Cable Television Regulation

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After the typical survey of the recent history of regulation and its effects in the cable television industry, this chapter focuses on two main questions. The first asks whether the rise of direct-broadcast satellite (DBS) as a competitor to cable obviates the need for further regulation in cable markets. The second reflects the very recent focus of lawmakers and policymakers on bundling in the industry and its consequences, largely to consumers. There has been some interesting recent research on bundling that suggests the possibility of bundling as a market failure in cable markets. I propose to analyze that possibility in detail. Other possible topics are included in the discussion notes at the end of the outline.

1. Introduction: Cable Regulation and Its Effects

   (a) A Brief History of Cable Regulation (and Deregulation)

      - Pre-1984: Regulation according to terms of local franchise agreements.
      - 1984 Cable Act: Dereg I
      - 1992 Cable Act: Rereg I
      - 1994 (FCC) Going-Forward Rules: Dereg IIa
      - 1996 Telecommunications Act: Dereg IIb
      - 1999 Satellite Home Viewer Improvement Act (SHVIA)
        - Watershed legislation permitting widespread provision of local broadcast networks (ABC, NBC, etc.) by direct-broadcast satellite (DBS) companies.

   (b) The Consequences of Cable Regulation and Deregulation

      - Prices and Market Shares: (S: CPI, FCC Annual Reports)
        - Consistent increases at rates exceeding inflation (exc. '92-'94).
      - Quality: (S: FCC Annual Reports, Hazlett and Spitzer (1997), Kagan)
        - Also steadily increasing, due both to (i) entry of new networks and (ii) increased expenditure per network.
      - Choice: (S: FCC Annual Reports, Factbook)
        - Mixed evidence.
          * More services offered (movie multiplex packages, PPV, radio), but...
          * Only moderate increase in choice among most popular (Basic and Expanded Basic) services, despite significant increases in package size.

   (c) Conclusions:

- Price regulations had limited impact.
- Quality regulation infeasible (1st Amendment grounds).
- Bottom Line: Cable regulation has been ineffective at improving consumer welfare.
  - i. *If* there is a short-run market failure due to market power, is it offset by efficient long-run investment incentives?
  - ii. If not, how to correct in a dynamic, innovative environment?

2. Cable and Satellite Competition: Does Cable Need to be Regulated (Any More)?

   (a) The Multichannel Video Programming (Retail) Market

      i. Cable and satellite outcomes since SHVIA
         - Market shares: Satellite growing fast; cable flat.
         - Prices: Continue to increase (for both).
         - Quality: Continues to increase (for both).

      ii. Measuring cable market power after SHVIA
         - Goolsbee and Petrin (2004): 2001 own-price elasticities for cable and satellite are -1.5 and -2.5, respectively. While higher than previous estimates, suggests moderate market power remains.
         - Other evidence on Cable/Satellite substitutability.

      iii. The dynamics of competition between cable and satellite.

   (b) The Programming (Input) Market

      i. Programming Outcomes
         - Ownership, diversity, and network carriage.
         - Broadcast/Cable cross-ownership

      ii. The impact of horizontal and vertical concentration on program carriage
         - What are appropriate subscriber / affiliate carriage limits?
         - Concentration and network entry.

3. Choice Regulation in Cable Markets: Is Bundling a Market Failure in Cable?

   (a) Current regulatory focus is on *bundling* in cable and satellite markets.
      - 10/03 GAO Report, 3/04 Senate hearings, 7/04 FCC Symposium.

   (b) Reasons bundling may be a market failure:

      i. Bundling as price discrimination
         - Consumers may not choose individual networks; they may only choose bundles of networks.

      - Theoretical and empirical research in cable markets find such bundling acts like price discrimination (Adams and Yellen (1976), Bakos and Brynjolfsson (1999), Crawford (2004)).
      - Welfare effects: pro-firm, anti-consumer, pro-society.
   ii. Bundling as entry deterrent
      - Competition in bundles limits entry in distribution.
      - This effect reinforced by contracts between program suppliers and distributors requiring carriage on particular tiers.
      - Theoretical research (Nalebuff (2004)) suggests strong anti-competitive effects. No existing empirical evidence.
   iii. Bundling and cable quality (new research, in progress)
      - Bundling introduces externalities into investment and pricing decisions of program suppliers.
      - Can yield *over-investment* in quality (e.g. fees for broadcast rights to sports leagues)
      - Particularly important if short-run market power a perceived cost of efficient long-run incentives.

(c) Reasons bundling may not be a market failure:
   i. Analog (older) technology favors bundling; becoming irrelevant as industry migrates to digital access and control.
   ii. Simplifies choice, reduces administrative and marketing costs.
   iii. Guarantees widespread availability, viewed as *essential* in advertising market.

(d) Conclusions:
   i. Discrimination likely a moderate effect at most. What of entry deterrence and investment distortions?
   ii. If a market failure, what are appropriate remedies?
      - What analogies can be drawn from unbundling in other regulated industries (e.g. electric power, telecommunications)?

Discussion notes: Issues not listed above that might also be be addressed include:

1. Cable and broadband internet access.
2. Cross-country comparisons.
3. Cable and franchise bidding.