

# Reflection Paper: Fixed vs Variables costs and the importance of sunk costs in Strategic Decision-Making

During the development phase of a *real estate brokerage website*, one of the early challenges we encountered revolved around infrastructure decisions — specifically, hosting the platform in the standard cloud platforms like AWS, Azure, GCP etc. versus exploring cost-effective alternatives.

This reflection will explore how the study of **fixed and variable costs**, as well as an understanding of the **sunk cost fallacy**, will significantly influence a pivotal business decision that will ultimately contribute to operational sustainability and cost-efficiency.

## Initial Strategy and Emerging Concerns

Initially, the decision was to host the platform using a popular cloud infrastructure provider like AWS, Azure, GCP etc., were attractive for their scalability, security, and reliability.

However, in the absence of a real customer base in the initial days of business operation, the variable costs of usage-based cloud services will be a huge variable operating cost. Monthly expenses is anticipated to increase; including compute, bandwidth, storage, and third-party integrations. While there will be no significant income is expected, as the whole websites income model relies solely on advertisement income which is again pivoted on customer base.

This situation led to a growing misalignment between operating costs and value generation. The cloud services, although top-tier, is expected to be underutilized in the initial days. As low traffic is expected, the marginal cost per visitor or lead generated is anticipated to grow disproportionately, creating a financial strain on the project's sustainability.

## Cost Structure Awareness and Decision Pivot

Through our foundational understanding of **fixed vs. variable costs**, it became evident that we will be inadvertently **tying** our costs too closely to activity levels without a proportional return.

Cloud hosting, in this case, exemplified a purely **variable cost model**, where each user or byte of data incurred an incremental cost. With no guaranteed customer base, this model lacked predictability and risked long-term burn.

Furthermore, a key concept that helped realign our thinking was the **sunk cost fallacy**.

There exists some degree of psychological resistance to host the website in popular cloud platforms taking advantage of its various managed services as opposed

to managing everything in house.

However, economic reasoning reminded us that **sunk costs should not influence** future decisions. Only **marginal costs** and future returns matter. Acknowledging this key concept helped us pivot without regret.

## Strategic Shift to On-Premises Hosting and Open Source Platforms

The new strategy was to host the website on on-premise low-cost server using NextCloud, an open-source content collaboration platform that could emulate several cloud functionalities at a fraction of the cost. This move transformed our cost structure:

- **Fixed costs** → involves purchasing the hardware and setup, but these did not scale with usage.
- **Variable costs** → has **reduced** dramatically as we would not be paying for metered services.
- **Flexibility and control** → increased, allowing us to iterate quickly and test the platform in a controlled environment.

This shift will enable us to continue operations at a faster pace, gather user feedback, and experiment with new features — all without the financial pressure of a rising cloud bill.

It will help buy us time and clarity to focus on product-market fit and audience acquisition, essential ingredients for future monetization.

## Conclusion: Applying Cost Theory to Business Practice

The lessons drawn from **fixed vs variable cost theory**, coupled with a rational view of **sunk costs**, were instrumental in this business pivot.

This helped us decide to move away from a high-risk, consumption-based cloud model to a more stable and manageable cost structure. Importantly, this transition is not just about saving money — it is all about **gaining strategic breathing** room to focus on the core value proposition of the website.

In conclusion, this experience reaffirmed how **economic principles** are not merely academic but deeply practical tools that guide better decision-making.

For any startup or early-stage business with uncertain demand, **understanding cost behavior and avoiding the trap of sunk cost bias** is not just useful — *it's essential for survival !!!*