Creativity at Work:

Creative Encounters in the Film Industry: Content, Cost, Chance, and Collection

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Abstract

This Working Paper argues that the film industry is a paradigmatic example of how the organization of the cultural economy is shaped by balancing creativity with contextual issues. In the film industry, organization is far from determined only by creative concerns for content production: Issues of cost, chance and collection also play important roles. Through analyzing creativity and its context in the film industry, the paper explains the industry's organization, and opens up for understanding its significant national and regional differences. The paper carries out a literature study of economic, socioeconomic and economic geography literature on the film industry, analyzing the importance of creativity, cost, chance and collection in the film industry, and exemplifies how these issues are balanced differently in different clusters. The analytical framework presented in the paper may be used to understanding different "models" of filmmaking.

Keyword

Creativity, film industry, organization, innovation, transaction costs

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1. Introduction

The issue of creativity is not just at the heart of research on cultural industries (e.g., Caves 2000; Hesmondhalgh 2002), it is also becoming part of a broader agenda related to technological innovation, the rise of "the knowledge economy", and labour market dynamics (e.g., Florida 2002). It is a common theme in these literatures that the issue at stake is not really the creativity of single individuals, because this is a raw material in quite some abundance. It is how firms, industries, and society at large organize for creativity that is a core issue, and the challenge is for managers and policymakers to opt for the most efficient organization in order to profit from the creativity of labour and citizens. In the case of cultural industries, therefore, the key issue is how firms, labour markets, and industries are built around the raw material constituted by "creatives", i.e., individuals with cultural (as well as technical) skills. However, as noted by Richard Florida (2002), firms and industries do not just organize for creativity: a range of other concerns — for example, of control — is always balanced against creativity, and strategies and organizations reflect how this balance is made and unmade. Arguably, this is also true for cultural industries: contrary to popular belief, cultural industries are not only organized to maximize creativity, creativity is very often balanced with other factors. Hence, to understand the organization of cultural industries we must study creativity in context. By taking this into account, the study of cultural industries may well become inspirational to the study of creativity in other industries.

This paper seeks to do just this. We pick an extreme case of a cultural industry where creativity is balanced with other concerns: the film industry. In the organization of this industry, creativity is traded off against contextual issues — even to the extent that creativity is often subsumed under other concerns. Through analyzing creativity and its context in the film industry, the paper explains the industry's organization, and opens up for understanding its significant national and regional differences.

The paper is conceptual, carrying out a literature study of economic, socioeconomic and economic geography literature on the film industry, analyzing the importance of creativity, cost, chance and collection in the film industry, and exemplifies how these issues are balanced differently in different clusters. Hence, the paper develops an analytical framework that may be used for understanding different "models" of filmmaking in future comparative work on the film industry, but also as inspiration for other work on cultural industries.

The paper is structured as follows. Section 2 presents the film industry, and sketches out how different film clusters of the world perform very differently in economic terms. Section 3 calls for a study of organization, and of creativity in context, in order to understand these persistent performance differences of the film industry. Section 4 presents the first part of the analysis of what drives organization in the film industry, by discussing how creativity is balanced with concerns of cost. Section 5 discusses how creativity is also balanced by concerns of compensating for chance elements in the demand for films, and section 6 presents the last part of the analysis, discussing the balance of creativity with concerns of collection. A short section 7 summarizes the analytical framework and concludes the paper.

2. Economic Development and Performance Measures in the Film Industry

The film industry is measured by its annual turnover of more than US$25 billion in 2006 (MPAA 2007), the largest of the sectors in the cultural economy, and, in terms of global penetration and shaping of identities the most prolific (Hesmondhalgh 2002; Scott 2005). The film industry can be viewed as a paradigmatic case for a broader understanding of the development of cultural industries. On one hand, it shares its maturity and the nature of its product development processes — dominated by variety creation more than innovation (Lorenzen 2007) — with many other cultural industries, such as music, publishing, and arts. On the other hand, it is undergoing changes that may point to the future for other cultural industries, with increasing rates of product development, including stylistic and product innovations, as well as changes in its organization in terms of globalization, the performance growth of new clusters, and horizontal integration. Hence, the need for understanding the film industry is more acute than ever.

The film industry is truly global. At the beginning of the 1900s, countries as different as France, Denmark, India, and the USA undertook film production and sales on a large scale, but with the growing importance of mass marketing during the latter half of the 1900s, US film production underwent significant organizational changes and became the most commercially successful. With a few notable exceptions in the UK (which is highly intertwined with US film production (Galina and Pratt 2007) and Asia, film production outside the USA is today small-scale. At this point, we should note that even if national regulation − in the guise of, for example, tariffs, trade policy, tax, education, censorship and subsidies − greatly impacts the film industry (Moran 1996; Segrave 1997; de Turegano 2006; Flew 2007), the film industry has a distinct geography. The industry consists of *production* activities (preproduction [scripting, budgeting, casting, art design, etc]; production [shooting); and postproduction [editing, effects, scoring and sound]); *marketing*; *distribution* (i.e. sales and physical transport to cinemas and video, other sales channels); and *exhibition* (cinemas, video retail, TV, etc.) (for a more thorough presentation of these activities, see e.g. Vogel 2003; Wasko 2003; Eliashberg et al. 2006). Exhibition is localized where consumers are, but film production, marketing and distribution firms are to a wide extent clustered in major cities, and there are huge and consistent differences in output as well as in organization between these urban film clusters. Even if analysis of the national film industries of, for example, India, USA, Japan, France, UK, Italy and Denmark is interesting, even more insights are yielded by analyzing clusters in Bollywood (Mumbai), Hyderabad, Chennai; Hollywood (Los Angeles), New York; Kyoto, Tokyo; Paris; London; Rome, Copenhagen, and so on.

There are, as mentioned, notable differences between the performance and organization of the world's film clusters. The first global mass medium, film, continues not only to have a huge cultural impact, but also to be an industry with a notable potential for economic development. When that is said, how do we measure a cluster's potential for economic development?

Revenues

Measuring the revenues of film firms is a direct way of measuring national or regional economic performance. With US accounting for almost half of the world's box office (Screen Digest Newsletter 2007) and with the film production companies with the highest revenues (such as Universal, 20th Century Fox, Paramount, Columbia, MGM, Warner Bros., and Walt Disney) located in Hollywood, this cluster is the undisputed world top performer in terms of revenue collections. Kyoto/Tokyo (Japan) and London (UK) follow. Unfortunately, even if organizations such as the *Motion Pictures Producers' Association of America* and *European Audiovisual Observatory* seek to collect comparable statistics from national statistical offices and consultancy agencies (such as *Screen Digest* and *Nielsen EDI*), statistics are poor and difficult to compare across countries and regions (and the measurement of revenues is further complicated by the fact that media corporations and distributors register their turnover in other countries than films were revenues are produced).

Employment

While the number of jobs in the film industry captures economic performance in terms of economic activity, it does not necessarily indicate it in terms of economic growth, as employment is not necessarily a sign of revenue collection. While Hollywood, Bollywood and other Asian film clusters are biggest in terms of size of their labour pool and number of jobs, a range of film clusters undertaking runaway production tasks (Wasko 2003), typically outsourced from Hollywood, now experience booming employment. Examples are Vancouver (Canada), the Gold Cost (Australia) and Wellington (New Zealand), all undertaking the late stages in preproduction and shooting (Coe 2001; Coe and Johns 2004; Scott 2005; Flew 2007), and Manila (Philippines) and Bangalore (India) undertaking animation, EFX and postproduction. However, these clusters typically release few or no films themselves, and the outsourcing production companies, typically in Hollywood, London, or Bollywood, capture the rights to, and hence the revenues from, the finished products.

Releases

The total number of films released first and foremost reflects market size in terms of exhibition infrastructure (number of screens), cinema attendance, and purchase power. With huge home markets, clusters in India, USA, Japan, and China release most films annually (see *Table 1*). The clusters with the biggest markets have typically bifurcated their film releases: in addition to the many films produced for niche audiences (e.g. art house or religious films, documentaries, or more mainstream films failing to reach mass audiences for reasons we shall discuss later), these clusters also release a lower number of films targeting mass audiences. Even if fewer in number, these films account for the bulk of revenues. The hugely successful mass market segments of Hollywood and Bollywood films are best known, but we see bifurcation into niche vs. mass market mainstream films in most clusters with a high number of releases.

However, a large number of film releases does not necessarily indicate that a cluster has developed a commercially successful mass market segment, nor does it point to performance in terms of competitiveness or revenue collection. Due to state subsidies, clusters in some small European countries release an impressive number of films — in fact, Iceland, Denmark, Switzerland and Sweden release many more films per capita than non-subsidized and commercial clusters elsewhere.[1] Hong Kong is a rare example of a non-subsidized film cluster releasing many films per capita (in 2005, only Iceland released more per capita) (see *Table 1*).

Table 1: Film releases

Number of films released 2005	**Number of films released per million capita 2005**
1: India (1,041)	1: Iceland (10.17)
2: USA (699)	2: Hong Kong (7.98)
3: Japan (356)	3: Denmark (7.58)
4: China (260)	4: Switzerland (6.48)
5: France (240)	5: Sweden (5.99)
6: Russia (160)	6: Slovenia (5.04)
7: Spain (142)	7: Luxembourg (4.39)
8: UK (124)	8: Norway (4.18)
9: Germany (103)	9: France (3.96)
10: Bangladesh (102)	10: Spain (3.28)
13: Korea (82)	14: Japan (2.79)
16: Hong Kong (55)	19: USA (2.36)
21: Denmark (41)	22: UK (2.06)
	24: Korea (1.70)
	38: India (0.93)
	64: China (0.20)
Source: ScreenDigest (2006)	

[1] Munich (Germany) is another subsidized cluster that has also been releasing an increasing number of films per capita during the last decade (Kaiser and Liecke 2007).

Home market share

Releasing many films per capita does not necessarily entail capturing large home market shares (often measured as domestic films' share of gross box office revenues in the home market, and also called "self-sufficiency ratio"). Home market share measures economic performance in terms of different kinds of competitiveness. First, competitiveness in terms of the experience value (see section 4) of the content of films can be important for winning the home market. State subsidies and high-value content of films have allowed French, Danish, and Italian clusters to successfully compete against imports, capturing notable shares of their home markets (see *Table 2*). Second, competitiveness in terms of a protected position through trade policies or language barriers may also lead to large home market shares, as is the case for film clusters in India and China and the Seoul (Korea) cluster. Third, a large home market share may also be a sign of competitiveness in terms of marketing and distribution capabilities. The unmatched home market share of Hollywood has been achieved through a combination of home market protection, high production values of Hollywood mass market films, and Hollywood firms' unparalleled marketing and distribution capabilities.

Whether big home market shares result in notable economic development depends upon the purchase power of the home market. The wealth of the US home market compared to markets in India and China explains why the high home market shares and many releases of Indian and Chinese clusters do not translate into economic growth comparable to Hollywood's.

Table2 : Home market shares

Share of home market 2005
1: India (94.1%)
2: USA (93.4%)
3: China (60%)
4: Korea (57%)
5: Turkey (41.4%)
6: Japan (41.3%)
7: France (37.7%)
8: Thailand (35%)
9: UK (34%)
10: Hong Kong (31.4%)
11: Denmark (30.1%)
Source: ScreenDigest (2006)

Exports

Arguably, a film cluster's exports have a notable economic development potential, as exports capture revenue and prolong windows of earning beyond the home market. Of course, the economic potential of exports depends upon the ratio of the purchase power of home vs. export markets: a cluster with a poor home market may increase its revenues notably by a modest increase in exports to rich markets, whereas a cluster with a rich home market exporting to poorer markets needs a sizeable increase of exports (and possible an increase in the number of export markets) in order to increase revenues significantly (Hoskins and Mirus 1988; Hoskins et al. 1997; Vogel 1998) For example, Bollywood's recent export growth may be modest, but it aimed at a few rich Western markets and caused a revenue boom. By contrast, Hollywood's export revenues were built up over many years and entailed a lot of investments in many markets, because purchase power outside the USA is relatively low.

Exports indicate competitiveness of a film cluster in several dimensions. First, export may indicate the competitive content of films. This is reflected in the list of major exporters to the combined EU-US markets in 1999 where Belgium, Brazil and Denmark are featured prominently (see *Table 3*). However, exports based on film content alone may fluctuate a lot from year to year. For clusters with a low number of releases, export rates are highly influenced by single, successful films (as was exactly the case in 1999 for Belgium, Brazil and Denmark in *Table 3*). Second, exports may also reflect a cluster's cultural competitiveness, or the preferences of consumers for particular film narratives, aesthetics or, more simply, language (Hoskins and Mirus 1988; Papandrea 1998; Doh 2001). A look at the EU (12) market in 2004 indicates that, while USA still has the undisputed highest market share (71.4%), France (9.5%), UK (6.1%), Germany (4.5%), Italy (2.2%) and Spain (2.1%) capture audiences with other preferences than English language and Hollywood-type narratives (Newman-Baudais 2005). However, 1999 figures (*Table 3*) show that outside the home market, UK is a stronger European exporter than France: cleansed for home market sales, big-budget, English-language films produced in USA and UK capture the greatest share of the combined EU-US market. Third, exports of course also reflect a cluster's competitiveness in terms of capabilities. As any cluster typically exports only a fraction of its releases, a strong global distribution network is essential to match indigenous films in various markets, and good marketing is important to overpower them.

However, a high export rate (typically measured as the percentage of revenues stemming from export markets) does not unequivocally indicate that a cluster has developed content-based, cultural preference-based, or capability-based export capabilities. This is because many film clusters enjoy state subsidies, not just for production, but also for export activities. In the EU, there is governmental export support at EU level, for both smaller and larger film clusters (de Turegano 2006), and in Asia, Hong Kong is also beginning to attract government export support. Even if the world's most exporting film cluster, Hollywood, operates without government subsidies, its export success has been positively influenced by government regulation. Because exports would boost domestic scale economies, the US State Department, the Department of Commerce, and various US embassies have traded strategically in film and paved the way for US film exports to Europe through the Marshall aid and EU disputes, and to Asia through GATT (Segrave 1997; Ulff-Møller 2001; Scott, 2005).

Table 3: Exports

Admissions (cleansed for home market admissions) on the combined US-EU markets 1999
1: USA (536,7 millions)
2: UK (103,5 millions)
3: France (27,8 millions)
4: Italy (24 millions)
5: Japan (18 millions)
6: Canada (7,5 millions)
7: Spain (6,5 millions)
8: Hong Kong (4,8 millions)
9: Germany (4,3 millions)
10: Denmark (3,1 millions)
11: Brazil (2,4 millions)
12: Belgium (1,7 millions)
13: Russia (1,4 millions)
14: India (1,3 millions)
Note: Apart from USA, UK, France and India, size of exports was determined mainly by the success of one film.
Source: European Audiovisual Observatory (2006)

3. Organization and Performance

Performance differences

Not surprisingly, Hollywood stands out as the top performing film cluster in most of the dimensions mentioned above. Even if several Asian clusters employ more people and the clusters in India release more films, Hollywood has many releases not just on a wealthy home market where it completely dominates, but also on all global markets, including those with highest purchase power: Japan and the EU (Segrave 1997). This translates into revenue. As mentioned, clusters in Kyoto/Tokyo (Japan) and London (UK) are next best performing with respect to revenues, but because of the distribution of two other performance measurements, the position of these clusters may be eroding. First, the rapidly growing purchase power on the home markets completely dominated by

Indian and Chinese clusters is in the process of raising the revenues of these clusters. Second, the rapidly increasing export rates of a range of European as well as Asian clusters are stealing market share from London as well as Hollywood. Given the modest number of releases of Hong Kong and Seoul (Hong Kong had 55 and Korea 82 in 2005 [Screen Digest 2006]), the recent export boom of these clusters hardly threatens London or Hollywood. However, the slow but steady export rise of the hugely productive Bollywood cluster, moving beyond its traditional Asian and African export markets and successfully targeting EU and North America, may turn this cluster into a future major player with respect to economic development (Lorenzen and Taeube 2007).

What is the cause for the performance differences of film clusters? As hinted at above, four factors *external* to the clusters play a role. First (in some cases) FDI influences employment. Second, cinema attendance and purchase power on home markets precondition the number of film releases. Third, cultural consumer preferences on foreign markets influence exports. And fourth, public policy plays a role for the home market share and exports of many, if not all, film clusters. However, external factors alone cannot explain performance differences. Concerning the first external factor, FDI, what determines if a cluster receives or makes it? Why is Manila a recipient of FDI and Bollywood an investor, when both clusters have sizeable labour pools and low labour costs? Second, concerning home market size, what determines whether a cluster takes advantage of it? Why have Indian film clusters invested more in exhibition infrastructure (cinemas) than Chinese when India has fewer inhabitants with lower purchase power; and why does Bollywood release more films than Hollywood when USA's cinema attendance and purchase power is much higher than India's? Third, what determines consumer preferences for imported films? Why do consumers in Korea prefer Hollywood films to films from Asia or France, with whom Korea has much more trade and interaction, and, by the same logic, why do consumers in Finland prefer Hollywood films to Swedish or Russian? And finally, why do some countries, like Denmark and Korea, seem to benefit so much more from public subsidies and promotion than others?

Integration and market organization

The answer to these questions is, of course, *organization*. Even if there may be external preconditions for employment, the number of releases, home market shares, and exports, it is the internal organization of the film clusters that determines if they benefit from advantageous external conditions, or even invest in slowly changing them. Furthermore, organization greatly influences the major determinants of home market share and exports: the content (experience value) of films, and the marketing and distribution capabilities used for selling films. According to Wildman and Siwek (1988) and Wildman (1995), it was the *horizontal integration* and scale economies in Hollywood's production activities that made this cluster win large home market share and export so much. Hoskins et al. (1997), on the other hand, suggest that it was Hollywood's *vertical integration* of production, distribution, and exhibition, which was the key driver of US dominance on world film markets. This dominance may become self-reinforcing through cultural advantages. Gradually, if a powerful horizontally and vertically integrated film industry sinks sufficient investments into marketing and distribution over sufficiently long time, it may change consumer preferences in foreign markets (Hoskins and Mirus 1988; Vogel 1998; Elberse and Eliashberg 2003). The preferences on many national markets for English language films over other foreign language films (Doh 2001), and for Hollywood-type narratives and aesthetics, have been created by Hollywood itself. The greater cultural differences there are among the world's other exporting film clusters, the greater the cultural advantages of Hollywood (Papandrea 1998).

This issue of integration — whether firms choose to internalize particular tasks and transactions through ownership and long-term employment contracts — is classic in the economics of organization (Coase 1937; Williamson 1975; 2000). But organization is not just a question of where the boundaries of firms (hierarchies) go; it is also about how, in the *absence* of integration, firms "organize the market" instead (Richardson 1972; Langlois 1986; Maskell and Lorenzen 2004). Market organization encompasses the institutions other than ownership that may coordinate and manage tasks and transactions *among* firms, such as projects, alliances, and social networks.

Even if home market size, policy, and so on, also play important roles for performance differences between clusters, the clusters' differences in terms of the extent and nature of horizontal integration (scale), vertical integration (joint ownership of several activities in the value chain), as well as the extent and nature of transactions among firms and people in projects, alliances, and networks (for example, recurrence, collusion, and whether they are strategic or short-term), take centre stage.

Creativity and its context in organization

So, what drives organization? Why are different clusters organized differently? In the sections that follow, we analyze the factors behind organization in the film industry. Recently, scholars have dedicated growing attention to the role of *creativity* in cultural industries — the volume to which this working paper has been submitted being an example of this research strand (see also Caves 2000; and Hesmondhalgh 2002). Creativity is also controversial among cultural industry observers, some arguing for the growing importance role of creativity ("content is king"), some arguing in the opposite vein that in the organization of mass-consumer cultural industries, creativity has long been subsumed under other concerns.

The following analysis of the film industry suggests a middle way. It argues that creativity plays a necessary role for the organization of the film industry, but that there are different ways of trading creativity off against logics of cost, chance and collection. We will here sketch how the film industry organizes for, around, and some times against, creativity. This shapes the different organization, and ultimately performance, of the world's film clusters.

4. Creativity vs. Cost

Creativity: Project organization of production

Cultural consumer industries (such as music, games, publishing and arts) produce *experience goods* (Nelson 1970), in the sense that even if products are often developed with much involvement, dedication and integrity of creative labour or even artists, their market value ultimately hinges upon how their content is experienced by consumers (Pine and Gilmore 1999; Cowen 2000). The film industry is no exception, as the market value in cinemas, TV, and video of its core product, the feature film[2], depends on how the audience judges the narrative and aesthetic content of the film. This judgment, and hence the market value, of a film is related to the degree by which the aesthetics and narrative of its content *differentiate* themselves (Burke 1996) from incumbent films on the market. To have experience value, a film needs to differentiate its content in terms of both narrative and aesthetics: a differentiated aesthetics, obtained through a particularly high production value or a stylistic innovation, applied to a well-known narrative, has often proved valuable.

The film industry produces differentiated content by differentiating creative inputs. A film is an immensely complex product, integrating numerous art forms (such as writing, design, and performing arts), and the scope for combining the inputs in order to achieve new content varieties are, in Caves's (2000) words, infinite (see also Eliashberg 2006). Most content development of films is in reality the production of *variety* through recombining inputs (and proper innovations in the guise of new styles or whole new ways of marketing or distribution are rare) (Lorenzen 2007). In order to thus recombine inputs, films productions are organized as *projects* — temporary and flexible groupings of skills and other inputs with given budgets and deadlines (Lundin and Söderholm 1995; Hobday 2000; Lorenzen and Frederiksen 2005) and the end goal of producing a feature film.

The necessary skills for a film project are often so specialized into narrow creative, technical, and managerial realms that they are held by individual experts: creatives (e.g. writers, designers, choreographers, actors, directors), technicians (e.g. editors, cinematographers, lighting technicians) and managers (e.g. producers, line producers, controllers, accountants, financiers, and marketers), working concurrently and successively on a film (Wasko 2003; Eliashberg et al. 2006). A film project is typically set up and controlled by a production company where the producers, marketers, and sometimes the financiers, are long-term employed.

Creativity: Horizontal disintegration of production

In the pre-WWII period, cost concerns typically overrode creativity in the

[2] Definitions of "feature film" vary, but the US Academy of Motion Picture Arts and Sciences define it as a film longer than 40 minutes.

organization of film projects. As a result, not just managers, but also creatives and technicians, were employed long-term in large "studios" — a somewhat misleading term, as these production firms integrated all aspects of production, not just studio facilities. Prior to WWII, there were integrated film producers in many different clusters, including Copenhagen (the integrated film company Nordisk Film), Paris (the companies Gaumont and Pathé) Bollywood (Prabhat, Wadia, Bombay Talkies and other companies), and of course Hollywood (the "seven sisters" − Columbia, Walt Disney, 20th Century Fox, MGM, Paramount, Universal and Warner Bros.). The advantages of this horizontal integration of production was mostly in terms of planning of resource use with parallel film projects, and Hollywood, with the biggest home market and number of release of all clusters, was able to make the most out of such scale economies (Wildman 1995). Scale of production also encompassed re-use of concepts and brands in successive projects: the integrated film companies had huge success with producing low-budget films and serials (for example, Bollywood's *Fearless Nadia* and Hollywood's *Kings of Comedy* series) (Chisholm 2003).

TV, which was introduced on a large scale in the US in the 1950s, in Europe in the 1960s, and in most parts of Asia in the 1980s, quickly took over the market for low-budget films and serials (Chisholm, 1993; de Vany and Eckert 1991; de Vany and Walls 1999). In addition, the increasing purchase power and heterogeneity of markets in the US and Europe since WWII has changed demand for films: film audiences now wanted high production value and high product variety. This demand for variety, and hence for more varied inputs to projects, undermined the internal economies of planning and carrying them out in-house (Lorenzen and Frederiksen 2005). The profits of the integrated production companies in Europe and Bollywood had already been eroded by WWII, Bollywood's incumbent production companies saw a huge entry after Indian independence, and the business model of Hollywood's integrated production companies — combining horizontal integration of production with vertical integration of distribution and exhibition (see the section below) — was punctuated by an anti-trust High Court ruling in 1948. As a result of these combined pressures, after WWII, production disintegrated in many of the world's film clusters, into a flexibly specialized production model of small-scale independent production firms and numerous specialized suppliers (Robins 1993; Storper 1989), and a labour market of freelancing creatives and technicians (Faulkner and Anderson 1987; Storper and Christopherson, 1987; Blair 2001). This model allowed for much higher variety of film aesthetics and narratives, and in Hollywood, the growing skill levels of specialized suppliers also raised production values.

The horizontal disintegration of production was also spurred by the integrated production companies' problems of motivating labour in long-term employment. New small production companies and a thickening labour market offered both creatives and technicians attractive freelance alternatives to long-term contracts: Freelance work, or the option to start up own companies. The tendency to go freelance was most prominent for star actors, and from the 1950s, they broke out of their long-term contracts with production firms in many clusters, including Hollywood and Bollywood. The disintegration of production was thus the beginning of an era where star actors became independent, but also (as shall be discussed in the next section) powerful.

According to classic economic logic (Smith 1776), the horizontally disintegrated system of production should make those world's film clusters with the largest labour pools, such as Hollywood, Paris, London and the clusters in India, particularly competitive with respect to creativity. The size of their internal market for projects and labour should, *ceteris paribus*, allow for the high specialization of firms and labour, and hence deepening of firm competences and labour skills. Even if it may be subject to controversy whether all clusters take due advantage of the potential for creativity offered by the size of their labour pool, it is true that the film clusters that perform well in terms of number of releases have sufficient reputation to create significant backwash effects for talent. Hollywood, Bollywood, Paris and London remain magnets for film talent from a regional or even global hinterland, constantly adding to these clusters' stock of specialized firms and the density of their labour markets. However, with targeted (often public) investments in education, some clusters that are smaller in terms of both employment and number of releases are able to boost skill levels beyond what their size would allow for in a pure market logic. For example, public education in the Copenhagen and Rome clusters has made skills in scriptwriting and direction at least at par with the huge market-driven cluster of Bollywood, where investments in public film education are very modest.

Cost: Horizontal ecologies and small world networks of production

A disintegrated organization of production is beneficial to creativity in the film industry, but also raises the question of how production companies may manage film projects that cross the companies' boundaries, using more freelancers than long-term employees. In the design of projects "on the market" (Lorenzen and Frederiksen 2005), there seems to be a trade-off between maximizing creativity and minimizing transaction costs. The optimal design in terms of variety and differentiation *vis à vis* earlier projects is to use as many *new* creative (and possibly also technical) skill holders as possible. However, the creative benefits of using new skill holders must be balanced against the costs of using strangers who may shirk or cheat (Williamson 1975; 2000). To minimize such transaction costs, it makes better sense if the producer signs creatives and technicians with whom he has a relation because they have worked with him before.

This trade-off between creativity and cost is typically solved by producers through social networks. Producers sign new people who they may not have worked with before, but whom they can find and whose past performance they can check, through relations to other people who *have* worked with them before. This informal way of hiring, checking and controlling new people is possible because of the geographical clustering of film production and labour markets. Film clusters are project *ecologies* (Grabher 2002) of skill holders who are constantly combined and recombined in new film projects. Because of this constant recombination of people, ecologies get socially structured into dense and ever-growing *social networks* constituted by friendships and acquaintanceships made in earlier film projects. In such networks, reputation effects and sharing of information may allow participants to a new project to achieve swift trust (Meyerson et al. 1996), even if none of them have worked together before. There is evidence for how film projects are thus based on social networks in Hollywood (Baker and Faulkner 1991; Sorenson and Waguespack 2006); Rome (Soda et al. 2004; Delmistri et al. 2005), and Bollywood (Lorenzen and Taeube 2007).

We argued earlier that film clusters with big labour pools have particular creative potentials, by virtue of the size of their internal markets for labour and projects. We can now see that whether a film cluster realizes its potential for taking advantage of its variety of local competencies and skills depends upon the social structure of its project ecology. If the social networks of the cluster are in collusion, there is much re-use of skill holders, and less variety of film aesthetics and narratives. If the social networks, on the other hand, provide access to many new skill holders in each new film project, creativity may blossom. The bifurcation of clusters with many film releases into a segment of niche films and a segment of mainstream films also typically means social bifurcation — the rise of one network of skill holders who mainly participate in the production of niche films, and another network of skill holders who mainly participate in mainstream film production.[3] If these two social networks are cut off from each other, bifurcation entails a division of a cluster's project ecology into smaller and less varied markets for labour and projects. If, on the other hand, the social networks centered around niche and mainstream film segments, respectively, are coupled to each other by a few central people who work in both film segments, such as eclectic actors or directors, the cluster's ecology is socially structured so that it allows for higher creativity. The coupling of different internally densely knit social networks to each other through a few crucial social relations is called a *small world network* (Milgram 1967; Watts et al. 2002). In a film cluster, such a social structure allows for minimizing transaction costs in the majority of project relations (which are carried out internally in dense networks where people know about each other and can easily build trust), while boosting creativity in a few crucial project relations that cross over to other networks and access the information and skills found here (Granovetter 2005; Uzzi and Spiro 2005). As will be discussed below, while Bollywood has historically been more of a collusion than Hollywood, as its mainstream network was relatively closed to outsiders, Hollywood is now moving towards more collusion while Bollywood is opening up. Bollywood may be moving towards greater creativity and Hollywood towards less.

[3] In Hollywood, there is even evidence that there is a third network of skill holders related to porn films, clearly distinguishable from the networks of skill holders involved in mainstream and niche non-porn films.

Cost: Outsourcing
While transaction costs may be kept at bay through social networks, even with horizontal disintegration, production costs of most film projects have exploded over the last decades, due to the demand for ever more production value and the salaries of star actors (see below), in combination with the lack of scale economies of planning after the horizontal disintegration of production. Several of the clusters with big-budget productions, including Hollywood, London, and Bollywood, are now outsourcing labour-intensive production tasks to clusters with lower labour costs, such as Vancouver, Australia's Gold Cost, and Wellington. This "runaway" mode of organization (Wasko 2003) mostly concerns the technical aspects of production, leaving creative tasks in the home cluster. While this growing aspect of the organization of the film industry thus influences creativity of the outsourcing clusters little, it also bears only modest development potential for those clusters receiving runaway production tasks (as mentioned in section 2, see Coe 2001; Chaminade and Vang 2007).

5. Creativity vs Chance

Chance: Horizontal network collusion and integration of production
Like other cultural products, films have a highly uncertain demand. In film clusters as different as German (Jansen 2005), Indian (Kohli-Khandekar 2006; Lorenzen and Taeube 2007), and US (Vogel 1998; de Vany and Walls 1997; de Vany 2004; Eliashberg et al. 2006), less than 20 per cent of films break even, and much fewer make notable revenues. The demand for art house or other niche films is limited, but it varies on a relatively predictable scale (Cameron 2003). It is mass markets that are really uncertain. Growth, globalization, and increased consumer spending on experience goods since WWII have created global mass markets for feature films with potentially huge revenues, and this has facilitated the rise of mass market film segments in the clusters with most releases. However, mass markets are also characterized by unforeseeable — and rapidly changing — consumer tastes and infinite variance of revenue distribution (de Vany and Walls 1997; Sawhny and Eliashberg 1996; Walls 2005). Hence, in mass markets for films, "nobody knows anything" about demand (a phrase coined by the scriptwriter Goldman [1983] and empirically addressed by a range of scholars, for example in a 2005 special issue of *Journal of Cultural Economics*).

Economists of an evolutionary stance (e.g. Nelson and Winter 1982; Rosenberg 1992) often associate demand uncertainty, producing and marketing to the firm-level process of *experimentation*: developing new products without whether they will sell or not, and subsequently testing them on consumers over limited (if often flexible) test periods (Raubitschek 1988; Kerke and Srinivasan 1990). Such experimentation with producing mass market films can be costly. With life cycles of mass market films shortening (the dramatic shortening of a film's life span in movie theatres has not yet been compensated for by the prolongation of windows of earning on TV and video), there is significant pressure on production companies within the mass market segments to develop new films at a rapid pace, which further increases the potential costs of experimentation. Consequently, the incentives for production companies in the mass market segment for *compensating* for the aspect of chance are great. This impacts upon the organization of not just the mass market segment, but the entire film industry.

One means of compensating for chance is the use of *stars* — that is, creatives with proven consumer appeal and high brand value — in the production and marketing of mass market feature films. Worldwide, the most prominent stars are actors, but to some extent, directors (and, in Bollywood, composers) are also gaining star status. Contrary to common belief among film producers and marketers, there is little evidence that star actors systematically increase the likelihood of box office performance (de Vany and Walls 1996; 1999; 2004). However, their brand value for attracting investments remains huge in Hollywood as well as Bollywood (de Vany and Walls 1996; 1999; Elberse 2006; Lorenzen and Taube 2007), and their salaries have increased to constitute half of some mass market films' budgets. A disproportional number of film projects centres around the most branded star actors and directors (some stars are even in a position to fund and produce own film projects). However, this centering does not necessarily inhibit creativity. Quite the opposite, the use of stars may reinforce the small world properties of a cluster's social network. For example, in both Hollywood and Bollywood, some star actors or directors who are highly paid in the mass market segment occasionally work for much less in more artistically satisfying projects in the niche segment, thus coupling the skill holders in the two segments who are otherwise segregated into a small world network.[4]

Another means to compensate for the element of chance in demand for mainstream films is by producing *sequels.* Whereas stars are used in both mass market and niche films, the production of sequels is a strategy used almost exclusively in mass market films. As mentioned, the use of stars alone does not efficiently compensate for chance. However, the re-use of a star cast in combination with the brand value of a previous box office success has proved a much more successful success formula (Elberse and Eliashberg 2003). Today's serials do not resemble the low budget productions of Hollywood and Bollywood 50 years ago: *Spiderman 2* or *Pirates of the Caribbean 2* are top of the range productions, with the most expensive stars, lavish production value, and often technical virtuosity. Their box office success notwithstanding, as sequels prioritize brand value over novelty, they also prioritize compensating for chance over creativity. They encompass not only the re-use of a star cast but also writers, directors, producers, and sometimes also designers and some technical staff, thus lowering the variety of narratives and aesthetics.

Chance: Horizontal integration of marketing — and vertical integration of production into marketing

[4] Folklore often describes Kevin Bacon as "the centre of the Hollywood universe", but actually, Rod Steiger has highest centrality in Hollywood's small world network, according to University of Virginia Computer Science Department's *Oracle of Bacon*, www.oracleofbacon.org/center_list.html

The box office collections of niche films depend mainly upon the films' content, and this content often encompasses widely varied narratives and novel aesthetics. Due to the limited budgets for advertising, niche films typically need to signal the experience value of their content at film festivals, through critical reviews (Caves 2000; De Vany 2004), and at award shows (awards being important for niche films on both big and small markets (de Vany 2004; Jansen 2005)). The ultimate aim for a niche film is to create sufficient word-of-mouth "buzz" and reputation to convince theatre owners and other exhibitors to take the film on. This slow and cheap mode of marketing of niche films corresponds to their long windows of earning and low collections.

The collections of mass market films, on the other hand, depend primarily on good targeting of particular audience segments (age, class, race, sometimes also religion), and good timing of release (as these films often target moviegoers at particular holidays and coordinate their timing to competitors' releases). The experience value of mass market films often encompasses high production value and/or formulaic narratives. Huge marketing campaigns signal this experience value of new releases to target audiences, aiming at creating hoarding effects (Caves 2000; de Vany 2004). Large-scale marketing also serves to achieve nominations for major commercial awards (but not necessarily winning them) (Deuchert et al. 2005), and ultimately convincing theater owners of the market potential of new releases, paving the way for exhibition at just the right time. In sum, large-scale marketing is an efficient means of compensating for chance (Prag and Casavant 1994; Eliashberg et al. 2006), and its value grows with market size (Lee and Waterman 2006).

There are notable scale economies in marketing, as the marginal costs of e.g. promotion campaigns decrease rapidly (Caves 2000; Chisholm 2003). The larger the market, the larger the endogenous sunk costs represented by marketing (Sutton 1991; Bakker 2005) and the more prominent the scale advantages: for example, Elberse and Eliashberg (2003) argue that Hollywood's large-scale marketing on the huge US home market forms a necessary platform for the global marketing of Hollywood films.

Due to these scale economies and sunk costs, the film industry often sees notable horizontal integration in marketing — the dominance of a few, powerful marketing firms. With respect to scale economies and horizontal integration, film marketing is very different from film production, which, for reasons discussed above, is organized in disintegrated projects. Hence, in many film clusters, production firms and marketing firms stay separate, the former employing the latter. However, in a few clusters with a big commercial segment, such as Hollywood and London, producers of mass market films have integrated mass marketing. The Hollywood pre-WWII major production companies did not just integrate production horizontally, they also integrated marketing, distribution, and exhibition vertically, and boasted large-scale marketing departments, distribution networks, and theatre ownership. As mentioned, demand developments and creative concerns after the 1950s led to the horizontal disintegration of production, and the 1948 US High Court ruling forced vertical disintegration of exhibition, but the major Hollywood film companies remained powerful in marketing and distribution (for a discussion of the latter, see below). They developed core competencies in finance, marketing, and distribution — outsourcing production to specialized subsidiaries or even to "independent" production companies, occasionally buying and marketing niche films with potential mass appeal. Such vertical integration of production with marketing is a costly, but also efficient response of a few powerful firms to the high demand uncertainty on mass markets, and as pointed out by Hoskins et al. (1997), this organization of Hollywood's mass market segment is a key explanation for the export success of this film cluster.

Ever since WWII, the growing marketing power and the gradual development into media conglomerates of these Hollywood major film companies have shaped the development of not just Hollywood, but the entire film industry. For the mass market segment, it represents a further compromise regarding creativity for the sake of compensating for chance: Producers of mass market films in, for example, Hollywood or the UK, who are also first and foremost marketing firms, focus increasingly upon marketing and are gradually less prone to experiment with variety. In the niche market segments, creativity is not compromised by this organization of the mass market segment, but, as will be outlined below, the competition for exhibition — and ultimately survival — in *all* of the film industry is significantly stiffened by the organization in the few large clusters' mass market segments.

Chance: Horizontal integration of distribution — and vertical integration of production and marketing into distribution

Distribution of niche films and mass market films functions quite differently. Because the main selling point of niche films is their content, they are often long in production and postproduction, and can take long after completion to find distributors targeting the right niche markets. The success of mass market films, on the other hand, is hugely dependent upon scale of exhibition and timing of release (which sometimes leads mass market films to be rushed through post production): opening in many screens simultaneously — "block booking" — is a way of propagating hoarding effects while crowding out competing films (Donahue 1987; Caves 2000). This means that efficient, large-scale distribution is immensely important to take advantage of mass marketing.

As in marketing, there are also advantages in large scale distribution, given the decreasing marginal costs of for example, physically transporting prints, and keeping contact with theatre owners (Caves 2000; Chisholm 2003). Scale — spreading risk over a large number of films — is also a means by which distributors can compensate for chance (Cameron 2003). Scale economies have driven integrated organization of distribution in smaller clusters, such as Denmark or Korea. Here, a few large distribution firms distribute for all production companies. The sunk costs represented by distribution are, like marketing, also endogenous, so *ceteris paribus*, larger markets should render horizontal integration efficient (Sutton 1991; Bakker 2005). However, this is not the case for all clusters with big home markets: whereas Hollywood is dominated by a few powerful distributors of mass market films, Bollywood continues to demonstrate disintegration, with hundreds of small-scale independent distributors.

One explanation for the horizontally integrated organization of distribution in Hollywood is that the media conglomerates which integrate both production and marketing have also vertically integrated into distribution, driven firm sizes up here, and raised entry barriers against newcomer distributors (Caves 2000). The reason for this vertical integration of production and marketing into distribution is simple: it is the ultimate way of compensating for chance. Controlling distribution, integrated production and marketing companies can ensure preferential treatment of their own films in the best (first-run) theatres (Vogel 1998) and systematically use block booking as competitive strategy (Hanssen 2000). The Hollywood media conglomerates have used these effects to a wide extent during the last two decades of the last century. As these conglomerates now also re-invest in exhibition (buying theatres as well as TV channels), hence compensating even more for chance while appropriating residual earnings from successful films (Chisholm 2003), scholars such as Schatz (1997) refer to "the return of the Hollywood studio system" of the pre-WWII period. Through their unique control over marketing and distribution, these new conglomerates are able to completely finance their own film productions, as well as ensuring them large-scale exhibition.

To the extent that media conglomerates also facilitate the distribution of niche films, horizontal integration of distribution, and vertical integration of production and marketing into distribution, does not necessarily negatively influence creativity as such. However, if niche films are denied distribution for strategic reasons, this organization of a film cluster adversely influences the diffusion of niche films produced with a comparatively high emphasis on a variety of inputs, narratives and aesthetics — and ultimately the survival of firms in the niche film segment. As we shall see below, in some film clusters, the distribution of collaborations between niche producers and media conglomerates is becoming rarer still.

Chance: Horizontal integration of production

With a scale sufficient to finance, market, and distribute own film productions (as well as the occasional "independent" film), the major Hollywood media conglomerates of the late twentieth century pursued a strategy of releasing different types of films simultaneously, compensating for chance by spreading risk across different films. While the high horizontal as well as vertical integration in the mass market segment of Hollywood put some competitive pressure on niche producers, there was, as mentioned, some collaboration between the segments, allowing for finance, marketing and wider distribution of the occasional niche film, and the maintenance of a small world social network coupling creatives across segments.

However, there are signs that the mass market segment in Hollywood and others among the big commercial clusters, such as London, is moving towards an organization that further prioritizes compensating for chance over creativity.

As mentioned above, mass market segments in many clusters currently produce a rising number of sequels, in an attempt to compensate for chance. Many sequels are also examples of a third recent strategy for mainstream films, *flagpole productions.* Earlier, managers and economists (e.g. de Vany 2004) agreed that budget size did not necessarily increase chances of box office success, but some of today's films with more than double the average production and marketing budget have proven able to sweep the tables, as well as create brand value for use in subsequent TV shows, video games, music, books, and so forth.[5] Given the size of their production budgets, as well as their necessary scale of marketing, distribution, and collection (see below), flagpole productions are only undertaken by the biggest film production companies that are a part of large media conglomerates. Over the last five years, the strategy of flagpole productions has added to the horizontal integration of production in Hollywood and the UK, because the big production companies tend to finance fewer, but larger productions. As flagpole productions are designed to minimize experimentation, and as they imply the integration of production, they clearly represent a strategy that prioritizes compensating for chance over creativity. As documented by Scott (2005), in Hollywood, this results in collusion and still less coupling between the parts of the bifurcated cluster, with fewer films — and more of them own productions — financed, marketed and distributed by major conglomerates, and niche producers left with still more difficulties in achieving finance, marketing, and distribution. However, Bollywood looks a bit different: even if flagpole productions are now also seen here, the cluster's disintegrated industry structure means that this strategy does not lead to noteworthy changes in how creativity is balanced with compensation for chance in the cluster as a whole.

6. Creativity vs. Collection

Collection: Cross-industry integration

The basic value of feature films lie in the *property rights* to them, and the *collection* of the payment for using such rights has always been a part activity in film distribution. However, such rights, and collection on the basis of them, are becoming an increasingly complex and much growing business in itself (for discussions, see Caves 2000; and Andersen et al. 2007). Whereas for the first century of the film industry, copyrights — the use of rights to copies of the feature film — were central to earnings, a range of auxiliary revenue streams is now arising from further rights. The rights to parts of the feature film product are now also sold and re-sold. A classic example is soundtracks, but to an increasing extent, other parts of successful mass market films, such as the scripts (and re-make rights), characters, and art design, are also sold separately.

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[5] The average combined production and marketing costs of a Hollywood film was US$100.3 million in 2006 (MPAA 2007). *Spiderman 2* cost an estimated US$200 million and collected US$784 million worldwide. *Pirates of the Caribbean 2* cost an estimated US$225 million and collected over US$1 billion worldwide (IMDB.com).

This has created specialized firms in the guise of publishing houses, which typically administer, sell, and collect fees based on rights.

There are notable scale economies (diminishing marginal costs) in trading with and collecting fees from rights, and quite similarly to marketing and distribution activities, these scale advantages grow with market size. There are also synergies of selling use rights in bundles, and of targeting multiple outlets with bundles of rights. For instance, the rights to the storyline and character of *Spiderman* can be sold to TV production companies wanting to produce a show based on the feature film, toy and (computer) game producers, book publishers, and so on. Consequently, publishing houses are often big, they often administer rights not just in films, but also in music, plays, books, and more, and they have often grown to spanning globally.

Not surprisingly, the integrated media corporations in Hollywood and other large film clusters are also integrating into publishing. As the media conglomerates focus more and more on how they can collect from existing successful films (such as sequels and flagpole productions), they also focus upon the efficient administration of property rights to these films, creating and capturing as many auxiliary revenue streams as possible. Investing in the media industries where synergies of rights are most profound, US, UK, German, French and Japanese media conglomerates are now turning into *multi*-media conglomerates, integrating the production, marketing, distribution (and to some extent also exhibition) of films, TV, music, computer games, book publishing, and more (Litman 1998). The "return of the studios" (Schatz 1997) is in reality the rise of a new breed of global multi-media conglomerates, organized around rights and collection.

This increasing focus upon collection in the mass market segments of Hollywood and other of the big commercial clusters complements their increased focus upon sequels, flagpole productions, and brand value. As mentioned above, this also represents a shift in balance away from creativity, since the result is fewer mass market films with less variety, as well as higher entry barriers for niche films to marketing and distribution.

7. Summary and Conclusion

The sections above have sketched the main drivers of organization in the film industry. The basic argument is that different clusters' different economic performance in the film industry is related to how these clusters organize as a means of balancing concerns for creativity, cost, chance, and collection. As far space has allowed, the sections have also exemplified how different clusters balance these concerns:

- The concern for *creativity* — consumer demand for differentiation of content (aesthetics and narrative) — drives *project organization*. Arguably, this type of organization is ubiquitous in all film clusters.
- The concern for *creativity* — variety of inputs — drives *disintegration of production activities and use of new and varied freelancers and firms*. Whereas all clusters have functionally disintegrated production activities, the

major production companies in some of the biggest clusters maintain a relatively higher level of control over production than many other clusters, owning them or writing multi-film contracts with them.

- The concern for lowering transaction *costs* drives the emergence of *small world social networks* in project ecologies. But whereas some clusters are well coupled internally, others are less so, to some extent hampering creativity.
- The concern for lowering labour *costs* drives *outsourcing* from some clusters in high-wage countries to new peripheral clusters, but this impacts creativity little.
- The concern for compensating for *chance* in demand drives the increasing use of stars in most clusters, but as this may *strengthen small work network structures*, this has not *per se* an adverse effect on creativity.
- The concern for compensating for *chance* drives the increasing number of sequels in most clusters with mass market segments, and this leads to *network collusion*, impacting adversely upon creativity.
- The concern for compensating for *chance* drives *horizontal and vertical integration of marketing* in Hollywood, and until recently, this has not hugely counteracted creativity.
- The concern for compensating for *chance* drives *horizontal and vertical integration of distribution* in Hollywood, and until recently, this has not had any major adverse effect on creativity either.
- The concern for compensating for *chance* drives the increasing number of flagpole productions in some clusters with mass market segments and hence increased *horizontal integration of production*, compromising creativity to some extent.
- The concern for *collection* of auxiliary revenues from multiple rights in different industries has created *cross-industry integration* and multi-media conglomerations in some of the world's biggest clusters, with potential negative impacts on creativity.

While film as a cultural endeavor is recognized as a global phenomenon, many film scholars have equated film as an industry with Hollywood. However, there is clearly not just a Hollywood industrial model of commercial filmmaking; there are other models. Even if all commercial filmmaking models balance creativity, cost, and collection issues, they do so in different ways. We have briefly exemplified how clusters in, for example, Bollywood; Hollywood; Kyoto/Tokyo; Paris; London; Rome, and Copenhagen have developed differently. Even if the drivers of organization are the same, chance and local historical events have set these clusters on different paths, and future comparative work should take on the challenge of systematically comparing them. The analytical framework presented in this paper is, hopefully, a useful tool for such cross-cluster comparisons in the film industry, but may also give hints as to how studies of the organization — and the historical development of such organization — in the world's cultural industries can be conducted in the future.

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August 2007

#4 **Hvilke kulturtilbud bruger den kreative klasse?**
By: Trine Bille
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