differential between national and retail advertising in a study sponsored by the Ford Foundation. He found no evidence to suggest that the differential could be laid upon higher costs to the paper for national advertising. The main factor, he said, is the value of retail advertising to the paper.

"Newspapers have held down retail rates relative to national rates in an attempt to attract retail advertising and thereby increase circulation and attract still more advertising," Ferguson wrote. "In order to maximize profits, the interrelationships among circulation, retail advertising, and national advertising make it necessary to charge retailers less than national advertisers, despite the more inelastic demand of the retailers."[11]

Compared with the prices of products, the rates of advertising space have been unusually rigid over time, perhaps reflecting the view promulgated by McClure, that to operate profitably and ". . .hold the confidence of advertisers," newspapers must keep fairly rigid rate structures.[12]

"Publishers of individual newspapers and their business staffs have been forced to make rate decisions based almost entirely on their own analyses, however good or poor these may be," says S. Watson Dunn, an advertising professor who has devoted considerable attention to newspapers. "In general they have played it safe by keeping their rate structure fairly rigid in spite of ups and downs in the business cycle and changes in operating costs."[13]

Despite the rather uninformed approaches to pricing policies, newspapers have done well financially, annually yielding after-tax profits of about 10%, well above the average for other industries. Should the industry begin paying more attention to pricing strategy, that figure might be increased significantly.

"A newspaper, with its heavy fixed costs, can achieve a tremendous increase in profits through even a slight increase in ad volume," reminds Jon Udell.[14] And if the increase in ad volume brings a concurrent increase in revenue as a result of new pricing policies, the investment of time and effort in researching and gaining a better understanding of pricing strategy implications will be well worth the effort.

Competition and Ad Rates

How competition for advertising dollars affects advertising rates must be the major consideration in any serious discussion of newspaper advertising issues.

In its broadest sense, newspaper competition for advertising involves all media, including broadcast media, direct mail publications, posters, coupons and vehicle-borne ads. But for the purposes of this article, discussion of competition will be limited to the battle for advertising dollars between units of

the newspaper medium, mainly daily papers, but also including weekly and shopper publications serving the same general marketing area.

Circulation, as was shown earlier, is a prime determinant of the attraction of a particular newspaper to an advertiser. But advertisements in a newspaper also play a role in increasing circulation because newspaper readers are attracted to the information provided by advertising.

The newspaper with the largest circulation in a given marketing area has advantages which enable it to gain ground in both circulation and advertising, at the expense of papers competing with lower circulation and advertising revenue, forcing them into less advantageous situations, says Lars Furhoff, a researcher in newspaper economics. And publishing a large amount of advertising is one of those advantages.

"That newspaper which has achieved the highest density of distribution also enjoys the largest market potential, i.e. the largest number of readers within the territory in which advertisers are interested," Furhoff contends. "This attracts an increased flow of advertising and thus larger resources to support the competitive strategems and low copy prices by which new readers and further advertising income will be gained."[15]

The leading newspaper also has the advantage of determining the standards of advertising, editorial, production and distribution quality expected by advertisers and readers. It therefore puts increased pressure on competing papers to live up to these standards. As those papers attempt to meet the demands, their economic difficulties increase, trapping them into a vicious circle or "circulation spiral" which aggravates the problems of selling advertising space and the rates which can be charged for that space.

Furhoff's contentions were later born out by Karl Erik Gustafsson, who showed that in Scandinavia only a household penetration of at least 50% made a competing newspaper indispensable to advertisers in a given market.[16] More recently, a review of Furhoff's and Gustafsson's work argued that theories of oligopoly help explain their observations and that in competitive situations the only way for a newspaper that does not have market leadership to survive is by pursuing policies that differentiate the product from the leading newspaper in terms of content and readership.[17]

In this symbiotic relationship between circulation and advertising are the makings of a vigorous battle for advertising dollars when more than one paper competes for the available advertising. When this type of competitive situation exists, the setting of advertising rates plays an important role in the advertising marketing process.

"In a highly competitive field, newspapers operate on narrower magins of profit and tend to pay lower salaries and trim expenses wherever possible," says McClure. "As a result, they frequently offer their customers relatively low rates to prevent loss of lineage to competitors and to take business away from those competitors."

Udell concurs that low-rate policy attracts business away from competitors and that the setting of rates determines whether lineage is large or small. "...A low-rate paper will sell more advertising lineage to an advertiser than a high-rate paper because of the relatively fixed ratio of advertising expenditures to retail sales," he says.

The realities of publishing make it more likely that the largest paper in a community will be able to offer the lowest advertising rates, attracting more advertisers than it would if it had a higher rate, thus making up for any revenue that was lost when lowering the rates. The low-rate policy doesn't necessarily gain a paper more advertising revenue, but it can harm the competitor and thus may in the end have the effect of reducing the competition for advertising dollars.

This effect is shown starkly in Salem, Ore., where over the past few years the Gannett Corp. sharply reduced advertising rates for its *Oregon Statesman* and *Capitol* Journal and actively pursued strategies to attract advertisers away from a successful weekly newspaper. As a result of the ensuing advertising war, the weekly paper was forced out of business and the Gannett papers were able to raise rates—increasing revenue—without fear that advertisers would move their business to the weekly newspaper.[18]

Jon Udell has observed that "The largest-circulation newspaper in a given market generally gets a disproportionately large amount of newspaper advertising revenue in that market. A competitive second paper, while it may be behind only slightly in circulation, is often a more distant second in advertising revenue."

Such a situation is well illustrated by the newspaper situation in Washington, D.C., where the second paper, the Washington *Star,* recently ceased operation for financial reasons.

The Washington Post had a daily circulation of 578,831 and the *Star* a circulation of 342,760.[19] While the *Star* accounted for nearly a 40% share of the daily circulation, it received only a 24% share of the advertising lineage.[20]

Many of the newspapers competing in the few remaining multi-newspapers markets are also facing similar problems. A recent study of these markets named newspapers in Detroit, Buffalo and Denver markets as facing extinction soon, and warned about difficulties facing the Philadelphia *Bulletin,* Cleveland *Post,* Los Angeles *Herald-Examiner* and other major newspapers.[21]

Competitive situations generally result in papers pursuing low-rate competition-oriented pricing policies, sometimes artificially low, to carry out marketing strategies to dominate the advertising market. But the low-rate strategy generally covers only retail advertisers. Firms wishing to place national advertising are still saddled with higher rates because of the common rate differential between national and retail advertising rates.

The situation obviously aggravates national advertisers, but publishers are aware that the demand for space by national advertisers is relatively inelastic and therefore would not be likely to increase as a result of lowering national rates, even in a competitive situation.

A study of weekly newspapers found that competition was not always a cause of lower rates and that the closeness of competition is "modestly related" to higher rates.[22] Since these publishers are apparently not pursuing tough competition-oriented pricing policies to the extent of competitive daily newspapers, and the markets appear to sustain the competing papers, questions are raised about the effects of different pricing policies on competition, advertising revenue and the ability of markets to sustain multiple newspapers. Unfortunately, the literature of journalism today offers no answers to the questions.

Non-competitive situations, of course, place newspapers at an advantage when it comes to rate setting since less attention must be paid to the rate card than in competitive situations. A study of daily newspapers without competitors, a situation that helps create economies of scale, showed that the savings were retained by the paper, not passed on to advertisers. Instead, the study concluded, "Newspaper monopolists charge monopolist prices."[23] Whether the advantage of non-competitive situations could be used to compete more successfully with other media in the market served by such a newspaper has not yet been considered.

Conclusions

A steady, forecasted flow of advertising revenue is crucial to the existence of newspapers in the United States today. Newspapers survive or fail depending upon their fortunes in seeking the patronage of advertisers.

Advertisers, likewise, depend upon the newspaper as the major outlet for their commercial information, and approximately half of all dollars spent for promoting sales of products and services are allocated to newspaper advertising. The purchasing decision has now grown into a specialized process in which a wide variety of factors is carefully weighed to determine where and how to allocate financial resources for advertising. Much effort is being made by advertisers to understand media and the economics of newspapers.

On the newspaper side, however, the procedures for marketing space to advertisers and setting rates for that space are handled in an almost cavalier manner. Newspaper executives make pricing decisions more according to hunches than marketing knowledge or economic theories and research.

Competition between newspapers in the same marketing area for advertising generally lowers the cost per line to the advertiser. In these competitive situations the paper with the smaller circulation is at a distinct disadvantage in terms of gaining advertising and sufficient revenue, unless it serves a special audience or provides wide coverage which may be especially attractive to advertisers.

It appears clear newspaper executives place much less emphasis on understanding advertiser economics, the economics of pricing advertising space and general industry trends than do advertising executives. Advertising topics aren't given much space in journalism periodicals and books, and there is a general lack of discussion about them at industry congresses. Advertising publications, books and meetings often address the topics from the advertisers' standpoint, however, and thus give advertisers an informational edge when dealing with the media.

The economics of the newspaper industry today is forcing more papers to fold or seek financial strength in chain ownership. This need not necessarily be the case—taking the time to understand the economic issues involved can improve marketing and financial positions and help preserve independent and competitive newspapers.

Such understanding can only develop through concerted effort on the part of all connected with newspapering—reporters, editors, publishers and educators.

These areas of research must be pursued and the results conveyed to newspaper personnel to help them cope with competitive situations:

1) The effects of different pricing policies on advertising competition between newspapers, and between newspapers and other media;
2) Should rate schedules be kept rigid at all times?
3) What circulation or advertising share levels are required for newspaper survival in the U.S.?
4) Effects of the rate differentials between national and local advertising;
5) How can smaller competing newspapers survive low rate policies of competitors?

Attention also needs to be directed to producing how-to books or articles on rate setting for newspaper managers, and some attempts should be made to find ways to forecast advertising revenue more efficiently so managers can more accurately plan for the future.

Without increased interest in the relationship between advertising and newspaper finances, the newspaper industry will remain lacking in vital information, and in a less than equal position to that of advertisers. Remaining at this disadvantage can only increase the economic difficulties of newspapers and promote the continued decline of competing and independent newspapers in the United States.

NOTES

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