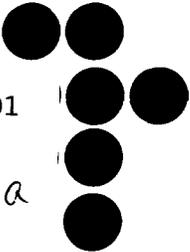


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COMMUNICATIONS
FORUM

MERGERS IN THE COMMUNICATIONS INDUSTRY

Richard H. Churchill (T.A. Associates)

Benjamin Compaine (Harvard Program on
Information Resources Policy)

Kevin Chandler (House Subcommittee on
Telecommunications, Consumer Pro-
tection and Finance)

February 13, 1986

Genga Arulampalam, Rapporteur

**Massachusetts Institute of Technology
Communications Forum**

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Mergers in the Communications Industry

Benjamin Compaine - Harvard Program on Information
Resources Policy

Compaine began by stating that there was nothing unusual in the current merger activity taking place among the media companies. He briefly traced the history of media companies describing the flurry of merger activity experienced by educational publishing companies in the mid '60s and newspaper companies in the mid '70s. In the mid '70s there were some who held the view that there was an unhealthy growth of concentration in the media business, while the Federal Trade Commission (FTC) symposium by and large found that there was certainly nothing that warranted legislation or major anti-trust activity. Many were surprised at that stage with the robustness and diversity in the media. He commented that the publishing industry was less concentrated in 1978 than it was in the 1940s and 1950s.

Analysing the reason for this sudden increase in merger activity he stated that it was primarily due to the desire of human nature to grow and get larger. No one likes to stay still. He also pointed out that there are other media companies that are always coming up from the bottom and get less attention until they get bought out. He then used a slide to show that not too many of the players in the media industry are large in all its sectors. This was further emphasized with a list of the ten largest media companies in terms of media revenue. The big companies are not big across the board. They are not multimedia companies but rather tend to specialize in one area. Also, the big companies are not getting bigger relative to the whole picture. Compaine confirmed that in 1984 there was a lot of activity among the 100 largest media companies. However, for every acquisition someone has sold. The point being that there is divestiture as well as acquisition taking place.

Turning his attention to some of the largest newspaper companies, Compaine stated that they had been making a lot of acquisitions lately. He then showed comparative percentage circulation figures for these large newspaper companies for the years 1946, 1966, and 1984.

	1946	1966	1984
Hearst	10.4	4.4	1.6
Scripps	4.4	4.8	2.2
K-R	3.4	4.0	5.8
Newhouse	1.0	5.0	4.6
Gannett	1.2	1.9	7.6

Companies like Gannett had increased their share of daily newspaper circulation. However, their circulation was still below the percentage circulation of newspaper giants of the

past like Hearst. Hearst today has become a much smaller factor.

Compaine pointed out that one of the things that are controversial when talking of the effects of mergers is, "what measure is being used". Is it revenue, circulation, audience reach, control over advertising, monopoly pricing of advertising, or something else? He said that we need to take a broad view of the media. It is no longer legitimate to talk about concentration in the newspaper or broadcasting industry as being good or bad because all these have substitutes. He referred to the 'blurring of the boundaries' between different sectors of the media. As examples he quoted cable and network TV and also newspapers and direct mail.

Compaine stated that in the '60s there was concern that the US automobile industry was becoming concentrated. However, no one worries about that today because General Motors, Chrystler, and Ford have very real competition with a lot of world wide players. The situation is very similar in the steel industry.

One of the fears in a concentrated media industry is that of a reduction in the diversity of voices. However, a recent paper published in the Journal of Communication (Summer 1985) looked at a number of measures of diversity. The author could not find any indication that competing media were anymore or less diverse than newspapers that have just a single owner in the city.

In closing Compaine said that it would be useful to keep an eye on all the new players in the game who like Gannett might become major players in the future.

Richard H. Churchill - T.A. Associates

Churchill stated that there has been a large investment in broadcasting and cable companies during the last few years. His company alone had invested about \$200 million in the last 4-5 years. While admitting that there was atleast some craziness in the marketplace giving rise to all of this merger activity, he said that the prices being paid are such because of the substantial underlying value. This underlying value he defined as CASH FLOW. He said that the newspaper, cable, and broadcasting companies have very high cash flows. In addition, these cash flows are very stable and always likely to go up rather than down. Also as a result of the cash flow, companies have very good growth prospects. He differentiated cash flow from net income. The media industry he said requires comparatively little, in terms of its resources, to be re-invested in such areas as research and development, plant and equipment, etc., unlike most of the American industry. Also it has no need for inventory which in

other industries absorb a large portion of a company's working capital. He further stated that since there are very high barriers to entry in each of the media businesses, it gives rise to oligopolistic pricing with high operating margins (in the range of 30%-60%). Over a very wide period of time these companies have grown very consistently (well in excess of GNP).

With reference to the stability of companies in the media industry, Churchill stated that he did not see any likelihood of them being blown out of the water with improving technologies. He said that owners of TV broadcasting companies were able to increase rates successfully even in the face of declining audiences. Referring to radio he said that though it was 'knocked out' by TV, it still reaches a good audience and carries high advertising potential. As for cable, he did not see it threatened by direct broadcasting in anyway but suggested the possibility of it being affected to some degree by the advent in the future of MMDS (Multichannel Multipoint Distribution Service).

Churchill was convinced that the media in general were a very successful business. The reason for privatization he said, was that the public companies had undervalued the market. He was of the opinion that these businesses should be managed to maximise cash flow rather than recorded earnings. Private companies have a high leverage on debt but public companies are more embarrassed to do so. The new players entering the market are pushing out the old. Churchill said that today TV stations sell in the region of 11-15 times their cash flow. For radio and cable companies the multiples are comparatively less significant (8-10 times cash flow) though still rather large. Churchill was convinced that the media companies as a result of growing cash flows will continue to attract buyers.

Finally, Churchill summarized the reasons for media mergers apart from cash flow as being: a) the trend towards privatization taking place in the US economy in general, b) the growth desire of some companies and the ability of media companies to easily generate a return on investment greater than 15%. Ofcourse some seek to buy media companies on a very long term perspective.

Kevin Chandler - House Subcommittee on Telecommunications

Chandler focussed his attention on the Electronic Media (EM). He said that the EM is more pervasive than any other form of media and has a significant impact/influence on the minds of the public. As a result it has drawn more attention from the House Subcommittee (HS). It has been reviewing the potential effects of recent mergers and takeovers both in mass media and in other industries. The common goal in all these businesses is to

attain a greater share of the market. However, a few corporations aim to also gain greater control.

Chandler said that in EM we are talking about knowledge and information, the news we receive, and the social values being communicated. As a result he said that we cannot address mass media the same way we address other industries. The media have tremendous power, much more than any other industry. During a recent hearing one witness estimated that of all companies targeted for takeover, about 80% eventually lose their independence. In terms of broadcasting however, the loss of independence causes serious questions as to the impact of takeovers - the effect on editorial judgement, and whether editors and producers of news programs will alter their news content to make sure they retain control of their company. In this context he quoted Senator Helms' grass-roots effort aimed at the takeover of CBS, which raises the concern of ideologically motivated takeovers of media companies. The HS is very concerned of ideological intentions although they realize that there are insurmountable first amendment problems that make it very difficult to deal with this kind of situation. Another concern on "the Hill" is that mergers will reduce diversity which in turn is crucial to democracy. The HS's goal is to make the most information available to the greatest number of people despite the changing nature of the conduits in which the information passes. Chandler referred to the Supreme Court's statement that the first amendment right is not only to protect the press from government intrusion, but also to protect the rights of the public to a robust marketplace and ideals.

During the HS's hearing on takeovers, some witnesses raised concerns about the potential possibility of reduction in R&D to boost up prices. In the broadcasting industry this could lead to reduced quality children's programming, programming for needs of minority and elders, public affairs programming, etc. all of which are not very lucrative. Takeovers in the broadcast industry he said could lead to just a profit and mass taste orientation.

He referred to Compaine's earlier assertion that mergers had always taken place. Chandler stated that the difference now is that all this is happening when deregulation is popular and regulation is not. He stressed that broadcasting is not an ordinary business. Broadcasters are effectively 'public trustees'. They are given an extremely valuable public resource and the high prices are due to the limitations to this resource.

The practice of the FCC that is extremely distressing at present he said, is that as a result of all the merger activity there have been more requests for waivers from the 'cross ownership' rules of the Commission. These rules have been critical in promoting diversity. However, the FCC has been granting these waivers more and more liberally without any criteria whatsoever. As an example he quoted Rupert Murdoch's request for a two year waiver on the grounds of the possible

occurrence of 'distress sale'. This was approved by the FCC without any proof, etc.

The FCC he said had recently attacked the 'fairness doctrine' (FD), again another crucial element in the promotion of diversity. Their reasoning was that the FD chills speech and violates the first amendment rights of broadcasters. He said that the FCC looks at only two FD complaints per year out of all the broadcasters. Since presenting both sides of controversial issues is what respectable journalists would do anyway, Chandler found it hard to believe that it chills speech.

In concluding he said that market forces must be balanced by government's efforts to set public interest and public service standards. The goal is to have EM with many tongues speaking and many voices. It should not just be profit oriented only, but conscious of values and first amendment rights. The broadcaster's primary obligation is to serve the public's interest.

Speakers' Comments and Responses to Questions

The question was asked as to why Chandler referred to broadcasting as "public trustees for limited resources". To this he responded by stating that the limitation of the resource is because of the restricted number of frequencies for broadcasting. He added that the Communications act of 1934 was established to restore some order to a chaotic system. Broadcasters licensed to serve on a particular frequency have certain obligations to the public. Not only is it a limited resource, but the license too is given free of charge.

Responding to a question on why DBS is not a competitive media, Churchill said that the competition is "not that significant". The technology is still evolving and potential maximum exploitation of the media is still a few years off. In the context of TV he added that, normally the first supplier is usually there to stay and difficult to dislodge. As a result there is a scramble among various forms of TV programming suppliers to open up new markets, particularly unwired cities. Churchill further commented that DBS even when they get their act together cannot deliver a much cheaper product than cable. However cable he said, runs the risk of repeating the mistakes made by network broadcasting.

Churchill was asked as to whether advertising had oversold its impact. In which case it could erode the assumption made by financiers. He responded that the situation varies with the eye of the beholder. To some it makes sense to advertise and they will even overpay whereas others may not consider it feasible.

He also pointed out that TV advertising is mostly done by a few big companies, which as a result puts TV in a risky situation.

A member of the audience commented that it appeared as though Compaine and Chandler held totally opposing views. To this, Compaine responded saying that Chandler's comments could have been written 20 years ago because he was still looking at old attitudes. With the advancement in technology he stated that Chandler's comments regarding limited spectrum space did not hold true. Compaine said that in today's context because of satellites etc., you now have 300 TV stations sending their own reporters to national conventions. As a result they are not dependent on just three networks to provide news. In response Chandler defended his position saying that Senator Tim Wirth has been a very strong supporter of competition. He added that we may eventually get to a point where there would not be a scarcity of spectrum space, but right now it was not so. He further emphasized that the problem of cross ownership could not be disregarded lightly as it certainly did affect the rights of the public to receive diverse points of view.

Finally a question was asked about the importance to the cable business of the 'publisher first amendment rights' (i.e. the ability to be free of regulation). Chandler responded saying that the cable industry existed as it did at present because of the benefits it received at the start. Allowing telephone companies to come in has the possibility of undermining the cable industry's position. However he predicted that this may not occur for 10-15 years, and even then cable would still have a good chance of maintaining its proprietary place. Also though telephone companies could pose a threat by developing the use of fibre optics, this technology would be available to other competitors as well.
