Chazen Society Fellow Interest Paper
Hollywood Gone Global

MATTHEW PRICE MBA '09

If someone had suggested after the Asian and Russian crises of 1997 and 1998 that the United States would be the cause of the next global financial crisis, many people might have laughed. Many people might also have reacted similarly 10 years ago if they had been told Hollywood would morph into a nexus of international talent and money. The Hollywood studios have always sought to adapt to trends—whether in markets or in content—and have a record of aggressively pursuing new sources of talent, and of financing for and distribution of their product. Recently, though, the studios have come, in part, to function as much like an export-import bank as the creators of the American cultural export good known as the movies. The flow of content, financing and influence from abroad has taken on dazzling proportions.

The major Hollywood studios have a colorful international history that dates back, most prominently, to the influx of foreign talent in the 1930s and 1940s, including prominent European Jewish émigrés who became some of Hollywood's leading figures. In recent years, the presence of internationalism within the Hollywood system, and the response to challenges from outside it, demonstrates a wholesale adaptation to the winds of globalization.

Consider some notable examples of the new international mix. A New Zealander reigned at the Oscars in the mid-2000s with *The Lord of the Rings,* a franchise based on a British academic's epic fantasy. A Hollywood film that included Arabic, Berber and Japanese Sign Language among its primary script languages (of which there were seven), *Babel,* was nominated for Best Picture. A Taiwanese director won the Oscar for *Brokeback Mountain,* a story about two gay American cowboys. This year Meg Ryan and Antonio Banderas together opened the Middle East International Film Festival in Abu Dhabi. Finally, Hollywood has slipped to the *third*-largest player in the global film industry—behind distant Bollywood and the nearby porn industry of the San Fernando Valley. And, lest it fall further behind, Hollywood is now making Bollywood films.

Since globalization began to take root, many industries have undergone previously inconceivable changes, and Hollywood is no different. The reality is that in the fabled Hollywood Hills the gates have been thrown wide open to globalization.

Follow the Money

One of the most recognizable sources of these changes is the dramatic shift in revenues coming to Hollywood. From 2001—when international box office revenues first exceeded half of Hollywood's theatrical income—to 2007, foreign box-office income increased to 64 percent. This increase reflects very robust growth in foreign spending at the box office, up from US$11 billion in 2003 to US$17 billion in 2007, reaching nearly twice the box-office spending in the United States. The most recent installment of *Pirates of the Caribbean* alone took in US$653 million in foreign box-office gross. The international box office is, quite simply, a strong growth area that the industry cannot ignore.

But there are two sides to the equation. Is this also a story of shrinkage on the domestic side? According to the Motion Picture Association of America, the average media consumer in the United States currently devotes a mere 4.8 percent of yearly entertainment spending to the theatrical-film box office. As is widely known, the studios have turned to DVD and other secondary revenue sources to make up for the supposedly lost American filmgoer. But the overall domestic entertainment market has experienced strong growth through the decade, and surprisingly, the much-maligned shrinkage is not exactly where it might be expected. Since 1992, the number of U.S. admissions to movies has grown in all but five calendar years. Domestic box office actually experienced nominal growth during the current decade, reaching US$9.6 billion in 2007, up from US$8.1 billion in 2001, while home video *decreased* significantly over the same period as a share of the entertainment wallet, from 16.6 percent to 13.9 percent.

So what other factors are at work? There are the some less obvious sides to the story. In-flight and mobile entertainment surpassed theatergoing in 2006 in terms of numbers of hours of consumption. Americans now watch more on the go now than they do in movie theaters. Some of this is booked as international revenue, depending on the country of origin of the airline carrier. But the largest shift is surprising: television. Americans watched 129 times more filmed entertainment on TV than in movie theaters last year, yet they spent under 10 times as much to do so. Television as a secondary source of revenue is demonstrating strong growth in volume, but it is very weak in contributing through price.

The domestic market's obvious shifts have perplexed Hollywood, as studios continue to chase new revenue streams. The recent series of guild strikes is a symptom of the problem, because for every new source being implemented, new contracts need to be made to disburse it. Whatever the perceived nature of weakness in the domestic market and whatever the complexity of the actual changes, the international market is robust, which leads to some interesting developments. The studios have moved beyond reliance on foreign revenue to acceptance and generation of foreign content, and a rapid shift toward international financing is emerging in Hollywood.

The Hollywood Ex-Im Bank: Roll in *Babel* . . .

Taking a few rather well known examples, Hollywood can be viewed as an Ex-Im bank in operation. *Babel* is an Academy Award–winning film distributed by Paramount Vantage in 2006. It was conceived by two Mexican artists, writer Guillermo Arriaga and director and producer Alejandro González Iñárritu. Its story seems to be an impressionist image of global differences—audiences think they are witnessing an amorphous interpretation of the biblical story of Babel, with its confusion of languages, on screen. In reality, the film's message is one of extreme global linkages: that of the Moroccan children's "shot heard round the world," which wreaked havoc in Morocco and touched lives in Japan, Mexico and back home in San Diego, just down the I-5 freeway from Paramount.

Ticket sales similarly went around the world. Though the film was not a blockbuster, its US$135 million in box-office revenues were even more skewed toward international than the average: only 25 percent originated in the United States and Canada. Furthermore, Paramount Vantage's model in making the film is illustrative of the changes afoot. Its investment was limited to the distribution rights for English- and Spanish-speaking territories—which cost nearly as much as the production costs of about US$25 million—and to the rights to sell the film on DVD. Others made the film. Others financed its production. Others sold it in other territories abroad. The studio art houses, or "mini-majors," are in place largely to take advantage of distributing already finished products, adding flexibility to the parent company's operating model.

As the available production model becomes more complex, it seems Hollywood is a selective market-maker or, in this case, broker. It uses its power to influence what gets done and how it gets released, in this case acting almost as a commodities trader using foreign intellectual property as a trading good.

. . . Roll Out *High-School Musical 3* . . .

A contrasting example is Disney's *High School Musical 3,* which was No. 1 in international revenues on its opening weekend in late October 2008, with US$40 million coming from 3,050 screens in 22 countries. The remaining (domestic) revenues were almost equal, so the film lies at the other end of the spectrum, with only 50 percent of its box-office revenues coming from abroad. This example fits the more traditional model: export of American culture, which audiences around the world have come either to love or bemoan.

. . . and Foreign Operations in Action

But Hollywood seems to know it may not succeed with this aging model forever and has chosen a radical point of departure with which the general public is not necessarily familiar: the studios are setting up their own local operations in foreign countries to make and sell local content abroad.

Have you heard of Twentieth Century Fox C.I.S.? Yes, that acronym stands for the Commonwealth of Independent States. BP may struggle to operate in Russia, but Hollywood can do so—thus far—with impunity. The territory also includes Armenia, Belarus, Estonia, Georgia, Kazakhstan, Kyrgyzstan, Latvia, Lithuania and Moldova. The Russian-made film *Admiral* has just been released by Fox under its name in those countries, in a move emblematic of the extent to which geopolitical thinking can be brushed aside by globalization—a Russian heroic film has been made under American control.

This development can be viewed as an extension of the on-location production of American films, which began with outsourcing to Eastern Europe in the 1990s because of cost savings. After the fall of the iron curtain, young opportunity-seeking Eastern Europeans set up production companies and attracted some large-scale Hollywood productions with massive savings on labor costs. One early example was *Mission Impossible* (1996), filmed largely in Prague, where it was also set. But Eastern Europe also came to serve as a stand-in: in *Cold Mountain* (2003), for example, the North Carolina hills were filmed completely in Romania, where an entire Civil War–era town was built. In the meantime, Eastern European locations also stand in for other Eastern European locations in American-made films. Daniel Craig will soon be seen in *Defiance,* a film about the WWII resistance set in the Belarusian forest but filmed in Lithuania.

Yet in contrast to these efforts, filming *Admiral* in Russia is not merely a matter of finding offshore production sources. Nor is this like marketing Coca-Cola or Ford cars abroad, with or without adaptations of design and style made to fit local sensibilities. This is a broad market entry in direct competition with national cinema, which for all intents and purposes has remained closed to outsiders since its beginnings in Europe and elsewhere.

If You Can't Beat 'Em, Join 'Em

Hollywood has also moved into another new territory where it believes it can thrive: it has made a move on Bollywood, India's treasure trove of money and talent and the largest film industry in the world by both number of movies made and by box-office revenues. But the move is to make local fare, not to export content from the United States. About 95 percent of box-office spending in India is for Indian movies, so U.S. companies have decided to swim with the Indian domestic tide, not against it.

In late 2007, Sony Pictures Entertainment became the first Hollywood major to release a Bollywood film in India, *Saawariya.* Notably, the studio also released it in North America—the Ex-Im bank is now also doing reimport, if you will. The film was not a box-office success. Nonetheless, other majors are in line to copy the model. Disney is releasing its first animated Indian film, *Roadside Romeo,* scheduled for summer 2009, Warner Brothers has two Bollywood projects in the pipeline and November 12, 2008, saw the U.S. opening of Fox Searchlight's *Slumdog Millionaire.*

The Spigot Is Wide Open

At the same time, politics and economics have driven further strategic changes in operating models. The burgeoning relationship with the United Arab Emirates is a case in point. What began as a topical necessity—films that aimed to reflect the post-2001 political environment in their content and needed to be filmed in the Middle East—has evolved into an open spigot of producing joint ventures and building physical facilities and of capital flow.

Early one-off efforts, such as *Syriana* and *The Kingdom,* both of which were filmed largely in the Emirates, have rapidly given way to a bevy of long-term deals. Abu Dhabi and Dubai are now in open competition to attract the best Western media outlets, opening massive facilities for film and TV news production.

Billions of dollars have been invested in joint ventures to create theme parks in the region, with Universal City Dubailand and Paramount's competitor park in Dubai. A year ago, Warner Brothers announced a billion dollar joint venture with the Abu Dhabi Media Co. to market its video games and to produce a slate of films. It will also team with a real estate company to develop a local theme park and hotel.

In the other direction, significant deals for foreign investment in Hollywood were announced around the same time U.S. banks were making the rounds among sovereign wealth funds in efforts to recapitalize. Until recently, the film world had come to rely largely on financing deals using hedge-fund money and private equity, brokered by leading investment banks. This had all but dried up, and a replacement was urgently needed. This fall, the Abu Dhabi Media Co., through its subsidiary Imagenation, invested US$250 million in a production fund with Participant Media in Hollywood and put US$100 million toward projects run by National Geographic Entertainment. The moves display the emirate's breadth of interest and reach, moving beyond Hollywood majors toward content producers with an agenda: Participant produces socially relevant movies, and National Geographic's films will capture "people's relationship to the world." Though these dollar amounts do not represent a significant proportion of overall film financing, they represent an unprecedented shift in financing sources.

And India will not be outdone: Reliance Big Entertainment (a subsidiary of Reliance ADA, the massive conglomerate), which controls much of Bollywood production, announced in June 2008 an investment of US$500 million in Steven Spielberg's DreamWorks SKG, with a further US$750 million of debt financing. Reliance also claimed at the Cannes Film Festival to have signed deals for financing the independent production companies run by such stars as Jim Carrey, George Clooney, Tom Hanks and Brad Pitt. In Spielberg's case, the deal was struck after his failure to reconcile differences with Paramount Studios. Now DreamWorks will split from Paramount with the Indian cash.

This development appears to parallel the (ill-fated) infusion of foreign cash into American banks, which took place repeatedly in 2008. But for the film world, where a schism between the studio majors and the independent world has existed for decades, the move represents a potentially significant structural change. A foreign conglomerate is acting as the de facto holding company for a diversified range of leading independent producers, all of whom would presumably sign distribution deals with the Hollywood studios. Foreign money thus presents the opportunity to lift such small shops to the level of direct competition with the majors, should an Indian company such as Reliance attempt to include distribution in its eventual operating model.

In a relatively short period of time, these kinds of developments—international sources of revenue, of talent, of content and local production and, most recently, of investment—have been game-changing forces in Hollywood. With new barriers falling nearly every month, it is apparently still quite true in show business that anything goes.

References

Cieply, Michael. “Tilting Hollywood’s Balance of Power to Talent Agency Clients.” *New York Times,* March 19, 2007.

Dapkus, Liudas. “On Location in Eastern Europe.” *Los Angeles Times,* December 21, 2007.

Economist. “Bollywood Rising.” February 7, 2008.

Foley, Stephen. “Spielberg Prepares for Deal Linking Hollywood with Bollywood Mogul.” *Independent,* June 19, 2008.

Giridharadas, Anand. “Hollywood Starts Making Bollywood Films in India.” *New York Times,* August 8, 2007.

Jaafar, Ali. “Sheik Waleed al-Ibrahim Expands Media Empire.” *Variety,* November 21, 2007.

Ramesh, Randeep. “Bollywood Billionaire Funds New Spielberg Studio.” *Guardian,* September 22, 2008.

Segers, Frank. “Eagle Eye Spots Overseas Win.” *Hollywood Reporter,* October 19, 2008.

———. “‘HSM3’ Packs Aisles Overseas.” *The Hollywood Reporter,* October 26, 2008.

For More Information

Imagenation Abu Dhabi, www.imagenationabudhabi.com.

Motion Picture Association of America, www.mpaa.org.