THE RELATIONSHIP BETWEEN DIFFERENT DISTRIBUTION CHANNELS FOR MOVIES: SOME LESSON FROM THE CASE OF FREE TELEVISION

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ABSTRACT

In the movie industry habit, the demand of exploitation windows next to theatres is usually related to the success in cinemas, which is assumed to orient subsequent consumption among audience.

Using a data base made of 1035 movies broadcast in peak time by the six main Italian networks during the period 1993-2002, we regress movies’ tv audience outcome on several independent variables as the attendance in cinemas, movie genre, country of production, temporal gap between tv and theatres, average share of the tv network on which the movie is broadcast in the transmission year.

Results show a statistically significant positive relation between the success in cinemas and tv audience, nevertheless the regression prove a far more powerful positive relation with the average share of the tv network on which the movie is broadcast. In particular movies that had a scanty success in cinemas reach high audience performance if broadcast on hi-share tv networks.

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1 INTRODUCTION

Movies are one of the main output of the audio video industry and they show a chain of
exploitation based on many distribution channels in subsequent temporal windows which start from
the showing in cinemas and come to television broadcasting through home video and pay-tv.

During the last years new potential ways of distribution have emerged including broadband
telecommunication networks in which movies are often distributed in Video-on-Demand form.
Several observers estimate online movie distribution can largely replace DVD distribution in the
long run.

Many operators consider movies as new broadband networks killer application.

In the movie industry habit, the demand of exploitation windows next to theatres is usually
related to the success in cinemas, which is assumed to orient subsequent consumption among
audience.

Then, demand in subsequent channels is partly exogenous being partially determined by
movies success in their first release in theatres.

That’s why movies are considered by many a potential killer application of new broadband lines,
capable of generate an increase in the demand of connections.

The paper looks into these dynamics starting from the consumption of movies on free television.

Movies are a main part of tv schedule and reach in Italy nearly 20% of prime time total time of
transmission. During last ten years though, audience and share figures show a decline of movie
audiences due either to changes in consumers’ preferences and to a better exploitation of
distribution channels prior to tv broadcast.

Using a data base made of 1035 movies broadcast in peak time by the six main Italian networks
during the period 1993-2002, we regress movies’ tv audience outcome on several independent
variables as the attendance in cinemas, movie genre, country of production, temporal gap between
tv and theatres, average share of the tv network on which the movie is broadcast in the
transmission year.

We have tested several functional specifications and we consider as dependent variable the
audience of the single movie in the first case while the log of the ratio between audience and
attendance in cinemas is the dependent variable in the second specification.

Results show a statistically significant positive relation between the success in cinemas and tv
audience, nevertheless the regression prove a far more powerful positive relation with the average
share of the tv network on which the movie is broadcast. In particular movies that had a scanty
success in cinemas reach high audience performance if broadcast on hi-share tv networks.

According with theory, tv outcome is negatively affected by the home video and pay tv diffusion,
which are a proxy of the exploitation of movies in distribution channels placed before tv free
transmission in the windowing system.

These findings may explain price reductions up the last three years in the intermediate market,
where tv networks buy movies transmission rights by movie producers.

The results have implications both on the use of movies in tv schedules and on would-be new
relations between rights owners and new distribution channels like broadband telecommunication
systems.

The paper is organised as follows: in the next paragraph I discuss the use of movies in tv and
the ways different programmes and genres are inserted in the tv schedule; in the third paragraph I
describe the windowing system used by movie industry as a mean of temporal price discrimination,
different windowing strategies are discussed and I try to find out conditions that lead to the birth of
a new window of exploitation; in the fourth paragraph the statistical model for the empirical work is
presented, describing relations to be tested by regression, and I describe data bases and variables
used; in the fifth paragraph regression outcomes are presented and discussed; in the sixth
paragraph I discuss figures implications for other movie distribution channels and specially for potential new exploitation windows that might develop thanks to broadband telecommunication systems.

2 MOVIES IN TELEVISION PROGRAM SCHEDULES

In many countries movies are an important component of television programming. Indeed, thanks to the public good nature of film and the existence of an international market, TV broadcasters can obtain a high-quality product (measured according to the resources invested) for substantially less than it would cost to produce. Furthermore, the preceding theatrical release serves as a process for selecting the best products and reduces the uncertainty concerning consumer reaction which is typical with audiovisual products.

A movie, especially if it is a success, can constitute a breakthrough product for television programming and in some cases is managed as an event (possibly with advance publicity in the normal television programs). As a highly diversified audiovisual product it allows all tastes to be covered and enables a network to reach a large number of viewers quickly. The movie is a finished product, already recognisable to the public, as a result of its previous marketing in other areas.

Of course there are some genres particularly suited to television use, especially those that allow family viewing such as social drama. Other programs, for example daily strips, need an introductory period which can last up to 5 or 6 weeks. The episodes aired in this period represent an investment in the viewer loyalty they can create for the future.

However, particularly for channels funded by advertising, there is also a downside to programming films on television: it does not permit the building up of loyalty because every film is different, with no recurring elements: on the contrary, unpredictability is one of the attractions. It is difficult to set up a regular appointment with a defined target audience, so the contacts produced tend to be devalued, from a commercial point of view, by their variety and unpredictability: it is difficult to select the audience and therefore difficult to use movies as a channel segmentation product.

In comparison with other programs, movies – like other fictional genres – generally have a guaranteed viewer permanence (relation between viewers in the average minute and viewers for at least a minute) averaging over 30% and sometimes reaching 40%. In other words more viewers stay to watch the entire program. For other programs the retainment rate generally sits between 25% and 30%, but if it drops permanently below 25% it means the program is unsuccessful.

In the area of pay television, movies – along with sport – are one of the main components of programming. The demand for these genres is in fact relatively inelastic in relation to price, and consumers are prepared to pay above-zero prices to have the programs available.

Finally, in Europe there are restrictions on the programming of movies in relation to both origin (a certain percentage of the films shown must be European) and scheduling: in France, TV stations may not program movies in prime time on Friday or Saturday evening, to protect theatres from television competition.

In Italy, the programming of movies on television increased steadily throughout the 1980s – the period of development of commercial television, which used them to take audiences away from RAI, the incumbent public broadcaster. From 1995 the number of movies shown on television, particularly in prime time, decreased on all channels, and parallel to this average viewer numbers went down. There are a number of reasons for this dynamic. On the one hand the expansion of distribution channels for movies, with home video, pay TV and pay-per-view, means that the movie comes to television already worn and therefore attracts a smaller audience. On the other hand the median price trend, at least up until 2002, did not reflect this diminished value and so for the broadcasters the opportunity cost of showing movies as opposed to other programs became less favourable.

Strong competition in the movie sector and the shrinking utilisation window drove producers to emphasise film content that was in line with the typical tastes of the dominant moviegoing public, that is to say young people in the 10 to 25 age bracket: this resulted in a product less suited to television audiences, which are mainly older age groups. Lastly, viewer tastes may have changed, as TV audiences in Italy and other European countries watch many telefilms and series that are made in their home country and deal with local themes.
In some ways this is not a new phenomenon. In the United States at the end of the 1960s the use of movies by the three networks rose over several years, driving an increase in the average prices the studios charged the networks, which in the end meant movies no longer represented value for money in programming. At that point they were removed from television programming, also because in the meantime cable television offered various theme-based channels which used movies as their main component; the three networks focused more on products they could more directly control, which also allowed more precise management of the audience segmentation in different time bands.

The audience for movies shown on television is of course linked to the power of the individual product, which changes over time and depends on production choices made by the studios years earlier. In addition, the presence and the quality of other programs influence the space available for any given type of movie in the viewer’s allocation of time. Finally, specific programming choices, meaning the programs scheduled before and after a movie and other channels’ counter-programming or mimicking strategies, can influence the median results for the genre.

In Italy Rete 4, a television network of the Mediaset group, has for several years programmed a movie every day in the late-night timeslot. Of course these are mainly repeats, but the continuity of programming enables us to establish whether some role can be attributed to movies in generating a specific typology of television viewing.

The demographic profile of the Rete 4 late-night audience shows no particular characteristics to differentiate it from the profile of the other time bands.

This first observation appears to confirm a proposition which I shall be developing in the following sections: that the viewing of movies on television is influenced more by the audience characteristics for the channel on which it is shown than by the specific traits of the movie itself.

3 RELATIONSHIPS BETWEEN DISTRIBUTION CHANNELS AND WINDOWING STRATEGIES

The movie is distributed through various sales channels in separate successive time frames, beginning with its projection in theatres followed by home video, video on demand and pay TV, until after two or three years it is aired on the generalist networks.

It is distributed at different times and at different prices (unit price per viewer) to the various channels, according to a time sequence which includes the American and other foreign markets. With each fresh release the movie can attract a further audience and its fixed production costs are absorbed by a larger number of total viewers; moreover it is possible to tap into the different degrees of willingness to pay to see the movie as close as possible to the initial release date.

The total return generated by an audiovisual product is made up of the revenue from all distribution channels, in other words theatre audience numbers plus the number of those who hire or buy videos and the viewers of pay television and commercial channels, multiplied by the wholesale unit price with the distribution margin deducted. However in regard to television it should be noted that the rights are mostly sold for a flat fee, so it is not precisely the number of viewers that determines the revenue from this area, but rather the number of subscribers in the case of pay TV and the the catchment area/ratings in the case of generalist television.

Windowing can be used to maximise the profits generated by an audiovisual commodity: where there is a client prepared to pay more for a product or one who would buy at a lower price than the one quoted, price discrimination produces a bigger profit than that generated by a uniform price. In the audiovisual field discrimination is achieved by distributing the same product through different channels and at different times, since it is possible to separate the various segments of demand on the basis of both the format (movie or television) and the desire to watch a new show.

Windowing, then, is a system of time-based price discrimination which allows film producers to obtain higher revenue and profits than with simultaneous distribution through all channels. The
main driver of price discrimination would appear to be the consumers’ desire to see a film as soon as possible. Consumers are assigned to the various windows according to their willingness to pay.

In reality however the relationships between the windows are more complex, and the producer’s net proceeds from the releases occurring first in time are not always higher than from subsequent releases. The net proceeds actually depend on the level of downstream vertical integration in the various distribution channels and the amount of added value the producer manages to secure.

Going first into theatres means not only favouring a distribution channel where the leadership of producers is established and exclusive, it also performs an important signalling function. The segmentation of the movies and prices in the subsequent windows of time are in fact defined in terms of the box office. For this reason, the amount spent on advertising for this initial release is not only decided on the basis of the larger audience numbers, it is also dependent on the revenue growth in the subsequent distribution channels.

Whereas in the early 1980s theatres represented the main channel for movie distribution and made up a total of about half the overall revenue, their incidence diminished progressively and for the past few years has been down to about 20%; however in spite of this decrease the theatrical release is crucial for the movie’s success. A movie is always a new product, and the information consumers receive about its quality is indirect and imprecise. The performance of a movie in its first few weeks in theatres sets in motion the dissemination of information by word of mouth and can trigger both an expanded demand for tickets and a potential curiosity which becomes evident with subsequent releases.

At present home video is the first release after the theatres, with a delay varying between three and six months; it is on the whole the most important distribution channel for the movie industry, accounting for around 50% of sales globally for the major film companies. The home video sector in turn is divided into rental and retail. Whereas in the United States the studios sell cassettes and DVDs at a uniform price and the retailer decides whether to rent them or sell them, in many European countries different prices may be quoted for rental-only (enjoying a protected window of 2-3 months) and for sale. This way, by applying higher prices, they manage to extract for themselves part of the revenue generated by renting. Comparisons between the returns from these two sales channels are not always clear-cut. In fact, taking into consideration the prevailing level of vertical integration, film producers get more money from the theatres than is generated by a rental, but less from these two sales channels are not always clear-cut. In fact, taking into consideration the prevailing level of vertical integration, film producers get more money from the theatres than is generated by a rental, but less than the amount from the sale of a video, let alone a DVD. This also explains the push by producers to move from rental to sales as the main marketing mode for home videos.

Many of the new distribution channels including video on demand, Internet, pay-per-view and distribution on broad-band telecommunications are concentrated in the period between five and ten months after theatrical release. In many cases contractual arrangements consist of revenue sharing with the rights holder, who gets 60% to 70% of what the end-customer spends, beyond guaranteed minimums which ensure a minimum return for each title and shift most of the commercial risk onto the distribution channel.

Pay television channels specialising in movies are big consumers and consequently often use output deal agreements in which they undertake to buy the entire output of a given supplier at predetermined prices. Prices on this intermediate market are fixed according to the number of pay TV subscribers, with a guaranteed minimum usually set at 4000-5000, the price per subscriber dropping substantially when the 4-5 million subscriber threshold is passed, due to the increased bargaining power. On the one hand contracts of this kind may be like the seller exercising bargaining power, but there is also an efficiency component because they save both parties the hard work of researching and testing information concerning the value of each individual movie.

Free-to-air television funded by advertising is the final distribution channel. It is not strictly speaking a distribution channel, because for the broadcaster the movie is a component of the production process which together with other programs delivers viewers to be sold on the advertising market. Television demand for movies thus depends on the tastes of the viewers and the range of programs in the schedules at any given moment. In recent years the demand has dropped in many European countries because other types of program – such as entertainment shows and programs based on invention rather than fact - have proved more effective in delivering audiences, and because the intermediate costs have not come down sufficiently to reflect this change. In many European countries there are limits placed on the number of advertising breaks that can be inserted during a movie. All things being equal this consideration reduces a movie’s revenue potential for the broadcasters and encourages its replacement by other genres.

The relationships between different windows include complementarity and interchangeability at the same time. When a movie is used in a window at the beginning of its use cycle it has contradictory effects. On the one hand it satisfies the demand for that particular title and reduces the demand in subsequent windows. On
the other hand success in one distribution channel can become an indication of quality and may increase the
demand for that title in subsequent distribution channels. Which of these two effects prevails depends on the
individual title and the specific conditions of the market.

Up to the mid-1990s the windows system was fairly fixed and followed a largely predetermined sequence,
but recent years have seen a tendency to adapt the windows to individual movies according to their
characteristics and the potential of the various distribution channels. There have been several instances of
going direct to video, especially with sequels, and a few films have been released early on television for the
purpose of creating a special event. This greater complexity and variety of distribution strategies for each
movie requires more expertise on the part of producers in the characteristics of each distribution channel, and
more monitoring activity.

In addition there is a build-up of windows, in order to drive the demand of the distribution channel
concerned, in the period between three and nine months after a movie’s theatrical release when several
distribution channels compete among themselves for titles that have not been over-exploited by other
channels. The interests of producers and distributors do not always coincide in these cases: the former always
concentrate more on maximising revenue over all the distribution channels than on the performances of the
separate channels. So it is not enough for a potential distribution channel to have viewers/subscribers in order
to achieve a good supply of films: it must position itself well in the producers’ overall strategies.

4 EMPIRICAL TESTING AND CONSTRUCTING THE DATABASE

In the empirical test my objective was to analyse the main factors determining consumption in
one particular distribution channel: free-to-air television funded by advertising. In particular it is
interesting to establish how much the viewing of movies is due to the inherent power of the
product, represented in the regression by theatre audience totals, and how much to the specific
power of the channel, represented by the median share for the television season in which the film
is shown.

In recent years the use of movies in television programming, especially in prime time, has
diminished in many European countries including Italy. This could be due to changing audience
tastes or to the reduced pulling power of movies because of increased exploitation of the product in
previous distribution channels.

Data has been gathered on the movies which were released in Italian theatres beginning with
the 1991-2 movie season and shown on television up to the 2002-3 television season: a total of
2400 films. In order to make the comparisons more uniform however, only the movies shown in
prime time on Italy’s six major television channels were considered: the three public television
channels, RAI 1, RAI 2 and RAI 3 and the three Mediaset Group channels, Canale 5, Rete 4 and
Italia 1.

Only the first showing of each movie was considered, not any repeats aired in subsequent
years. Moreover, to make the observations more uniform only those shown in prime time, from
8.30 PM to 10.30 PM, were included. About half of Italy’s families in fact watch television at this
time and that datum is fairly constant over the ten years under consideration, which makes the
share values of the individual channels more significant.

With regard to theatre consumption, for each movie we looked at the total number of tickets sold
and the date of release. The data come from Cinetel, who represent approximately 80% of the
movie theatre universe.

For television consumption, we looked at the audience and the audience share for the first
showing, the date, the day of the week and the channel, using data from Auditel, the official system
for surveying TV viewing using a meter.

Also added were data relating to the specific film such as the country of production and the
genre, supplied by Mediaset’s movie data bank.

The window, in other words the time in months between the two releases, was obtained by
comparing the theatrical release date and the date the movie was shown on television.

Further, the audience share and the average audience for the television season on the channel
showing the film were matched to each movie, as a proxy for the power of the channel
independent of the attraction of the movie.

In Italy there are no data on home video sales and pay TV viewer numbers for individual
movies. So for home video we used the annual percentage of Italian families with video recorders
and those with videodisc players, while for pay television we used the average number of annual subscribers; these data were matched to each movie, bearing in mind the year it was shown on television. This way the appeal of the other means used for watching a movie after its theatre run is captured indirectly when it is shown on television.

5 RESULTS OF THE EMPIRICAL TEST

Several functional formulations of the connection between the viewing of a movie on television and its success in theatres were constructed.

The television audience reached by the particular movie and also the audience share were used as the dependent variable. The latter measure allows the result to be normalised with respect to the audience fluctuations that occur during the year due to seasonal variations in TV consumption.

In general television consumption of movies is shown to be positively linked to their theatrical consumption, and the relationship proves to be statistically significant in the various formulations.

The distance in time (window) is predictably a negative element because the more time passes the more the interest of potential viewers declines, although the impact of this variable is not very strong.

The watching of movies on television is a positive result of the power of the channel showing them as well, and the connection is statistically significant and generally much stronger than the relationship to theatre audiences. American movies achieve better than average results, as do Italian films but to a lesser degree.

The effects of the impact of pay TV and home video are weaker, and the latter at least are not statistically significant.

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6 CONCLUSIONS

Despite the growing complexity of the windowing system, television remains an important channel for the film industry in many countries. In this paper we have explored some of the factors determining the viewing audience generated by movies on television. This audience is positively linked to the movies’ theatrical success, however the performance is also significantly due to the
power of the television channel on which the film goes to air. This result can have implications for the operation of intermediate markets. The price paid for a movie may depend not only on its performance in the theatre but also on the channel showing it. The results appear to show that in the intermediate rights market the bargaining position of the purchasing broadcasters is stronger than is commonly thought.

The fall in the prices of film rights that occurred in Europe between 2001 and 2003 may be linked not only to the crisis in the advertising market but also to the reduced capacity of films to pull audiences due to increased usage in the previous windows.

Although our test was confined to the television sector, the fact that viewer demand for movies can depend so markedly on the general appeal of the channel showing them could have implications for the new distribution channels as well, although on the contrary they appear to be relying on the attraction of programs with strong content, such as films or sport, to encourage consumers to adopt new access and distribution systems.

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