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Three Things Economists Wish the FCC Knew about Broadband Markets

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A funny thing happens when economists get together: They discuss the real impacts of public policy. Wouldn't it be nice if the Federal Communications Commission (FCC) participated in these discussions? In particular, wouldn't it be nice if the FCC knew that: (1) technology-based competition drives broadband progress and adoption more than regulation-driven competition does; (2) high market shares are a sign of market success, not market failure; and (3) the FCC's universal service programs are expensive and largely ineffective.

These lessons come from just two of more than 520 sessions at the 2016 meeting of the [American Economic Association](#). These two sessions, sponsored by the [Transportation and Public Utilities Group](#), reviewed all the latest research on several regulatory issues, but three papers should have been particularly interesting to the FCC.

Technology competition drives high-speed broadband

Professor James Prieger of Pepperdine University presented research on how [competition affects broadband speeds](#). In the paper, he and his coauthors examine how incumbent telecommunications Internet service providers (ISPs), or ILECs,¹ such as [AT&T](#), respond to competition from cable ISPs, such as [Comcast](#), and from new telecommunications ISPs called CLECs,² such as [RCN](#) in California. Because CLECs launch their businesses largely using ILEC networks (either by reselling ILEC services or simply leasing ILEC facilities), ILECs and CLECs use similar technologies. The cable ISPs, however, come from the cable TV industry and therefore use technologies that differ from the telecommunications ISPs.

The research finds that competition matters, but competition from cable ISPs matters more than competition from CLECs. When a cable ISP is present in a market, the probability that the ILEC offers high-speed DSL (the standard ILEC broadband technology) goes up dramatically. This probability jumps even higher when the cable ISP offers speeds exceeding 50 Mbps. Interestingly, the probability of an ILEC offering high-speed DSL goes down if the cable ISP offers a more modest speed — in the 25–50 Mbps range, for example — indicating that the highest speeds matter most.

ILECs responded much less dramatically to competition from CLECs than to competition from cable ISPs. In some instances, the responses are not even statistically significant. Competition from CLEC fiber greater than 1 Gbps is statistically significant but does not match the economic impact of cable broadband.

Why does this research matter? It shows that the most effective means of increasing broadband speeds is technology-based competition. It has been known for years that [competition from cable ISPs promotes ILEC broadband](#) deployment more than CLEC competition does. It has also been known that [CLEC entry into a market is weakest](#) when regulators try to help them by giving them low-priced access to ILEC facilities. Despite these results, the FCC continues to think that [regulation is the way](#) to increase broadband speeds. The agency has even gone so far as to open the door to expanded leasing of ILEC facilities by adopting Title II regulation.

¹ An ILEC (incumbent local exchange carrier) is a telephone company that provided local service as a monopoly prior to opening local telephone service to competition.

² A CLEC (competitive local exchange carrier) is a telephone company that competes with an incumbent local exchange carrier (ILEC).

High market share signals success, not failure

Professor Glenn Woroch of the University of California Berkeley [presented research](#) on how mobile service quality affects market share. This research matters because, for the past 10 years, the FCC has used an antiquated view of market competition called structure-conduct-performance, which was popularized in the 1940s and 1950s. This paradigm assumes that high market shares are inimical to consumer welfare, and the FCC has pursued radio spectrum and merger policies on these grounds. Woroch's research, however, demonstrates that high market shares in US mobile services markets result from particular firms providing demonstrably better quality than their rivals. So higher market shares indicate market success, not market failure. The FCC should modernize its view of competition and allow more customers to benefit from high-quality services.

Telecom subsidies are costly and accomplish little

Professor Olga Ukhaneva of the Georgetown Center for Business and Public Policy [presented research](#) on the FCC's expansion of its Lifeline program. This program began in the mid-1980s and evolved out of the breakup of AT&T. At the time, the FCC believed the breakup would make it impossible to sustain subsidies from interstate long-distance services to local telephone services. As such, the agency acted to effectively increase local telephone prices. State telecom regulators and others objected that the poor could not afford higher prices, leading the FCC to launch the Lifeline program.

About a decade ago the FCC expanded Lifeline to cover mobile services, because many low-income households were dropping landline phones in favor of mobile phones. Of course, it strains logic to conclude that any agency should subsidize someone to do something he or she is already doing without a subsidy, but nevertheless the FCC launched the reform — which more than doubled [Lifeline expenditures](#).

Did the expansion of Lifeline help low-income customers? Yes, according to Ukhaneva, but not in the way the FCC probably intended. She finds that even if the FCC perfectly enforced its Lifeline policies (which is not true today — some people receive the subsidy even though they are ineligible), 7 out of 8 low-income households subsidized would have service even without the subsidy. As a result, providing mobile service via Lifeline costs somewhere between \$1,151 (with perfect enforcement) and \$3,093 (with inefficient enforcement) per household per year. So the majority of the households receiving the \$138 per-year subsidy probably could have afforded to pay for service on their own.

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At the end of the day, I can sympathize with the FCC — regulation is complicated work — but some attention to research should improve that work considerably.