

1 NOTES AND COMMUNICATIONS MEDIA & ECONOMICS:
2 UNEASY BEDFELLOWS?

3 BY

4 WILFRED DOLFSMA* AND RICHARD NAHUIS**

5 1 INTRODUCTION

6 Discussions in and about the media tend to stir up emotions. This is hardly
7 surprising as the media have become an intrinsic part of everyday life. People
8 spend a great deal of their time consuming various media. One could even
9 claim that the media play a key-role in developing social cohesion and in
10 shaping people's perspectives on policies and perception of, for instance, how
11 safe the country is they live in. Nevertheless, however valuable and reward-
12 ing (or frustrating) such passionate debates may be, the time has come for a
13 more down-to-earth approach that draws on economics. The papers delivered
14 at this year's Annual Meeting of The Royal Netherlands Economic Associa-
15 tion (the *Preadviezen*) deal with media and economics (Dolfsma and Nahuis,
16 2005).¹ This paper summarizes the contributions and tries to trace the links
17 between them.²

18 1.1 *The Difference between Information and Ordinary Goods*

19 From the point of view of economics, the products that the media produce –
20 information, content, and advertisements – are called information goods.
21 Information goods differ from regular goods in four important ways. First,
22 the production costs are characterised by high fixed costs and low variable
23 costs. Variable costs of content (without considering distribution) are in many
24 cases (close to) zero, making the goods non-rival. Second, controlling access
25 to information goods (excludability) is problematic. For example, a radio
26 signal can be received and consumed for free by anyone who has a radio
27 receiver. Content is also, thirdly, an experience good: it is difficult to assess
28 the content before purchasing it which means that consumers of information

* Erasmus University Rotterdam, Maastricht University (MERIT), 2005/6 fellow Netherlands Institute for Advanced Study (NIAS), and visiting research fellow Economics Department University of Aberdeen Business School, e-mail: dolfsma@nias.knaw.nl

** CPB Netherlands Bureau for Economic Policy Analysis and Utrecht School of Economics, P.O. Box 80510, 2508 GM The Hague, the Netherlands, e-mail: nahuis@cpb.nl

¹ When we refer to authors in italics, we refer to a contribution in the *Preadviezen* 2005.

² In this summary of the *Preadviezen*, we hope to do justice to the authors' individual contributions. The authors are not responsible for any of the interpretations of their work presented here. We would like to take this opportunity to thank all the contributors to this year's volume. It was a pleasure working with them.



29 run the risk of being disappointed *ex post*. Consumers can also choose not to
30 consume such an information good in the first place. There are mechanisms
31 that mitigate the problems this characteristic causes, such as reputation of the
32 producer. A brand name such as that of *The Economist* is an example. Prod-
33 uct reviews and word of mouth information transmission are further ways of
34 mitigating the problem. Finally, consuming information can generate negative
35 or positive externalities. Think of the violence thought to be induced by web-
36 sites, films or television programmes as examples of information induced neg-
37 ative externalities and news or the contribution of documentary programs to
38 the proper functioning of a democracy as examples of a positive externality.
39 It is these specific peculiarities of information goods that make the informa-
40 tion market potentially vulnerable to market failures.

41 1.2 *The Economics of Media Markets*

42 The contribution by *van Dijk* and *Waagmeester* provides an overview of pos-
43 sible market failures in media markets. Their starting point is that media
44 markets' main trade is in information. Content and advertisement are the
45 two key types of information traded. The particular properties of informa-
46 tion as a trade good, as described above and elaborated upon at length in
47 the *Preadviezen* themselves, can be the cause for media markets to fail. As
48 externalities are not confined to information goods and the remedies to cure
49 failing markets are the same for both information and standard markets, we
50 will turn our attention to other characteristics of information goods that can
51 cause media markets to fail.

52 High fixed costs and – suppose for the sake of the discussion – zero mar-
53 ginal production costs by definition introduce inefficiencies. Charging a posi-
54 tive market price is inefficient as marginal costs no longer equal marginal price.
55 A price equal to the marginal cost of zero, however, makes it impossible for
56 firms to recoup the fixed costs. There is no reason to expect such a market
57 to attain an optimal situation: information goods will be under-produced, if
58 at all. Price discrimination could partially solve this problem: consumers or
59 groups of consumers would be charged different prices for the same goods,
60 depending on their willingness to pay. However, this is not easy in a market
61 where it is easy and cheap for consumers to copy all kinds of information:
62 possibilities for arbitrage are rife. Legal protection under Intellectual Property
63 Right law is discussed in light of this issue. Another route is product differen-
64 tiation, or 'versioning', which involves producing (slightly) different versions
65 of the good to meet the needs of different audiences. This is why the film
66 companies try to exploit different 'windows': a film is first shown in the cin-
67 ema, then it is brought out on DVD or video and sold or rented and finally
68 it is broadcast. Versioning allows producers, in some cases, to run down the
69 demand curve, and may be combined with price discrimination. Versioning is



70 useful in the case of durable information products such as movies but not so
71 appropriate for short-lived information goods such as the news.

72 The problem of non-excludability as described above adds another perspec-
73 tive. A (potential) producer who is unable to generate revenues from his con-
74 sumers because he cannot exclude those who do not pay and will either have
75 to stop producing or will need to turn to other sources of income. One solu-
76 tion is to 'sell' advertisers the attention of those who view, read or listen to
77 information goods. As it is virtually impossible to prevent (some) non-paying
78 consumers from consuming the goods, media firms tend to operate in such
79 so-called two-sided markets. The implications of this are elaborated upon
80 below. Advertisement funding might appear to be an alternative pricing mech-
81 anism, but it differs with respect to one key aspect. For advertisers it is the
82 number of viewers or readers (number of "eyeballs") that are reached that
83 counts and the consumer's willingness to pay for a program or newspaper is
84 not important. Advertisement income is used to lower the price of the media
85 good for consumers. This means that prices for media goods do not provide
86 the information that they usually do in a market thus giving rise to a sub-
87 optimal allocation. A popular television program can, for instance, attract a
88 large audience (lots of "eyeballs"). If an advertiser wants to reach this large
89 audience it will pay for a commercial during the program but the audience
90 will not necessarily be interested in the product advertised, or they may find it
91 over-priced. Advertisers may want to access information about their *expected*
92 audience but they need the media firm for that purpose, which means that
93 moral hazard problems can arise. This suboptimal allocation of resources is
94 not likely for pay-per-view media. Here the audience pays for the media goods
95 directly; the media firm does not have to sell "eyeballs" to advertisers. Media
96 firms can also try to raise additional income by creating programmes that for
97 instance involve consumers using SMS text messages (the telecom operators
98 pay a commission to the media firms), and they can apply for subsidies from
99 the government to cover initial production costs.

100 Even if the above problems could be solved, the proper functioning of infor-
101 mation markets would not necessarily be guaranteed as consumers are not
102 autonomous when they make decisions. For example, people may not have
103 enough information to make well-founded (consumption) decisions: they might
104 be myopic. Especially when media are discussed, and most particularly when
105 discussed in society at large, this possible myopic behaviour of people causes
106 concerns. This issue is documented in economic literature but a discussion on
107 this matter would take us too far away from the topic addressed here.

108 2 KEY DEVELOPMENTS

109 Wider social trends also have an affect on the functioning of media mar-
110 kets and create new challenges. For example, technological developments,



111 demographic changes (ageing or immigration), and changes in the leisure time
112 available to people are all relevant. It is tempting to argue that recent devel-
113 opments are more radical than previous ones. In some sense they are but the
114 claim that the emergence of internet is more radical than the introduction of
115 television is not so easy to defend. Taken from a media perspective, the kind
116 of influence internet has on the media is not new. Newspapers were the first
117 media in modern times to disseminate information to the masses, radio was
118 the first medium that made instantaneous reporting possible and television
119 added a visual dimension. Internet encompasses all these modes. For exam-
120 ple, a web-log functions as a newspaper but is much cheaper to produce. Tele-
121 vision and especially radio on the internet proliferate. As much as existing
122 media find new ways to disseminate their goods on the internet, internet also
123 allows the combination of goods that media offer to be unbundled. It is for
124 this reason that we did not include internet as a separate medium.³ Neverthe-
125 less, the internet is and will continue to be an important factor in the future
126 of media and media policy.⁴ Digitalisation is the key technological advance
127 that facilitated the development of the web but its advantages are not exclu-
128 sive to internet. There are several distinct trends that can be distinguished in
129 advances related, directly or more indirectly, to digitalisation:

130 2.1 *The Cost of Producing and Spreading Information Decreases Rapidly*

131 Web-logs illustrate this trend very well; there has been an explosion in the
132 number of these sites. How does this trend alter the perspective on the qual-
133 ity of the products that the media offer, for instance in terms of a mea-
134 sure discussed below, pluriformity? Should web-logs be included in a measure
135 of pluriformity of media? The impact of web-logs on society in the United
136 States of America suggests this is not unimaginable. Another illustration is
137 that computer-generated special effects are can be much cheaper than the tra-
138 ditional methods of creating such features. *Van Dijk* and *Waagmeester* argue,
139 based on *Waterman* (2004), that implications for production costs are not as
140 straightforward as they may seem. Total costs for a movie may not decrease
141 but actually increase. To illustrate, the most recent sequel of *The Lords of the*
142 *Rings*, renowned for its use of computer-generated imaging, had production
143 costs exceeding a quarter of a billion euros. In relative terms costs of special
144 effects might have decreased, but this has made it easier to cater the demand
145 for such effects: more of it may be included in a movie. In addition, new, more
146 expensive techniques are used. Overall production costs may thus increase. The

3 The definition of media that we use is: agents or activities that produce combinations goods aimed at communication. Goods produced by the media are a platform that allows for the purposeful combination of related goods to cater to a heterogeneous market. The internet actually allows agents to disentangle information bundles.

4 Internet is, however, much more than a medium (cf. Soete & Ter Weel 2005).



147 new special effects may increase demand for the movie, which in turn leads to
 148 a higher marginal revenue. In equilibrium, more of these cheaper special effects
 149 may be used and the total production costs could rise.

150 *2.2 The Spectrum Scarcity that was Prevalent Until the 1980s has*
 151 *Completely Disappeared*

152 This applies mainly to radio and television in that terrestrial technology is
 153 now complemented by digital radio and digital television. In addition trans-
 154 mission is now also available via internet, cable and satellite. Magazines and
 155 newspapers have never been restricted in terms of capacity; the only con-
 156 straint is the amount of shelf-space in the stores and kiosks.⁵

157 *2.3 Excludability has Become Technically and Economically Feasible*

158 The problems and expenses that arise from trying to exclude people from
 159 using the terrestrial signal without payment are the key to understand past
 160 developments within television and radio. Non-excludability, together with
 161 non-rivalry were valid reasons to consider these media to be a public good.
 162 Nowadays with digital broadcasts, scrambling and decoding make excludabil-
 163 ity economically feasible and open up the way for pay-tv. This is rapidly
 164 occurring in most European countries.

165 *2.4 More Heterogeneous Demand*

166 Demand has become more heterogeneous as individualism progresses and in
 167 Dutch society pillarization along socio-political lines is reducing. This implies
 168 that consumers are less (ideologically) predictable and more likely to be aware
 169 of or have experience of a wider range of viewpoints. Consumers are becom-
 170 ing less predictable.

171 3 MEDIA

172 Technological developments have and still are profoundly affecting the media.
 173 Some media particularly daily newspapers appear to be in serious trouble
 174 whereas others are flourishing.

175 Media contribute to the solution of public choice issues in general (cf. Sen
 176 1999). In the developed countries the prospects for most media look bright
 177 and as economic development and democratization proceed in the develop-
 178 ing countries the media will flourish there as well. Indeed, there appears to

⁵ This has not changed recently. Indirectly, sales may be affected by web based magazine sales. For books it has been shown that internet shopping leads to a higher distribution of 'marginal' titles (cf. Brynjolfsson et al. 2003).



179 be a two-way causal relationship: media flourish when the economy is in good
 180 shape and societies are open, but well functioning media can also contribute
 181 to economic development. State ownership of media and poverty are posi-
 182 tively related (Djankov et al. 2002). It is not exactly clear if the same holds for
 183 state supported but independent media organizations such as the BBC in the
 184 United Kingdom, the BRT in Belgium, and the many pillarized broadcast-
 185 ing companies in the Netherlands. Certainly the democratic process is stimu-
 186 lated by free media. Where media are free and independent, people are better
 187 informed and politically more active (Leeson 2005). Free media make politi-
 188 cians more accountable (Stiglitz 2002). It is thus obvious that politicians are
 189 interested in the media and how they function.

190 Free media can also help resolve information asymmetries in the economy
 191 in a broad sense (Stiglitz 2002). In this way, the media can assist agents to
 192 make informed decisions, and not only as citizens casting their votes. This
 193 raises the question of whether the media can also influence agents' prefer-
 194 ences. This is an area that economists have only just begun to explore using
 195 concepts such as 'framing' and 'reference points' (cf. Bateman et al. 1997;
 196 Kahneman and Tversky 1981; Dolfsma 2004).
 197

Box 1:

ECONOMISTS IN THE MEDIA

Economists tend to take an ambivalent attitude towards the media. As
 economists, the idea of a market for ideas where they have to compete with
 others to get their voices heard makes sense. As academics, however, they
 tend to assume that the importance of what they have to say will be obvious,
 and obviously recognized. Often, however, they learn to their dismay that this
 is not the case. The messages they have to offer may be disregarded entirely,
 or forgotten about when preliminary discussions have ceased and awkward
 trade-offs have to be made (Klamer and Meehan 1999). The experience one
 is likely to have when approached by representatives from the media may be
 disheartening, as *Groot* and *Maassen van de Brink* notice. Being hardened
 experts by now, their advice is not to be disappointed when journalists merely
 want to pick your brain, want you to act as parrot for their own message, or
 make a highly biased selection from what you have to offer (and present it as
 their own). Maybe, as *Kalshoven* suggests, economists are too self absorbed
 and simply do not know what interests the broader audience, nor how to
 deliver a message. If your message is not welcome, or if you are unable to
 package it properly, perhaps it is best to have others take the honour/do the
 dirty work. There usually are (some) economists who are better able to medi-
 ate between the academic world and society at large. Some write op-eds, some
 write regular columns in daily newspapers or magazines. In the Netherlands
 there are the equivalents of Paul Krugman. They do not write for the New
 York Times, of course, but, being the cradle of newspapers in the world,

198



199 the Netherlands offer an astonishing array of them. Newspapers seek their columnists not just to offer facts and analysis, but also for their opinions and their reputation. Sometimes the expertise that is lacking in the editorial team needs to be complemented – while many trained economists have joined the editorial staffs of newspapers and magazines they are relegated to separate desks. As *de Kam* and *Nypels* further find, the economists involved do get an hourly fee that is higher than their hourly wage as professor, but intrinsic motivations are likely to be equally important. What can be a better sign of recognition than to see that you have a noticeable influence of public policy or opinion?

200 3.1 *Television*

201 Television is currently the quintessential medium. It attracts attention from
 202 audiences, politicians, and academics alike. People discuss the content of spe-
 203 cific programs, but also hotly debate television's role in society. Economists
 204 tend to translate the character of such discussions as welfare economics.
 205 However, welfare economics is not the topic of choice of a large group of
 206 economists. The term 'television' was first coined in 1900 to refer to a method
 207 to transmit visual information. It was first put into practice in 1926, and
 208 has since proved to be able to arouse a variety of opinions and emotions.
 209 In 1948, the first television broadcast in the Netherlands went on air and
 210 some 400 television sets in the Eindhoven region were able to receive the
 211 signal although 'officially' the first broadcast was in 1951. The government
 212 expressed concerns that technology was encroaching on people's leisure time.
 213 They were worried that this new technology would become a master or even
 214 a tyrant alienating people from each other and themselves. Television would
 215 have to be controlled and could not simply be left in the hands of private par-
 216 ties, it was held at least in the Netherlands. Television may offer ways to edu-
 217 cate and civilize the people, but could just as easily be used to demean them,
 218 or so it was perceived. Allowing the profit motive to play a role would be a
 219 certain way of the latter to ensue.

220 When television first started it was entrusted to broadcasting organizations
 221 based on the pillars or segments of Dutch society (Lijphart 1968) in the same
 222 way radio had always been (*Hoefnagel*). As a result of considerations men-
 223 tioned above the Netherlands ended up with one of the most complicated
 224 broadcasting systems in the world. The elites within the pillars made sure
 225 that only programs or topics they considered appropriate were aired (Dolfsma
 226 2004). Only when television had diffused widely and drew all of the attention,
 227 for instance, could radio experiment a little with products for which there was
 228 a huge demand yet were considered inappropriate such as pop music.

229 At present the Dutch broadcasting system is considered to be one of the
 230 most competitive in the world, at least according to the British newspaper



231 *The Economist*. The pillarized broadcasters are still an important part of the
232 system and draw their income from fees from members, tax revenues from
233 the government and advertisement income. A new policy has been [2005]
234 drafted to 'modernize' the system, but *Hoefnagel* comments that economic
235 arguments should play a more important role while *van der Ploeg* criticizes
236 the lack of commonsense economic logic in the newly proposed policy as well.
237 The incentives introduced in the proposal seem to be at odds with the public
238 goals one would associate with a system to produce television, as well as
239 the more specific goals included in the draft proposal. In this latter regard,
240 researchers such as *van der Ploeg* have asked, how can public broadcasters
241 offer high-quality products tailored to a small niche market while at the same
242 time catering to a large audience to generate resources? *Dommering* remarks
243 on how policy has remained relatively unchanged since the 1930s and that
244 bold decisions are shied away from.

245 Economies of scale necessary to produce television of high-quality by jour-
246 nalists or producers of television programs who can operate independently
247 will be difficult to attain. *Van der Ploeg* holds that, due to technological
248 developments, television products can be considered less and less as public
249 goods. The newly proposed policy will not necessarily jeopardize the variety
250 of programs offered as much as the quality. It is especially quality in
251 a journalistic and cultural sense that *van der Ploeg* worries about. Assuming
252 such qualities are covered by the term 'accuracy' that Mullainathan &
253 Shleifer (forthcoming) use, *van der Ploeg* either does not believe that there is
254 enough interest (of sufficient size to reach minimum efficient scales) in such
255 topics within the Dutch viewing population, or that market forces may not
256 be trusted to offer quality at all. Indeed, as broadcasters become more dependent
257 on the number of members they will have to compete (Hotelling 1929)
258 in the center of the preference spectrum.

259 *Van Cuilenburg* concludes that the unprecedented liberalization of the
260 Dutch television market has resulted in greater variety but that there has been
261 considerable crowding in the middle of the spectrum. This raises the question
262 of whether it is the task of a government to make ensure that its people are
263 able to access a varied offering of media products?

264 The television market may be assessed using a number of measures. Diversity,
265 the heterogeneity of content offered by the media, which is one of these
266 measures, can be further analyzed in terms of pluriformity and plurality.
267 Plurality refers primarily to the number of media, such as broadcasters or
268 titles, while pluriformity refers to the heterogeneity of the content. Plurality is
269 related to such measures as the Herfindahl–Hirschman Index and other concentration
270 ratios. The Dutch television market is dominated by three main
271 players who share the nine national general interest channels: the combined
272 public broadcasters, the RTL group, and the SBS group. Recently, even a



273 tenth channel started: Talpa.⁶ The radio market is much more competitive,
 274 needless to say. The two measures of plurality and pluriformity are related but
 275 they do not necessarily coincide. A monopolized market can still offer a het-
 276 erogeneous range of media products. Economic competition and journalistic
 277 competition are different; the two need not coincide. *Van Cuilenburg* argues
 278 that pluriformity is not necessarily a good thing: the pluriformity offered
 279 might represent what is demanded by the market, but may exclude minority
 280 voices. Most media markets are not so good at catering for minority voices:
 281 they are better at representing majority views. Public broadcasters tend to be
 282 a little more open to minorities and more representative than private ones are.
 283 Increased competition during the 1990s has sharpened this picture.

284 These two sub-currents that determine the pluriformity profile can both be
 285 measured. Pluriformity can be measured in terms of topic, format or genre
 286 etc. Using program categories as indicator and Theil's relative diversity mea-
 287 sure⁷ it seems that public and private broadcasters do not differ much. Public
 288 broadcasters pay more attention to news coverage, while private broadcasters
 289 spend more on foreign sit-coms, human interest programs and movies. The
 290 public broadcasters are somewhat more diverse in what they offer than the
 291 private ones (0.93 compared to 0.75).

292 Another way of judging what media firms offer their customers is the freedom
 293 of choice available: irrespective of the variety of different products, how big is
 294 the supply of media products in comparison to demand? The measure for 'media
 295 profusion', or the extent to which supply exceeds demand,⁸ shows the enormous
 296 choice available to the Dutch audience. For every 1½ hours of watching televi-
 297 sion during prime time – which is the average – some 45 hours of television is on
 298 offer. The performance of a media such as television increases when diversity and
 299 freedom of choice increase. An overall measure of the performance of a particular
 300 media can thus be obtained by using the following formula:

$$301 \quad \text{Media performance} = \text{Profusion} * \text{Diversity} \quad (1)$$

302 Table 1 shows that media performance in the Netherlands has clearly
 303 increased over the last 15 years. Dutch viewers have an astonishing amount
 304 choice which is currently still increasing. Again, public broadcasters do bet-
 305 ter than private ones. The doubling of supply of television products between
 306 1990, when liberalization of the market had just set in, and today far exceeds

6 For a country of barely 16 million inhabitants, the total number of television channels avail-
 able in the Netherlands – national and regional, general and special interest – currently is an
 astonishing 151.

7 Theil's relative entropy measure gives an indication of diversity: $D = (-\sum p_i^2 \log p_i) / \log n \cdot p_i$
 Is the proportion of program category i , and n is the number of categories; 0 (homogeneity) $\leq D$
 ≤ 1 (heterogeneity).

8 Profusion = Q_s / Q_d , where Q_s = supply of media products to the market, and Q_d is demand; $0 \leq$
 Profusion.



TABLE 1 DUTCH TELEVISION MARKET 1990–2004: PROFUSION, DIVERSITY AND PERFORMANCE (18–24 O’CLOCK)

	Television channels (#)	Hours of broadcast	Hours watched	Profusion	Diversity (Theil)	Performance entire system
1990 ^a	3	5731	423	13,5	0,78	10,5
1990	4	7687	423	18,2	0,76	13,9
1995	7	10754	464	23,2	0,68	15,9
2000	9	16291	484	33,7	0,67	22,4
2004	9	16422	561	29,3	0,86	25,3
	index 1990 = 100					
1990 ^a	75	75	100	75	102	76
1990	100	100	100	100	100	100
1995	175	140	110	128	90	114
2000	225	212	114	185	87	162
2004	225	214	133	161	113	183

^a Without the recently (1989) established private television channel RTL4.

Source: *van Cuilenburg* (in *Dolfsma and Nahuis* 2005).

307 the number of extra hours that people actually watch television. The number
 308 of viewing hours only increased by a third. Pressure on the players in the field
 309 to be more efficient and find ways of tapping new markets has thus increased
 310 substantially. *Van Cuilenburg* concludes that liberalization has not increased
 311 diversity or the quality of television programs, but especially the sheer num-
 312 ber of them and thus the freedom of choice. This has caused the doubling of
 313 the media performance measures between 1990 and today; a development for
 314 which the private broadcasters alone are to be thanked.

315 How sustainable, in an economic sense, is this situation? And, from a socie-
 316 tal perspective, does the ever increasing offer of media goods increasingly sub-
 317 vert common forums or points of reference? Perhaps discussions such as these
 318 will soon be irrelevant as technology develops and access to television becomes
 319 regulated through conditional, pay-per-view, which means that the media goods
 320 are no longer public goods. *Dommering* is firmly of this opinion.

321 3.2 Radio

322 Capacity for radio transmission has increased dramatically. The ‘new’ capac-
 323 ity is accessed via the cable or the internet. However, most people listen to the
 324 radio where this capacity is not available, for example in the car or at work
 325 (on construction sites). Many people may never bother to connect their radio
 326 set to the cable. So if broadcasters want to reach a larger audience, being
 327 able to reach those who receive the signal with an antenna is crucial. After
 328 considerable discussion, the available frequencies where (re-) allocated in 2003



329 by means of an auction. *Maasland, Onderstal* and *Rutten* analyze the chosen
330 allocation mechanism and discuss possible alternatives.

331 A long discussion preceded the actual decision on the allocation mechanism
332 that was used – indeed, politically, the process leading up to the decision about
333 how to allocate frequencies was a messy one. The government proposed auc-
334 tioning radio frequencies in the light of the auction of the GSM-frequencies
335 for the 3rd generation of mobile telecom applications. The vested interests of
336 incumbent radio stations delayed the decision as long as possible. When the
337 decision to auction the frequencies seemed to be finding support the radio
338 stations lobbied intensively against it. They even called upon their listeners to
339 make frequent phone calls to politicians and to send them emails and with suc-
340 cess. What was intended as an auction turned into a ‘beauty contest’. Moreover,
341 in contrast to initial plans, firms were allowed to obtain two nation-wide slots,
342 creating more room for incumbent parties in the radio market to maneuver
343 strategically and prevent new entry.

344 *Maasland* et al. argue that this was an unfortunate result of the political
345 process. A process organized along the lines of a ‘beauty contest’ introduces
346 many subjective elements. For example contenders were required to submit
347 a business plan and a draft broadcasting schedule for evaluation along with
348 their financial bid. Judging these two requirements adds a subjective element
349 to the decision. Many stations were displeased with the outcome of the pro-
350 cess. Some took the government to court, while others, who might have suf-
351 fered from a winner’s curse, tried to deviate from the broadcasting schedule
352 and mission that they had first proposed.

353 A look at other types of auctions shows that different (unpolluted) auc-
354 tion would have been a better allocation mechanism. To secure pluriformity
355 of what is offered on the radio it is likely to be sufficient to set minimum
356 requirements. Under these conditions, an auction involving several rounds
357 would be more likely to meet the demands postulated and would have avoided
358 some of the negative effects that occurred. For a discussion on the details of
359 the auction we refer to *Maasland* et al. It can be indisputably concluded that
360 the debate on what public interests are at stake should be dealt with sepa-
361 rately from the issue of how to organize the allocation itself. It seems that
362 the government’s lack of economic expertise concerning allocation procedures
363 (auctions) made it vulnerable to pressure from the actors in the field.

364 3.3 *Newspapers*

365 Newspapers that are free of charge are becoming increasingly wide-spread.
366 Some newspapers have become available on smaller ‘Berliner’ format – more
367 easily read while traveling. Do these developments or experiments constitute
368 a desperate attempt by publishers to extend the life-cycle of a product that
369 is nearing the end of its natural life? Or is there a healthy future ahead



370 for publishers who can adapt and cater to a changing demand-landscape?
371 Studies have shown that the amount of time spent reading has dropped while
372 the topics people are interested in have mushroomed. New technologies have
373 helped publishers to cater niche markets and people willing to spend money
374 on media products even if they consume them less intensively. The range of
375 topics covered in newspapers has increased as the number of sections and
376 supplements have especially in their Friday and Saturday issues.

377 For a long time the proliferation of newspapers has been artificially sup-
378 pressed by governments. Newspapers and their staffs were heavily taxed and
379 the freedom of the press was limited. In fact it can be said that it was not the
380 declaration of freedom of speech and press in the Dutch constitution of 1848
381 that allowed newspapers to flourish but the abolition of taxes. Much like any
382 other ordinary product, according to *Pfann*, interference by the government is
383 not to be welcomed. Despite increasing concentration ratios and a decreasing
384 number of editorially independent newspapers (see also *van Cuilenburg*), the
385 editorial foci of newspapers reveal a diverse range of approaches. Moreover,
386 newspapers have been subject to increased competition from the other media,
387 especially over the last few decades.

388 *Kalshoven* claims that the quality of economic news offered has increased,
389 at least on the pages explicitly devoted to economics. Other journalists might
390 need extra economic training or the economists among the editors could be
391 called on to contribute to or advise on subjects. What *Kalshoven* finds more
392 worrying is the fact that journalists tend to process information that is eas-
393 ily available, mostly from publicly listed firms, which often does not get much
394 further than the PR departments. Small and medium sized enterprises for
395 instance are thus largely neglected.

396 3.4 *Magazines*

397 *Hakfoort* discusses the Dutch market for popular magazines (excluding sci-
398 entific journals and professional magazines). The consumer magazine market
399 is very dynamic. In the 1990s, 400 – 500 new magazines were introduced
400 yearly, while at the same time some 150 magazines disappeared from the mar-
401 ket. The market, however, seems to have stabilized and in 2004 only about
402 50 magazines were introduced. The turbulent developments in the 1990s are
403 likely to be related to the long economic boom and the emergence of cost
404 reducing desktop-publishing technology. The fact that the amount of time
405 spent reading is still declining could also be one of the reasons the market
406 has stabilized. *Hakfoort* focuses on competition issues in the consumer mag-
407 azine market. He argues that one of the possible entry barriers to the market
408 is access to distribution channels. This is supported by the fact that the vast
409 range of magazines on offer is produced by a small number of publishers that
410 have access to distribution channels.



411 To find out whether publishers indeed have market power, traditional
 412 measures – like the price cost mark-up – are not useful, however, *Hakfoort*
 413 argues. Why is that? The magazine market and most other media markets are
 414 so-called two-sided markets. Two-sided markets can be characterized as “mar-
 415 kets in which one or several platforms enable interactions between end-users,
 416 and try to get the two (or multiple) sides ‘on board’ by appropriately charg-
 417 ing each side” (Rochet and Tirole 2004). To launch a new magazine, a pub-
 418 lisher needs advertisers as well as readers. If a publisher contacts potential
 419 advertisers the first thing they will ask is: what is the (expected) size of your
 420 readership or audience? However, it is not possible to set prices for and sell
 421 subscriptions without knowing the revenues from advertisements as this deter-
 422 mines the price of the magazine as well. Higher advertisement income will
 423 allow for a lower price charged to consumers, but may alienate the reader-
 424 ship too. How is this related to the question of measuring market power? To
 425 see this consider the extreme example of a free newspaper the *Metro*, which
 426 is distributed at train stations for instance. Consider a competition authority
 427 trying to estimate market power. They might calculate the price mark-up for
 428 consumers and see that it is zero. Based on traditional thinking about com-
 429 petition and market power, two conclusions could be drawn: *Metro* follows a
 430 strategy of predatory pricing against the incumbent newspapers. As soon as
 431 it has established a position in the market, or when competitors have had to
 432 exit the market, *Metro* is then expected to start charging a price to cover costs
 433 and possibly to recoup losses sustained. The other conclusion could be that
 434 the market is extremely competitive and soon *Metro* and possibly other news-
 435 papers as well will go bankrupt. Neither of these conclusions are necessarily
 436 valid. The competition authority should have taken the other side of the mar-
 437 ket into account as well. How much market power do the newspapers have on
 438 the advertisement side?
 439

Box 2:

THE MEDIA IN ECONOMICS

Where the attention of consumers of media products tends to focus on a limited number of people, issues or outlets, a similar trend is visible within the economics discipline as well. Are processes associated with the workings of the media entering the discipline? According to *Van Dalen and Klamer* the answer to this question is yes. This situation may be easily explained and need not necessarily be a bad thing. Most articles published are not noticed at all – there are simply too many of them. Time to read is limited, and you’d like to read something that you believe relevant. Even a small quality difference between

440



articles might thus result in highly skewed distribution of attention for them (Rosen 1981). The need to have common points of reference in discussions might even explain why an absence of differences in quality of a good offered can lead to a highly skewed distribution of attention (Adler 1985). The result of an efficient global communication of ideas might actually be an increased cluttering of economists in subfields that do not interact with each other. Within such subfields there are different ways of establishing reputations and institutions to galvanize them. Lists of economists who are most cited internationally or nationally are among these. Economists who can establish a link, creating a structural hole between a subfield with a more central field, can easily end up being reputed, at least in the cluster. May they have chosen the easy way out from the more central field where they may not have been top dogs? Will the cluster survive when the linking pins disappear from the scene? This is difficult to say.

441

442 4 A FOCUS ON CONTENT, MEDIA, OR BOTH?

443 In the previous section we discussed the four key media. In the first section, however, we argued that a media-economic view takes the goods that
444 are being traded – information or content – as a starting point. This seems
445 at odds with the focus on the distribution channel – the medium.
446

447 Indeed, WRR (2005) and Nahuis et al. (2005) argue that an analysis of the
448 media should start out from the relevant markets. The question is whether the
449 medium is the correct proxy for the relevant market. This is pertinent as internet
450 and wireless technology lead to a convergence of media. Are you watching
451 television, making a phone call or using the internet when you see the best
452 goals of a football match on your mobile phone? The internet offers magazines,
453 television, radio as well as newspapers. Another argument for a focus on
454 the product and the market, rather than the medium, is that market failures
455 are in most cases related to the product and its market. Whatever organization
456 has produced the goods is irrelevant. One simple example is the externalities
457 related to the consumption of information. Well-informed citizens are argued
458 to be important for a well-functioning democracy. It is obvious that it is not
459 important *how* citizens are informed – by means of television, newspaper or
460 the internet – but only *that* they informed. Finally, van Rees and van Eijck
461 (2003) show – by examining time-use data – that consumers in some cases first
462 choose what they want to consume (for instance news) and subsequently which
463 medium to use.⁹ Against this background *Hoefnagel* argues that an analysis of
464 the media markets had better started by analyzing content or *functions*, such as
465 the market for news, the market for amusement and so on. This, however, does
466 not imply that policy making can be restricted to the level of content. If an

9 Such time-use data offers a complicated scene, however, and is not easily interpretable.



467 analysis of content markets leads to the insight that public provision of some
468 content would be welfare enhancing it could still be decided of course that
469 policy is to be designed for a specific medium. As television is still the most
470 important source of information, it is not surprising that public interference
471 is most prominent with respect to this particular medium. *Hoefnagel* does not
472 argue that this is necessarily ineffective but he argues that policy should start
473 with an analysis of where markets fail and what public intervention aims at. His
474 review of the history of media policy shows, however, that policy makers are
475 almost exclusively focused on the (minor) issue of suggesting marginal changes
476 to the organisational aspects of the Dutch public service broadcaster. In his
477 view, the result of this persistent focus on aspects of implementation rather
478 than on developing a clear view on what public intervention should aim for
479 leads to an 'accumulation of compromises'. In this case the sum of the parts
480 is less than the whole.

481 5 LESSONS AND CHALLENGES

482 What general lessons can be drawn from the *Preadviezen*? And what questions
483 remain unanswered yet?

484 5.1 *Lessons*

485 Both from the papers on the public broadcasting service and from the allo-
486 cation of commercial radio frequencies it is clear that the government is pre-
487 occupied with details rather than the key questions: What public interests
488 should be served by policy? And subsequently: What is the most effective way
489 to get these interests served? *Maasland* et al. argue convincingly that the gov-
490 ernment should first have formulated its goals clearly and only then should it
491 have had the experts work out the best way to reach them. In reality, discus-
492 sion about mere details has bogged down debates on what the public goals
493 should be. Similarly, the discussion about the redesign of the Public Service
494 Broadcasting (PSB) system in 2005 first involved a detailed discussion about
495 individual television programs and the budgetary consequences for particular
496 players, and only later looked at the whole organisation and not even in a
497 structured way. We suggest that there should be a discussion about why one
498 would opt for a PSB in the first place. Such a discussion could still be staged.
499 The first lesson, thus, is: *policy makers try to guide developments in the media*
500 *but seem to lack direction.*

501 A second lesson is closely related to the first: the *vested interests of players*
502 *in the media influence policy making substantially.* This lesson is not unique for
503 the media, of course. Lobbying takes place on daily basis in policy making.
504 However, the ability of the media to influence the public opinion is unique.
505 Indeed, the media is in control of the media and may set the agenda. There



506 is thus all the more reason for the government to be well prepared when it
507 wants to change policy.

508 From all the papers included in the *Preadviezen* it is clear that econ-
509 omists can make a significant contribution to the public debate. Offering
510 common-sense reasoning, using basic insights from their own field, economists
511 can calm tempers and suggest useful distinctions to clarify the debate. How-
512 ever, *economists often enter the debate too late or are absent or excluded from*
513 *debates where they potentially could play a useful role.* Economists often enter
514 the debate when political compromises have already gelled. If the compromise
515 is at odds with basic economic insights, economists should put forward criti-
516 cism. However, delicate political compromises are difficult to challenge again.

517 A final lesson: *Economists are not overly influential in the media.* Newspa-
518 pers often ask economists to write for the economics pages. However, econo-
519 mists are seldom asked to apply their expertise to cover new topics as social
520 security, taxation and international policy even when relevant economically. It
521 seems logical to conclude that public debates, policy formation and media
522 reporting could benefit if economic insights were drawn on more often than
523 is currently the case.

524 5.2 Remaining Questions

525 A set of contributions on media and economics offers insights and answers,
526 but also gives rise to further questions. Some of the most important questions
527 that remain, according to us, are:

- 528 • How does the explosion of information available to people in society
529 affect the extent to which they are informed?
- 530 • What is the impact of media consumption on people's preferences and
531 happiness?
- 532 • How can competition be *measured* in two-sided markets?
- 533 • What effect would a 'free' fully advertisement supported newspaper
534 delivered at home have on the daily national newspapers?
- 535 • How should an auction for Dutch radio frequencies be designed if the
536 government redesigns the structure and content of five public radio
537 channels?
- 538 • Does high-quality public service broadcasting induce high-quality com-
539 mercial broadcasting, or is the opposite true?

REFERENCES

- 540
541 Adler, M. (1985), 'Stardom and Talent,' *American Economic Review*, 75, pp. 208–212.
542 Bateman, I., A. Munro, B. Rhodes, C. Starmer and R. Sugden (1997), 'A Test of the Theory of
543 Reference Dependent Preferences', *Quarterly Journal of Economics* 112(2), pp. 479–505.



- 544 Brynjolfsson, E., M.D. Smith, and Y. Hu (2003), 'Consumer Surplus in the Digital Economy:
545 Estimating the Value of Increased Product Variety at Online Booksellers,' *Management*
546 *Science*, 49(11).
- 547 Djankov, S., C. McLiesh, T. Nenova, and A. Shleifer (2002), 'Media Ownership and Prosperity,'
548 in: A. Clapp-Itnyre, R. Islam and C. McLiesh (eds.) *The Right to Tell; The Role of Mass Media*
549 *in Economic Development*, Washington DC, World Bank, pp. 141–166.
- 550 Dolfisma, W. (2004), *Institutional Economics and the Formation of Preferences*, Cheltenham,
551 Edward Elgar.
- 552 Dolfisma, W. and R. Nahuis (2005), *Media and Economie – Markten in Beweging en een Overheid*
553 *die Stuur zonder Kompas*, Den Haag & Amsterdam, BNG & Koninklijke Vereniging voor de
554 Staatshuishoudkunde (in Dutch).
- 555 Hotelling, H.H. (1929), 'Stability in Competition,' *Economic Journal* 39, pp. 41–57.
- 556 Kahneman, D and A. Tversky (1981) 'The Framing of Decisions and the Psychology of Choice.'
557 *Science* Jan. 30.
- 558 Klamer, A. and J. Meehan (1999), 'The Crowding Out of Academic Economists: The Case of
559 Nafta,' in: R.F. Garnett Jr. *What Do Economists Know?* London, Routledge, pp. 65–85.
- 560 Leeson, P.T. (2005), 'Ignorant and Apathetic: The effect of Media Dependence on Political Knowl-
561 edge and Participation,' mimeo.
- 562 Lijphart, A. (1968), *The Politics of Accommodation: Pluralism and Democracy in the Netherlands*,
563 Berkeley, University of California Press.
- 564 Mullainathan, S. and A. Shleifer (2005), 'The Market for News,' *American Economic Review*,
565 forthcoming.
- 566 Nahuis, R., M. Appelman, M. van Dijk, B. Vollaard and D. Waagmeester (2005), 'Onderweg
567 Naar Morgen – Een Economische Analyse van het Digitaliserende Medialandschap,' CPB doc-
568 ument, 78, Den Haag, Netherlands Bureau of Economic Policy Research.
- 569 Rees, K. van en and K. van Eijck, (2003), Media Repertoires of Selective Audiences: The Impact
570 of Status, Gender, and Age on Media Use, *Poetics*, 31, pp. 465–490.
- 571 Rochet, J.C. and J. Tirole (2004), 'Defining Two-Sided Markets,' Preliminary Draft, IDEA and
572 GREMAQ, Toulouse.
- 573 Rosen, S. (1981), 'The Economics of Superstars,' *American Economic Review*, 71, pp. 845–858.
- 574 Sen, A. (1999), *Development as Freedom*, New York, Oxford UP.
- 575 Soete, L. and B. Ter Weel, eds. (2005), *The Economics of the Digital Society*. Cheltenham: Edward
576 Elgar.
- 577 Stiglitz, J. (2002), 'Transparency in Government' in: A. Clapp-Itnyre, R. Islam and C. McLiesh
578 (eds.) *The Right to Tell; The Role of Mass Media in Economic Development*, Washington DC,
579 World Bank, pp. 27–44.
- 580 Waterman, D. (2004) 'The Effects of Technological Change on the Quality and Variety of Infor-
581 mation Goods' mimeo, Indiana University.
- 582 WRR, Wetenschappelijke Raad voor het Regeringsbeleid (2005), *Focus op functies: een agenda*
583 *voor een nieuw toekomstbestendig mediabeleid*. Amsterdam, Amsterdam UP.

