

The "free" economy comes at a cost

The Economist

2017.8.24

Facebook

- Facebook, whose users visit for an average of 50 minutes a day, promises members: "It's free and always will be."
- YouTube watchers devour 1bn hours of videos every day
- These free lunches do come at a cost; the problem is calculating how much it is

Users themselves produce value

- Unlike conventional merchants, companies like Facebook and Google have their users themselves produce value
- Information and pictures uploaded to social networks draw others to the site
- Online searches, selections and "likes" teach algorithms what people want. (Now you've bought "The Communist Manifesto", how about a copy of "Das Kapital"?)

History

- In 1993 MCI Mail was charging people 50 cents for the first 500 characters of a digital message, increasing by ten cents for each extra 500.
- The internet slashed that price to zero. Charging would have been impractical, so small is the marginal cost

Fixed cost

- Companies like Google and Facebook have fixed costs to cover: engineers, data centres, etc
- To make money, they squeeze their users indirectly, by charging companies to put appropriate advertisements in front of captive eyeballs
- In the second quarter of 2017, Facebook eked an average of \$4.65 out of each of its users by peppering screens with ads and promoted posts

What people are getting back

- Economists struggle to work out what people are getting back when they barter their data and attention for digital services
- A study offered people different cash amounts in exchange for giving up Facebook for a month
- They then estimated its average annual value to the consumer at around \$750
- A survey suggested that on average people value free search engines at \$16,600 per year, maps at \$2,800 and video at \$900

Problems

- Professionals are not allowed to evade tax by selling their services for benefits in kind, so why should consumers not be taxed if they are paid for their data in the form of services?
- GDP is mostly measured by transactions at market prices
- In 2013 American GDP should have been \$19bn higher than reported

- Consumers tend to respond much more strongly to "free" offers than to prices that are only fractionally higher than zero
- When Amazon first offered free shipping in European countries, orders surged—but not in France, where by mistake it charged around ten cents

Troubles competition authorities

- Excessive market power can be defined as the ability to raise prices above what would be charged in a competitive market
- But there is no prices to compare
- Google commands a market share for internet search of over 90% in most countries in the European Union, where antitrust authorities in June fined it \$2.7bn for promoting its own comparison shopping services above its competitors'

Trustbuster

- Its services may have been free, but the trustbusters judged that its market power was curbing consumers' choices
- Opinion is divided on whether the free economy needs fixing, and if so, how