

A Portfolio Approach to Print Legal Serials Pricing

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This paper reports results from a comprehensive study of print legal serials. Data on law serial prices, holdings, use and costs were collected for the period 1990-2000. Using a portfolio approach to interpret behavior in this market, the evidence suggests that the observed price increases are related to two factors: 1.) Inelastic library demand and 2.) Increased publisher market power due to mergers during the sample period. Changes in law serial use and costs do not appear to have contributed to the price increases.

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The trajectory of periodical prices, including law serials, has been tracked for decades by the American Library Association's Library Materials Price Index Committee (or LMPIC; go to <http://www.ala.org/online/archive/periodicals01.pdf> for the 2001 report). In addition, until 1996, the American Association of Law Librarians specifically tracked law serial prices. These indices can be used to measure changes in serial prices over time, and thus provide a basis for price forecasts. This information is useful for law librarians preparing annual serials budget requests, as well as for those interested in analyzing general trends in publishing markets. For example, according to the ALA's 2001 report, law periodical prices experienced a 75% increase over the period 1991-2000.^{1, 2} For the same period, consumer prices (as measured by the CPI) increased only 26%. A similar pattern is observed in other disciplines, e.g. the same ALA study reports a 165% increase in medical periodical prices over the 1991-2000 period. Of course, the existence of this inflationary pattern is common knowledge among librarians, regardless of discipline. What is perhaps not as well understood are the possible explanations, and the empirical support for these claims. Although the library science literature has devoted a considerable number of pages to these questions over the past decade or so, the attention has been focused primarily on journals published in the areas of science, technology and medicine.³ The same can be said for the small set of economics papers written on this subject.⁴ Thus, although the price trends among law serials resemble those of STM titles, there does not exist any systematic analysis of these trends or the factors determining price changes in the law serials "market."⁵

¹ According to the ALA's report this estimate is based on prices for 273 law periodicals. However, no details are provided regarding the identity of these publications.

² The 1991-2000 period is chosen to correspond to the data considered here in this report.

³ See Tenopir and King (2000, Ch. 13) for a review of this literature.

⁴ See, for example, Bergstrom (2001) and McCabe (2002).

⁵ Svengalis (various years) offers a brief history of the market for legal periodicals and identifies consolidation through merger as a likely explanation for at least some of the observed price inflation.

This study is the first to offer such an analysis. A thorough market analysis requires both a conceptual framework and the appropriate data. The basic analytical framework adopted here was first described in McCabe (2002 AER, 2002 working paper). Although this framework was initially developed to explain behavior in the market for STM journals, my discussions with law librarians suggests that there are many similarities between the two markets, and that many if not all of the concepts can be applied in the legal context. I assume that the market for legal serials consists of all titles available for sale (a “portfolio market”). This assumption reflects the belief that acquisition budgets are broadly defined (and include the eight serials categories defined below). Furthermore, given their budgets, I assume that librarians attempt to maximize the use value of their collections (in practical terms this means that librarians construct rough measures of cost/use for each title, and choose those titles with the best or lowest ratios). With these demand-side assumptions it is possible to generate various predictions regarding publisher pricing behavior. For example, this framework implies that publishers can increase their profits by increasing the size of their portfolios through merger or the introduction of new titles. Evidence that larger publishers charge prices higher than those charged by other smaller companies would be consistent with this hypothesis.

To evaluate the merits of this portfolio approach, it is necessary to collect price and holdings data, as well information about other demand and supply factors, e.g. periodical use patterns and their marginal costs. Ideally, this data should be representative of the sellers and buyers in the market, and span a period of time long enough to measure the impact of important changes in technology and market structure. Unfortunately, these objectives were only partially met. Although, the chosen sample period, 1990-2000, is long enough to permit examination of each of the paper’s objectives ⁶, deficiencies in the available data limit my ability to fully address each objective.

The AALL advisory committee for this project ⁷ and I defined a set of the “480 most important”

⁶ In particular, note that this choice of sample period allows me to assess the impact of (1) recent mergers, e.g. West/Thomson in 1996 and (2) the growing dependence on digital distribution for certain law serial categories, e.g. citators

⁷ The committee included Claire Engel, Nancy Johnson, Craig Lelansky, Bob Oakley, and Kendall Svengalis.

titles, drawn from eight broad categories of commercial, print legal serials – reporters, codes, digest, citators, encyclopedia, looseleaf services, newsletters, and treatises. Although many more legal serials exist it was not practical to collect information on additional titles (given the limited resources of the project and the absence of pre-existing data sources). Price data was obtained primarily from Georgetown University, and in the case of treatises, supplemented by Svengalis' annual price survey. Because Georgetown did not subscribe to all 480 titles, and since their data for codes and digests could not be used, about 370 titles are represented in the price data. Holdings data for all titles during the sample period was collected from approximately 60 libraries; use data was obtained from slightly more than half of these same libraries (for the years 1990 and 2000 only). Although the majority of AALL members are law firm libraries, with the remainder consisting of government, corporate and academic organizations, the largest group of participants in the study are law school libraries, followed by law firms. Since these two types of libraries may behave differently, separate results are reported for the two groups (the numbers for the other types of libraries are too small for any reliable analysis). Finally, with respect to marginal costs, most analyses of this type rely on some proxy measure such as the number of published pages, or volumes. For a variety of reasons (e.g. many of the materials are discarded soon after they are received) these proxy measures could not be compiled in most cases. However, reporter volumes were counted.

The paper is organized as follows. I first describe in greater detail the demand for law serials, and the implications for publisher pricing strategies. I then present the empirical evidence. This includes a series of descriptive statistics based on the price, holdings, use and cost data described earlier. I also report results from a regression analysis of the price data. This analysis measures serial price inflation during the sample period as well as the impact of two mergers, West/Thomson (1996) and Reed/Shepards/Matthew Bender (1998). I conclude with a discussion and summary of the results.

Demand for Law Serials

Experience as a user of law serials suggests that each *unique* title is at best an imperfect substitute for any other title. For example, it is difficult to argue that information contained in

Areeda and Turner's well known treatise on Antitrust is duplicated in Kintner's *Federal Antitrust Law*; and this claim is strengthened considerably if a non-treatise (or even a non-antitrust) title is considered in the comparison. This user perspective seems to suggest that demand for each title is largely independent of demand for other titles. Thus, owners of individual titles already have the capacity to achieve monopoly returns; a corollary is that mergers don't matter.⁸

However, this user perspective is faulty in one important respect: in most cases, lawyers don't purchase the titles that they use, libraries do. This separation between user and buyer has important implications for the analysis of demand. As in the case of STM journals, and based on discussions with law librarians, law serials acquisition appears to be based on two factors — annual subscription price and expected use. All else equal, a title is purchased if its “cost/use ratio” is relatively low.^{9, 10} And from year to year, as budgets, prices and use patterns change, collections are adjusted accordingly.

The most interesting aspect of this library perspective, of course, is that individual titles are considered simultaneously. So, law libraries group titles from the eight categories of legal serials described earlier into a single “portfolio” and broadly apply the cost per use criterion.

⁸ This user perspective was apparently adopted by the US Department of Justice in its examination of the 1996 merger of West and Thomson. The corresponding consent decree requested divestiture of only a handful of titles that the DOJ thought overlapped enough in content to warrant competitive concerns. In other words, with the exception of the divested titles, the DOJ considered the majority of the titles to be poor substitutes for each other.

⁹ STM librarians often construct cost/use ratios for each title, rank them from lowest to highest according to this ratio, and then, starting with the lowest ratio titles, add journals to their collections until their budgets are exhausted. However, even in cases where the precise use data necessary to perform these calculations are missing, (law) librarians often conduct informal cost/use comparisons in their annual acquisition deliberations. In any case, this is an empirical question that we can examine using the data collected for this study.

¹⁰ Note that this acquisition approach is equivalent to having a library maximize the use value of its collection, given the available budget. This type of constrained optimization problem is commonly referred to in the operations research literature as a “knapsack” problem. Note that in practice a library's budget constraint may be “soft”; it may be expanded slightly to accommodate the marginal title that doesn't quite “fit” the budget. For an introduction to this issue in the OR literature see Daellenbach and George (1978).

Thus, titles compete with each other for budget dollars across an entire discipline, rather than across a narrow sub-field, as intuition might otherwise suggest (an intuition based on the perspective of the typical user of legal materials).

Publishers' Pricing Strategies

Given this demand structure, how do commercial publishers set prices?¹¹

Like firms in any industry, they will take into account the structure of demand and the likely strategies of competitors when setting prices. As described earlier, libraries – which constitute the bulk of demand for legal serials – attempt to purchase the most “use” given their budgets for serials. In practice this amounts to ranking journals on a cost/use basis and identifying a threshold cost/use value above which titles are no longer added (the budget is exhausted).

Given this portfolio demand, McCabe (2002) proposes a pricing model in which publisher pricing strategies are determined by the distribution of budgets and a title's relative use value. Since all titles in a particular demand portfolio compete for the same budget dollars, relative use value determines demand for individual titles (if prices are equal, higher quality journals experience greater demand). And the budget distribution influences whether, for example, owners of high use titles choose “low” prices and sell to most libraries or set “high” prices and sell only to the largest budget institutions.

Furthermore, in the model, firms controlling larger portfolios of journals have an incentive to charge higher prices, all else equal. The intuition for this result is similar to that in more traditional product markets. Greater portfolio size, perhaps due to a merger, enables a publisher to better internalize pricing externalities. To understand this claim consider a market consisting of two separately owned titles, A and B, possibly with different use values (this analysis is easily generalized to cases where the number of titles exceeds two). In equilibrium, A's price will maximize its profits, given B's price; the same will be true for B's price. Now

¹¹ There is a small set of non-profit publishers that sell (mostly) law reviews at modest prices. In general, these publishers are primarily interested in disseminating knowledge as opposed to profits. Here I assume that these publishers set prices to cover costs (and are thus ignored in the analysis that follows)

suppose that one publisher owns both titles. In setting prices, the publisher hopes to maximize the *sum* of profits associated with each title. This is achieved at a price level higher than observed in the previous case. The reason is that when the titles are separately owned, neither publisher considers the impact of its price choice on its competitor's profits. When the two titles share the same owner, the publisher accounts for these "externalities." In particular, the publisher recognizes that demand for A increases when B's price is increased and that demand for B increases when A's price is increased. And when demand for a title increases, its optimal price is higher.

The Empirical Evidence

To identify the cause(s) of law serials price inflation, information about demand *and* supply factors needs to be considered. On the demand side, a number of factors may increase prices: 1. An "outward" shift in demand due to increases in law library budgets. 2. An "outward" shift in demand due to a relative increase in law serials use. (Note that these shifts may be associated with a decline in demand elasticity, i.e. the responsiveness of demand to changes in price). It is easy to demonstrate graphically that such outward shifts lead to higher prices in most cases. As mentioned earlier, I was able to collect data on law serials use. Although explicit budget data is not available, information on changes in holdings and prices over time is a good proxy.

On the supply side, there are at least two factors that might contribute to price inflation: 1. An increase in (marginal) publishing costs. Ideally, actual publisher cost data should be used to measure any changes in marginal costs. However, since this data is not available (nor is it usually trustworthy) the next best solution would be some exogenous proxy for these costs such as changes in the amount of legal information available for publication. Again, as I mentioned earlier I was largely unsuccessful in achieving this goal. The one exception – the number of annual reporter volumes – suffers from a number of deficiencies (no information on volume size was available, and changes in the number of volumes may be related to factors besides costs, e.g. publisher market power.). Nevertheless, if I find that the number of volumes and reporter price changes over time are unrelated, this would suggest that costs

factors do not explain the observed price trends. 2. Consolidation among publishers. As discussed earlier, mergers among publishers is likely to result in higher prices. The effects of two mergers during the sample period are evaluated.

If the data was more complete (especially with respect to use and cost information), it would be possible to estimate a model of supply and demand that directly addresses the various possibilities described above. In lieu of this option, it is still possible, using descriptive statistics and single equation regression analysis, to construct a fairly persuasive story to explain the trends in law serial prices. Note that because of my interest in merger effects, this analysis also examines publisher-specific trends in prices, holdings, etc.

To begin, consider **Table 1** : *Average Prices, by Category, 2000 v. 1991*.¹² This table offers some simple price statistics, comparing average prices in 1991 and 2000, by category. In all cases prices increased, ranging from 16% for reporters to 211% for encyclopedias. The fact that price changes appear to be category dependent may suggest that demand for each print category evolved differently over the sample period. Note, however, that the reported numbers may not accurately capture the “true” price levels for each category (see note 3; for example, in Table 9, it appears that the true price increase for reporters is about three times the rate reported here). Nevertheless, it appears that the price increases experienced during the period were substantial, and exceeded inflation (recall that CPI-based inflation was 26%).

Table 2 – *Subscriptions by Serial Category, Using University Library Holdings*.

This table reports some university law library holdings statistics for 1990 and 2000, by category. During the period the observed declines in print subscriptions appear to be substantially smaller than the price increases described in the previous table. This suggests that user demand elasticities are fairly modest and/or that library budgets expanded sufficiently. As expected, the largest decline in total subscriptions was experienced by citators. According to law librarians, users began switching extensively to digital versions of these titles during the sample period. In contrast, looseleaf and newsletter subscriptions actually

¹² A total of 11 tables are presented here. Please refer to the notes contained in each table for details on their construction.

increased for the 29 university libraries.

Table 3 – *Subscriptions by Serial Category, Using Law Firm Library Holdings*

This table replicates the statistics in the previous table using law firm library holdings. The basic pattern is the same, although the decline in citators is much more substantial. This is consistent with the idea that law firms have less need to “educate” their users on how to access print citators, given the efficiency of online access. With respect to the other categories, changes in law firm subscriptions for looseleaf services, newsletters and treatises closely resemble those observed for university libraries; the corresponding declines in reporters and encyclopedias were slightly larger. Note that given the small number of participating libraries, these conclusions are necessarily tentative (though certainly consistent with prior expectations).

Thus, Tables 1, 2 and 3 indicate that the magnitude of the price increases generally exceeded the mostly modest declines in library holdings. That is, budgets (for at least the “important” titles considered here) were growing during the sample period.

Table 4 – *Subscriptions by Publisher, Using University Library Holdings*

This table reports changes in university law library holdings by publisher (in the next version of this report, prices by publisher will also be reported). Given the category-based statistics in Table 2, there are no real surprises here. Note, however, that the Matthew Bender titles exhibit the greatest decline in subscriptions, aside from the Shepard *citators*. All MB titles in the sample are classified as treatises, and compared to the average treatise price in 1991 (\$270), the average MB title in 1991 sold for \$623 (See **Table 1A** for publisher specific prices in 1991 and 2000.) A substantial though relatively smaller price gap still existed in 2000 (\$567 for the average treatise versus \$934 for MB). My discussions with K. Svengalis suggest that MB had raised prices considerably faster than other publishers of treatises prior to the sample period, and then decided to slow the rate of increase during 1990-2000, presumably in response to buyer resistance. This would explain both the pattern of prices, and the greater observed demand elasticity. This is important in helping to explain the merger results in Table 10.

Table 5 – *Subscriptions by Publisher, Using Law Firm Library Holdings*

This table replicates the statistics in the previous table using law firm library holdings.

Some differences between university and law library holdings patterns appear here, e.g. law firm libraries reduced their holdings of Michie titles quite substantially (by about 25%) whereas universities increased their numbers. But for the most part, the trends are similar, e.g. both types of libraries only slightly reduced their BNA, CCH, West, CBC and lawyers coop titles. Again, relative to the average treatise in the sample (see Table 3), the Matthew Bender titles saw greater erosion. Note that the Shepard *treatises* increase in both types of libraries during the sample period, especially in the case of law firm collections.

Tables 6 and 7 – *Relative Use, by Serial Category, 1990 and 2000.*

These two tables report results from my survey of serials use at libraries. Librarians were asked to respond to a number of questions regarding use of print serials in their libraries in 1990 and 2000. The relevant question here concerns the relative use of the typical title in category X in 1990 and 2000 (see note 1 in both tables). For 1990 librarians at both types of libraries agreed that Citators were among the most heavily used types of titles. As expected, relative use of print citators dropped substantially at both types of libraries by 2000. At both types of libraries, relative use of treatises increased. Similar parallels can be seen for the other categories (with the exception of newsletters and looseleaf services, where the two type of libraries diverge in their use of these titles in both years; my early discussions with law librarians led me to expect the former result due to the day-to-day immediacy of practicing law. Also, in 2000, the two types of libraries differ substantially in their use of reporters – this may reflect the interaction of different institutional objectives and online access, as in the case of citators). Together with the results for prices and holdings, these data appear to be consistent with the portfolio model of demand. For example, consider citators and treatises. Both categories experienced similar price increases during the sample period (see Table 1). Thus, the average cost/use ratio for citators increased during the period while the ratio for treatises increased far less. The portfolio model of demand predicts that subscriptions for the former should decline relative to the latter, and in fact this is what we observe. That is, if a category's relative cost/use ratio increases (decreases), that category's share of total subscriptions will also decline (increase).

Table 8 – 2000 v 1990 Use responses, grouped by Serial Category.

This table summarizes librarians' response to a question regarding the relative use of *individual* titles in 2000 compared to 1990. The responses for both types of libraries are consistent: compared to 1990, use in 2000 is lower for reporters and citators, and about the same or slightly less for the other four categories.¹³ This result removes one possible explanation for the “excessive” price inflation observed during the sample period, namely, an increase in demand for legal serials.

Two other credible explanations remain – increases in costs, and/or increases in market power (due to mergers perhaps),. As described earlier, the cost-related data in this study is limited to the number of reporter volumes published annually. To determine whether variation in the number of volumes per year was related to reporter prices over time I estimated two linear regression models: one in which the number of reporter volumes was included as an explanatory variable and one in which it was not.¹⁴ Although reporter prices and volumes are positively related, the latter has no apparent effect on the *change* in reporter prices during the sample period. This result is consistent with evidence related to STM journals (see McCabe (2000)) – the observed price trends do not appear to be explained by changes in costs. The possibility that market consolidation may explain some of the observed inflation is addressed next.

Tables 9 and 10 – Regression Results, Price changes, 1991-2000, and Merger Effects

Table 9 reports the price changes by category based on estimation of a difference in differences model (see McCabe, AER, 2002). As alluded to earlier, this approach provides a more robust estimate of the actual price changes for an unbalanced panel of prices. Price changes between 1991 and 2000 range between 41% and 190%. However, if one examines the most recent five years (2000 v. 1995), it appears that with the exception of reporters, these

¹³ Note, that for MB titles, use in 2000 compared to 1990 is almost the same as the result for treatises as a whole. The MB-specific values for 2000 v. 1990 use are 2.90 (universities) and 2.92 (law firms). Thus, the decline in MB holdings compared to the average treatise is probably not due to a similar decline in relative use value.

¹⁴ In both cases the estimated model includes a fixed effect for each title, and a series of time dummies.

price increases have slowed somewhat. Nonetheless, they remain substantial with the important exception of citators (the corresponding change in the CPI was 13%). Turning to Table 10, the price impact of two mergers, West-Thomson (1996), and Reed-MB-Shepards (1998), are reported.¹⁵ In the case of West-Thomson it is clear that the merger was associated with a significant price jump for the affected titles, averaging more than 20%. Recall that DOJ approved the merger after the divestiture of about 50 titles and anticipated no adverse impact from the deal.¹⁶ This view was not based on a portfolio approach to the market; rather, the antitrust agency adopted a content-based market definition. That is, if two or more titles contained very similar content, e.g. two antitrust treatises, then monopoly control of these titles would be unacceptable. Otherwise, a merger of two or more firms with little or no content overlap among their portfolios poses little threat to competition. Clearly the empirical evidence is inconsistent with this view.

In contrast, the Reed-MB-Shepards transaction does not appear to have had any measurable adverse effect (of course, it is not possible to know how much *lower* prices for these titles would have been *but* for the merger). The likely explanation for this outcome relies on our previous analysis of holdings and use trends for the various types of titles. During the sample period, demand for Shepards citators dropped precipitously, and based on the price analysis in Table 9, this development probably accelerated in the 2nd half of the period. Thus, any attempt by a merging firm to raise these titles' prices faster than the market average is not likely to be profitable. With respect to the MB treatises, although demand for the titles may have not shifted (since use values were in line with those for other treatises), the observed price gap probably placed these titles in a more elastic region of their respective demand functions. Even though post-merger prices for MB titles increased at a rate slower than the rest of the market (this is the meaning of the negative coefficient reported in Table 10), holdings of these titles still declined at a rate higher than the average treatise. Again, it would seem that the

¹⁵ Note that the merger effects are estimated *simultaneously* with the price changes reported in Table 9; thus to obtain an estimate of price changes experienced during 1991-2000 by the average West treatise, for example, one needs to combine the results from Tables 9 and 10.

¹⁶ Seven of these divested titles are in the sample. In the regression analysis, their ownership status is changed from West or Thomson to Reed in the post-merger period.

merged firm's optimal strategy for these titles could not have entailed the type of price increase observed with West-Thomson. Given this situation for the Shepard citators and MB titles, McCabe (2002, working paper) shows that any remaining titles (the Michie portion of the Reed portfolio) are also likely to experience little benefit from the merger. Indeed, this is what is observed. Note that this type of analysis can be applied to the West-Thomson merger: in this study, that deal encompassed reporters, encyclopedias, and treatises, none of which suffered the precipitous drop in demand seen with citators; in fact, the majority of these titles are treatises and demand for them remained stable during the sample period.

Results Summary and Discussion

The results of this study are useful in several respects. As originally conceived, it was hoped that this project would shed some light on why law serial prices have escalated faster than economy-wide prices. Despite the shortcomings of the data, I believe that the likely causes have been identified. First and perhaps foremost, the unwillingness and/or inability of law libraries to eliminate important subscriptions (or equivalently, to reduce spending on law serials) has allowed publishers in most cases to raise their prices at a rate consistently higher than standard indices of inflation. Second, the lessening of competition among law serial publishers has enhanced market power and further raised prices. Most notable here is the merger of West and Thomson in 1996. The regression results indicate that titles affected by this transaction experienced a jump in prices exceeding 20% during the post-merger period. On the other hand, mergers do not always result in measurably higher prices. The Reed/Matthew Bender/Shepards merger in 1998 did not result in higher prices. However, the fact that print citators were largely abandoned by libraries during the 1990s and that Matthew Bender treatises exhibited relatively high demand elasticity in this period may account for this result. Furthermore, it is impossible to determine whether the affected titles would have experienced less price erosion but for the merger.

The evidence collected also allowed me to consider other possible causes of the observed price trends. Increases in the use value and/or marginal costs of law serials over time might account for some fraction of the price increases. However, if anything, the use data suggests that prices should have declined over the sample period. And although the available cost data

was limited in scope, it does not imply that publishers raised their prices in response to increasing costs.

Another important dimension of this study is revealed by comparing these results with research on other serial publishing markets, and in particular, the market for STM journals. In both cases, a portfolio approach to library demand is consistent with the data, i.e. that librarians consider many titles simultaneously in their collection decisions. The implication of this approach is that mergers among diverse sets of titles can raise prices. Both the law serials and STM journals markets offer empirical support for this hypothesis. Furthermore, in both cases inelastic demand appears to account for much of the observed price inflation. In contrast, changes in use value or costs do not appear to be important causal factors in either market.

A third policy-oriented dimension should also be considered. Since publisher mergers are often associated with significant price increases, this begs the question of why (US) antitrust officials have failed to take any significant action over the past decade. In the case of West-Thomson it appears that the DOJ adopted a “market definition” based on content overlap, i.e. a publishing merger was harmful only to the extent that some of the merging parties’ titles were clear substitutes for *users*. Since then, the DOJ has begun to consider the possibility that publishing markets should be defined more broadly, reflecting the realization that libraries and not users purchase the lions share of publications. Nevertheless, to date no such mergers have been substantially modified, much less blocked, due to concerns about anti-competitive effects.

Finally, the transition from print to digital distribution (which I only briefly touched upon in this study) promises dramatic change in serial publishing markets. In the world of STM, publishers have begun selling electronic bundles of their journal portfolios. In the law serials market a similar trend can be seen. In addition to the information traditionally available on Lexis- or Westlaw-type services it is expected that many if not all of the categories of print titles considered in this study will migrate to digital databases. Once this occurs the modest ability of libraries to discipline publishers by canceling individual titles will be eliminated. Faced with the difficult choice of purchasing or not purchasing the entire West/Thomson digital bundle, it

is hard to imagine that many law libraries will say no. In my 2002 working paper on this subject, I argue that the combination of bundling and the ability to price discriminate (i.e. charging each library a unique bundle price) should enhance the market power of the largest publishers, resulting in higher prices and less content for libraries. Obviously, this is an area that deserves future research attention.

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