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ENTRY BARRIERS AND THE DEVELOPMENT OF A CANADIAN FEATURE FILM INDUSTRY

by

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ABSTRACT

This thesis examines the development of the Canadian feature film industry from the late 1960s to the present with special reference to efforts made to overcome entry barriers.

This thesis begins with a general review of the film industry, including experience outside Canada. Following this is a review of the general theory of entry barriers and the identification of their relevance to the film industry. Canadian difficulties in feature film production are then identified and the public policies adopted since 1968 are described and discussed. Finally policy alternatives are analysed.

Through this study several important barrier factors hindering Canadian feature film production are identified. On the production side, a general lack of financial resources and skilled producers are primary causes. On the market side, foreign competition, a small domestic market, and inaccessibility to distribution facilities play critical roles. The distribution problem is further aggravated by the vertical structure of the the industry.

Since 1968 two major public policies were adopted to help develop a film production industry. They were the establishment of the Canadian Film Development Corporation

and the adoption of tax incentive through a 100 percent capital cost allowance for film production. As a result barriers in the production side were largely removed. Seed-money for new productions was made available through the CFDC and the tax incentive spurred a vigorous response from the private sector to provide production finance.

Unfortunately, market access remains a critical concern. Canadian pictures experience great difficulties in getting to cinemas through the existing distribution and exhibition system. Even though there are more and more examples of success, most of the new productions end up as financial failures.

In conclusion, public policies have achieved remarkable success in the production area. But to develop a mature feature film industry, the distribution barrier has to be dealt with more effectively. Possible public policy alternatives include distribution through television and the redesign of the exhibition and distribution structure. Finally, the philosophy and direction of public policies should be redefined. A more workable balance between national-cultural values and commercial viability has to be achieved.

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Chapter 1

Introduction

In the field of documentary and educational film production, Canadian producers, with the National Film Board as the best example, have demonstrated a tradition of excellence and productiveness. The numerous awards and accolades accorded to the NFB bear witness to that evaluation. However, the feature film situation is completely different. The Canadian cinemas continue to be deluged with foreign film products. Canadian-produced feature films, especially English-language ones, are conspicuous by their absence. This is true even with the existence of a federal film agency, the Canadian Film Development Corporation (CFDC). This phenomenon raises questions about the viability of a truly Canadian feature film industry that would employ Canadian talent and would reflect Canadian cultural values.

The primary object of this paper is to examine the development of the Canadian feature film industry in the decade since the establishment of the CFDC in 1968. One of the main objectives of this examination is to identify the barriers which have been preventing feature film production activities in Canada. Then the examination of the industry will be focused on the efforts, both in the public and the private sectors, made in the period under review to overcome these barriers in an attempt to create a truly Canadian feature film industry.

As a basis for understanding the Canadian film production, however, it is essential to gain a broader perspective on the feature film industry. A review of the industry in general will therefore be done in a chapter which includes surveys of the film industry in both the United States and Great Britain. The reason for using the film industry experience in these two countries is that they share a common language with Canada and export films to Canada. The review should provide insights on the possibilities of increased Canadian feature film output.

To see the possible factors hindering Canadian entry into feature film production, general analysis is necessary. This is provided in a chapter devoted to a survey on current economic literature on the theory of entry. Subsequently, using the American film industry's experience, these theoretical tools are used to illustrate the entry barrier aspects of the feature film production in general. With this knowledge in hand, Canadian difficulties in this industry will be highlighted.

Having identified the Canadian difficulties, a chapter is used to examine and evaluate Canadian efforts, since 1968, to create a feature film industry. Emphasis will be put on attempts to overcome the various barriers to entry. Through this examination, it is hoped to provide insight on the current standing of the industry and to improve understanding of the developments in the decade reviewed.

Relevant conclusions will then be provided and comments made on the future development of the industry.

Chapter 2

An Overview of the Feature Film Industry

To facilitate understanding of the development of the Canadian feature film production industry, a general examination on the industry will be made in this chapter. Topics will include the economic and social importance of the industry as well as its structural organization. International experience will be drawn on for insights.

I. ECONOMIC ASPECTS

The overall importance of the film industry is not as great as the glamour of the industry might suggest. A comparison of the industry's revenue with the total personal expenditure on consumer goods and services in Canada will shed some light. This is shown in Table 2-1.

Table 2-1

Theatrical Receipts and Total Personal Expenditures

Canada

Year	Receipts ($ Million)	Personal Expenditure on Goods & Services ($ Million)	Percent of Total
1970	128.7	50,327	0.26
1971	n.a.	55,616	-
1972	140.0	62,208	0.23
1973	150.6	71,278	0.21
1974	175.7	83,388	0.21
1975	211.4	97,108	0.22

Source :
1. Statistics Canada, National Income and Expenditure Accounts, 13-201.
2. Statistics Canada, Motion Picture Theatres and Film Distributors, 63-207.

n.a. Not available.

The fact that the film industry contributes only marginally to the overall Gross National Product is also true in the United States where there is a fully developed film industry. Statistics show that in 1975, the $2.5 billion theatrical admission receipts is only 0.26 % of total U.S. personal consumption expenditures.[1]

Audience Characteristics

One of the unique characteristics of the motion picture is its capricious audience taste for its product. In a certain year, one genre of films may be preferred to the other. However, the trend may be completely reversed in the next year. It is this that make the producer's job of predicting future market preference for a certain type of film difficult.

Fortunately for the industry, the general make-up of the audience is relatively clear. The industry has generally been termed as appealing mostly to the youth market. It is noted that with increasing age, people tend to frequent the theatres less.[2] Indeed, according to a survey done by the Opinion Research Corporation in the United States, it was found that three-quarters of the people attending movies are between the ages of twelve and

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1. See International Motion Picture Almanac, 1979.

2. Axel Madsen, The New Hollywood, (New York : Thomas Y. Crowell Co., 1975), p.58.

twenty-nine. And some nine-tenths of the admission receipts come from frequent moviegoers. While education had formerly been found to be an insignificant factor in influencing movie attendance habits, it is now known that two-thirds of the people with college education often attend movies.

Audience Decline

One important development in the film industry over the years was the gradual loss of movie patrons. This was an international phenomenon. In Canada, attendance dropped from 236.6 million in 1950 to about 90.4 million in 1974, which marked a 61.8% decrease. The British cinema also experienced the same kind of decline.[3] In the United States, the decline was more marked. It dropped from the all-time high of 82 million patrons a week in 1946 to somewhat less than 46 million per week in 1955. Actually, during the same period potential moviegoers had risen by 15 million.[4] Since then attendance kept dropping to a weekly total of 21 million in the 1960s and then stabilized somewhere around 15 million in 1970.[5]

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3. See "Developing British Films" in the March 8, 1969 issue of the Economists.

4. U.S., Congress, Senate, Report on the Motion Picture Distribution Trade Practices, 82nd Cong., 2nd sess., 1956, p.27.

5. Axel Madsen,op. cit., p.162.

Competition Without

There are several explanation for this steady decline in movie attendance. Changing social habits are one. Actually the decrease is not due to the fact that fewer individuals are going to cinemas. Rather, fewer people are going as often as before. This change can be understood in the light of new kinds of recreational activities available since the end of the Second World War. The industry now has to compete with such entertainments as sports, travelling, concerts and television. With so many alternatives, it is not surprising that movies occupy a much smaller share within a spectrum of leisure time activities.

Among competitors from the outside, television is viewed as one of the most serious. But while television has been viewed as a threat to the industry, it has also become a potential market for film productions. This results from the fact that television has come to realize that it can do much better with popular feature films being shown on the networks.[6] On the other hand film companies have also discovered the potential of this new small-screen machine as a revenue generating resource. This all started in 1961 when the National Broadcasting Company in the United States began to put on motion pictures in their prime time

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6. Robert Crandall, "The Post-War Performance of the Motion Picture Industry", Antitrust Bulletin, Spring 1975, p.65-67.

programming. By 1967, the networks were reported to be paying peak rentals of $1 million for a showing of recently released productions.

In Canada, for example, revenue for film rentals from television in fact constitutes some 30% of all the rental sources received by distributors in 1968. This revenue from television has risen about 16% from that in 1967.[7]

Competition Within

There are several aspects of competition within the industry. In the retail market, price competition between cinemas does not seem to play an important role in attracting audiences. This may be consistent with the fact that by 1930 the film industry in the U.S. had already developed into a mature oligopolistic industry. For mutual benefit, the few major film companies stressed other competitive methods than pricing. Apparently this is still the common policy in the industry today. However, one may also observe that the relative insignificance of price competition may also be due to the show-business nature of the industry and also the position of the industry in the general business environment today.

In terms of the final output, product differentiation

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7. Canadian Film Development Corporation, Annual Report, 1967-70, p.6. (Canadian Film Development Corporation is hereafter cited as CFDC)

is a norm rather than exception primarily because it is an entertainment industry. The product simply cannot be standardized. Thus in the production branch of the industry, to promote product differentiation competition, producers strive to 'package' a production with brand name actors and directors. Large advertising expense is often incurred when production has barely begun. In any case, with the assumption that advertising plays an important role on the success or failure of a picture, promotion campaigns become an important undertaking. Very often advertising is done in trade journals, newspapers, national magazines and television

Input for Production

There are several important input factors that are needed in film production. They are the movie script, creative and technical talents, financing capital, distributing facilities and producer expertise.

The most fundamental factor for a feature film is the basic story from which a script could be derived for filming. Its source may be a popular novel, a stage hit or an original screenplay. However, to use these underlying properties, producers must first acquire the motion picture rights to these literary materials.

In order to turn a script into an actual movie, creative and technical talents are needed for the job. Very often, the quality of a picture is determined by the quality of artistic talents and technical crews it can gather. Creative talents include such people as screen actors, film directors, art directors and editing directors. Certainly all these artists with their unique skill and talent contribute significantly to the final quality of the movie. The technical crew on the other hand include categories such as the management unit, photographic unit, stagehands and decorators. These specialized and skillful crews are needed for an efficient production operation and for minimizing the cost and uncertainty in production activities.

At the same time, access to financing capital is an important factor in film production. Since the making of a film is an expensive business undertaking, it involves tremendous capital outlay before the producer can see any returns from the picture. Especially due to the fact that film production has to be all or nothing, it is essential for a producer to secure enough financial backing before he starts production.

Closely related to financing, a producer's access to the distribution system often determines whether he gets his film made or not. The reason for this is that in this industry without any distribution guarantee it is almost impossible to get financing from the financial institutions. Since an opportunity for distribution would promise some return on the picture, the distribution guarantee is one way for banks to reduce the risk factor involved in film production financing.

Finally, it should be noted that because the making of a film involves a lot of business complexities and subtleties, much creativity and production experience are required of a film producer.

Risks and Uncertainties

Even though risks and uncertainties are common characteristics of business undertakings, the degree of uncertainty however is relatively higher in the film industry.

Because of a need for fresh subject matter for every new film, film producers are forced to make continuing projections of what film genre might appeal to the public best in the near future. This projection process is further hindered by the time-lag problem between when a feature film is first launched into production and the time when it will finally be released; this lag may run between one and two years. Thus by the time the movie is released, the box office trend may have changed. When this happens, it can cause financial disaster for the producer involved.

Also unlike other industries, where products can be made in various quantities and put to a market test, production of a feature film has to be all or nothing and be paid fully in advance. When a film is successful, it can yield a tremendous profit to the producers. However, when a film is a flop it can also bring financial disaster. Thus film production can actually be compared to the oil exploration industry where risk is a big factor.

II. STRUCTURE OF THE INDUSTRY

In studying the film industry, it can be classified into three stage : production, distribution and exhibition.

Production

At the early stage of the film industry are the production activities. The main function of this branch is the actual production undertakings which include the shooting of films, editing and the making negative copy to be duplicated into numerous positive prints for distribution. To make the negative print, producers have to pull together a group of talents such as directors, star performers, writers and technical personnel. For the role he plays a producer is commonly referred to as a 'packager'.

Distribution

Next to production is distribution. Distributors, by signing a contract agreement with producers, often handle post-production exploitation of films. Thus one of the distributor's main functions is the marketing of films as a finished product on the wholesale level. These activities include the physical distribution of films to the cinemas. Since the practice of outright sales has been abandoned in the early days of the industry's development, some of the essential jobs of distribution units include making of prints, arrangement for playdates and delivery of films to exhibitors. Finally distributors are also responsible for collecting the film rentals from the exhibitors. Usually, in return for such services, they receive a certain percentage of the gross return from the producers. This fee is termed as 'distribution fee'.

On the other hand, success of a film depends to a certain extent on proper promotion. Publicity and advertising campaigns are therefore important undertakings in the industry. However, mounting a vigorous advertising campaign requires huge capital outlays. It also demands special skill in the promotion activities in the industry. The common practice in the film production is once again to leave these activities to the distributors. The distributors usually advance most of the promotion expenses and recoup such costs later.

Finally it should be noted that the distributors also play a prominent role in film financing itself. In the first place, to back up a film production, all the distributor has to do is to agree to distribute the proposed film product. By agreeing to distribute such a film, distributors in effect help the prospective producer in getting often-needed bank financing. Secondly distributors also quite often put up the required capital for a project in return for the exclusive right of distributing that film.

Exhibition

In the lower spectrum of the industry lies the exhibition branch. It is at this stage that the film industry finally comes into contact with the public. Indeed it is the retail outlet of the film products.

Scattered all over the country, theatre operators have to decide what particular preference the people in their district will have. Accordingly they have to make the appropriate booking of the films. In this regard, one of the main concerns of exhibitors is a constant supply of film products. They have to see that a flow of different films is secured throughout a year in order to attract patrons. Cinemas in the United States are mostly operated by small businessmen.[8] This is also the case with Canada.

Integration in the Motion Picture Industry

The motion picture industry has been noted for its tendency to integrate, both vertically and horizontally. For example, until 1948, there were five major companies in

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8. U.S., Congress, Senate, op. cit., p.2.

the United States outstanding for their fully-integrated operation in the industry. The five major companies were Loews (MGM), Warner Brothers, Paramount, Twentieth Century Fox and RKO. In 1948, the U.S. Supreme Court ordered the divorce of production-distribution activities from exhibition in the industry. In Canada the industry is dominated by two major circuits of theatre companies, the Odeon Theatres Company and the Famous Players Company. These two companies hold two-thirds of the Canadian cinemas. At the same time, Famous Players is owned by a big distribution concern, Paramount Inc. Added to this is the fact that the seven largest distributing companies operating in Canada are branch offices of American film companies which are still financing film productions in the United States. Thus the film concerns in Canada have a more subtle vertically-integrated operation that is not readily obvious.

One argument for the tendency toward integration is the attempt by the industry to reduce risks and uncertainties. As has been observed, the production end of this industry is risky and expensive. The final demand is volatile. Success of a film depends on a proper promotion. Few producers would be happy to leave their products to distributors who might be too busy or too uninterested to give careful attention to the product. At the same time it would certainly be disastrous if a producer, once having finished a negative print, finds that he could not get access to any market outlets. Thus as a result of the producer's desire to reduce uncalled for risks and to ensure an efficient distribution operation, there is pressure to integrate forward. This explains in part why at least some link between production and distribution is desirable from the producer's perspective.

On the other hand, the tendency to integrate also results from the desire of exhibitors in the lower end of the industry to secure a constant supply of film products. To safeguard themselves from the shortage of quality films, it is quite natural for the exhibitors to attempt integrating backward in order to produce films for themselves. In this regard, the motive here is not very much different from oil refineries going back to crude oil production and steel mills securing iron ore supplies. This explains partly why the First National Circuit, a combination of theatre companies, in 1917 went into picture production. It also helps to explain why after the complete vertical integration in film industry has been declared illegal, exhibitors have again attempted to go into picture production.[9]

Another prominent feature in the exhibition branch of the industry is the prevalent horizontal combination among

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9. Simon Whitney, "Vertical disintegration in the Motion Picture Industry", American Economic Review, May 1955, p.493.

theatres. In a way the combinations are a means by which exhibitors can protect their own interests in bargaining with the powerful production companies. The history in the American film industry proved that by forming a large circuit of theatres, exhibitors could enhance their position in dealing with the producers.[10] As a result of their theatre-chains, large exhibitors attain a position that gives more bargaining power in securing film supplies and at a relatively better price than those who stay independent and small. Thus this horizontal integration is an attempt to achieve pecuniary benefits of a large scale operation.

In view of the characteristics of the film industry, it seems that mergers, especially vertical ones, may carry some real economic advantages. At least they can help to guarantee producers a marketing outlet. The exhibitors would also be benefited in their assured supply of film products. However, one serious question still remains in as much as such integrations could be instrumental for existing companies in the film industry to attain and abuse their market power.

As experience has shown, vertical integration in the United States film industry has proved to be a primary means by which major companies have achieved market control. Only

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10. Michael Conant, Antitrust in the Motion Picture Industry (Berkeley: University of California Press, 1960), pp.23-24.

by much government antitrust effort have some of these restrictive barriers to prospective producers been mitigated.

III. SOCIAL IMPLICATION

A perennial controversy surrounding the film industry is the question of whether films are entertainment or art. Especially in America the distinction between entertainment and art is much exaggerated.[11] Obviously the film industry is one that lies in an area which spans a spectrum between entertainment and art.

However, from an economic point of view, the controversy would not be of interest had it not been for the possibilities of externalities.

On the one hand, working under a pure entertainment-business philosophy the operation of the film industry could be left to the private sector of the economy. This is the case in the United States. The producers will undertake the production process under the motivation of prospective financial gains while at the same time having to bear the risks involved in the operation. In other words, film producers become enterprisers in an entertainment industry. Obviously this is a predominant

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11. Peter Harcourt, Movies and Mythologies,(Toronto : CBC publications, 1977), pp.75-77.

attitude toward film making among U.S. producers. In Canada some industry people also hold the same view.

On the other hand, it is noted that films are also a communication medium from which ideas could be put forth to the public. Even though entertainment films are not a medium for formal education, nevertheless, they certainly provide audiences with vital experience and emotional as well as intellectual stimulation. It is thus argued that entertainment films could also be an effective tool for promoting national unity and help to foster a nation's culture. For the country as a whole, benefits derived from film production and consumption might prove to be more than the benefits accrued to private individuals alone.

At the same time the tendency to transcend national boundaries as a result of their unique graphic languages makes films an important tool for promoting international understanding of a nation's culture. Good films would also enhance international respect for a country's art and ensure goodwill. If a country values the friendship and peaceful encounters with others this too would certainly be an important intangible benefit.

Furthermore, provided that a country could command its essential factors of production, film could be an ideal export item, since its finished product only consists of a few cans of film occupying negligible transportation space.

Thus films would add to the export base of a country and contribute to its balance of payments position if film industry achieves international success.

There may be other indirect benefits for the country as a whole such as providing employment opportunities to its talents and technicians. But the aforementioned characteristics of the industry should have indicated the possible existence of significant but intangible social benefits. Left to the working of a free market enterprise mechanism, an optimal social level of film production might not be achieved. This is because the indirect benefits involved would certainly be discarded by the private investors in their profit seeking calculations.

Following this line of thinking a case for government support of film production can therefore be made.[12] Only from such a perspective does one understand the existence of conscious efforts by the British government and some European governments such as those in France, Germany and

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12. The position of the British government on film matters could not be demonstrated better than by the following quotes : "The request which follows for a substantial measure of government support is based on the view that this should be forthcoming only for tasks which the private sector is either unable or unwilling to perform. We believe, moreover, that a positive and constructive policy which will operate in the national interest should not be based exclusively on considerations of commercial profitability, but on the benefits to be derived by the community as a whole." See Report of the Prime Minister's Working Party, op. cit., p.10.

Italy to help their own film industry. This consideration may also be relevant in a Canadian context since Canada is searching for national identity and is also involved in efforts to develop a feature film production industry. A clear understanding of this externality problem may help to generate a more coherent policy toward film production, once the government could choose their stand on the value of these film matters.

Chapter 3

Barriers to Entry and the Film Industry

Before we proceed to discuss and document the efforts to promote the Canadian feature film production industry, some understanding of the concept of entry and the factors behind entry into manufacturing industries in general and the film production industry in particular is desirable. In this chapter we will make a survey of the economic literature on the theoretical discussion of entry. The sources of barriers to entry will be investigated and an attempt will be made to apply some of these theories to the film production industry. Efforts will be made to identify the relative importance of the barrier factors in the film industry.

I. DETERMINANTS OF ENTRY CONDITIONS IN MANUFACTURING INDUSTRIES

Economic theories have identified several factors that work for or against new entry into manufacturing industries. These factors can be classified into structural aspects of the industry and the conduct of firms within such an industry.

Structurally, these factors are economies of scale, product differentiation considerations and absolute cost advantages. On the market conduct side, factors that contribute to raising the height of barriers to entry include strategies of pricing, desire to restrict competition, degree of integration and outright legal restriction.

A. Structural Barriers to Entry

Economies of scale.

One of the common factors deterring new entrants to an industry can be the existence of large scale economies within that industry. With economies of scale as a firm expands its operation, it realizes substantial unit cost savings. This is possible because as a firm's output volume grows, many of its production functions can be done by specialized units and by special machines. Thus it is possible that with a higher volume of output, a lower average cost per unit could be achieved.[1]

But economic theory also states that a firm could not keep on achieving lower costs by expanding indefinitely. This is because beyond a certain point, some forces of large scale diseconomies and diminishing returns in production might set in. This could be a result of problems in managerial coordination in a large production process and may also be due to difficulties in harmonious coordination between branch operations. Such is the reasoning behind the concept of U-shaped cost curves.

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1. F.M. Scherer, Industrial Market Structure and Economic Performance, (Chicago: Rand McNally College Publishing Co., 1970), p.72; See also Joe Bain, Industrial Organiztion, (New York : John Wiley and Son, 1968), pp.146-151, (hereafter cited as Bain, Organization.

However, empirical studies reveal that the long run average cost curve for firms would commonly look like the one in Figure 3-1. This means that as a firm expands productive capacity, it will achieve a lower per unit cost of output up to a certain point. Beyond that, further increases in firm size may neither increase nor decrease unit costs. Thus there may be a range of optimal production size for a firm. Within this range, the point where the smallest scale of the firm could attain the lowest cost is termed as the minimum optimal scale of the firm.[2]

With the concept of economies of scale, it is possible to show the negative effect of large scale operation on new entrants. Two important effects have been identified. They are the 'percentage effect' and the 'absolute capital requirement effect'.

i. Percentage Effect

The percentage effect could be explained with the Figure 3-1 again. Suppose the total output of an industry is OM at the going price. At the same time, suppose substantial economies exist in this industry, then to achieve a minimum optimal scale a firm has to establish itself at a size producing OB amount of the product. If

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2. Joe Bain, <u>Barriers to New Competition</u>, (Cambridge, Mass:Harvard University Press, 1956), p.53, (hereafter cited as Bain, <u>Barriers</u>.)

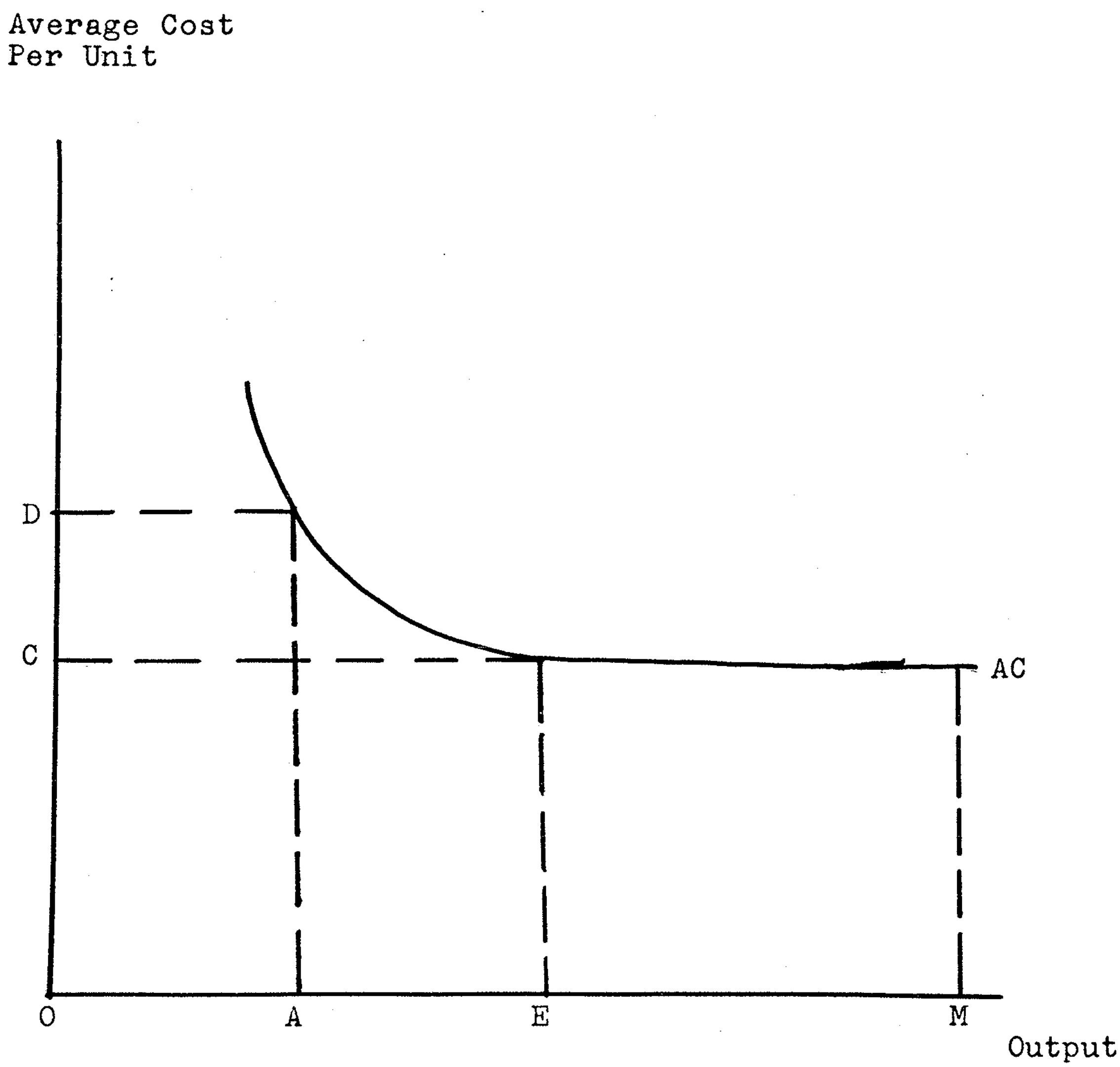

Figure 3-1 : Average Cost and Scale Economies.

this is true, then the market demand may be satisfied by two or three firms operating under the optimal scale. Given this condition, the market can be preempted by the existing firms and potential entrants would suffer a marked disadvantage. If a new firm were to break into the industry, it might be confronted with the following alternatives.

Firstly, to gain tolerance from the existing firms, a new firm could choose to enter with a small enough scale so that as a result of entry and the increased output, there is no obvious influence on the price and output of the existing firms. But then the new firm would be operating in a sub-optimal level and suffer a marked disadvantage of higher costs than that of the established firms. Alternately, the firm could choose to enter at a more optimal scale, resulting in a depressed price in the industry as output increases. Consequently, the post-entry price would be lower than that of the pre-entry level. The new firm might now find that the industry is no longer profitable. Finally, if a firm is to enter with a near optimal scale, it has to face the probable reaction by the existing firms to its new appearance. The reaction could take two forms.[3] One, the existing firm might tolerate its existence by cutting back its output to let the new firm have a share of

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3. Ibid., pp.54-55.

the market at the pre-entry level. In such a case, both the established firms and the new entrant would be working under a suboptimal scale. Or the existing firm might react negatively to the emergence of the new firm by retaliation through price cutting.

These are the difficulties the percentage effects of scale economies could create for a newcomer. In sum, it might be said that the greater the output a single firm with minimum optimal scale would supply, the harder it would be for a new firm to start out at an efficient level. Also, the steeper the rise in the cost curve as a result of reduction below the optimal scale of operation, the more difficult for a new firm to start at a suboptimal small scale in order to establish itself.

ii. Absolute Capital Requirement Effect

On the other hand, the absolute capital requirement effects refers to the fact that as a result of large scale operation, difficulties are created for some small new entrants in raising the required capital investment. Generally it has to do with the problem of imperfect capital markets. But for the study of its effect as a barrier to entry, most studies group it under the separate heading of absolute cost advantage consideration. This will be discussed in a later section.

Product Differentiation

Product differentiation refers to the possible differences perceived by consumers of some commodities that might basically be the same. Of course this perceived difference could be real or subjective. The essence of such a differentiation, however, is that the consumer might tie their preference for one brand of a product to the disadvantage of others. Thus, for example, when pricing a product such as toothpaste, or cigarettes, the consumer may have a stronger preference for producer A's to that of B's even though they are actually producing a substitute product. In this way the demand for the output A would become less elastic than it would otherwise be without differentiation. A producer whose output has a stronger consumer allegiance could thus gain some jurisdiction over the prices of this product and has more incentive to raise rather than lower the price. Thus as long as a product is differentiable, it seems worthwhile for producers to promote some kind of product differentiation.

Product differentiation is promoted by producers through such means as package designs and superior auxilliary services. By such means producers hope to create a much sought-after brand name of their own. Obviously, to create such a name and the allegiance of consumers, heavy advertising and sales promotion activities are effective tools and have become almost essential. As a result, additional promotion costs are often added to the production and distribution process.

Several important consequences arise. Firstly, as a result of buyer's preference, prices need not be identical among producers selling the same competing products. Secondly, substantial costs in undertaking product improvisation, advertising and promotion are incurred for the producers. These costs cannot be avoided if a producer is to secure a fair share of the market. Thirdly, given the desire to maintain a significant share of the market, producers may be encouraged to change their organization in order to give more force to promotion activities. An examples would be the urge to vertical integration in order to secure a reliable distributive facility. Finally, because of the disparity in pricing, selling outlays, and buyer preference among different producers, it is possible that in a competitive situation, different producers could gain significantly different shares of the market.[4]

These consequences are good hints to the possible role product differentiation could play as a barrier to entry.[5] In the first place, since the market has been tied up mostly by established sellers with their particular buyer

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4. Ibid., p.115.

5. F.M. Scherer, op. cit., p.341.

allegiance, a new entrant who might be selling a product of same quality would have to take one or both of the following measures in order to secure some standing in the market. He either has to sell his product at a lower price relative to those of established firms to establish a demand for his own product, or if he charges the same price as other established firms do, he may be forced to advertise his product very much in excess of the advertising activities required for an established one. Thus there is a marked disadvantage in the selling outlay of the new producers. This disadvantage may be depicted in Figure 3-2.

In either case, compared to the cost of established firms, it is obvious that the new firm suffers a distinct disadvantage. Moreover, the fact that there is some interaction between advertising activities and the economies of scale indeed makes the product differentiation type of barrier to entry even more formidable.[6] It is found that economies of scale often exist in the use of advertising. This is because a certain saturation threshold has to be reached for best results and because many media offer discount to high volume advertisers. Since it usually takes some time to establish a brand preference, the advertising cost advantage enjoyed by the established concerns may prove

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6. Ibid., p.341; see also W.S. Commonor and T.Wilson, "Advertising Market Structure and Performance", Review of Economics and Statistics, November 1967, pp.425-426.

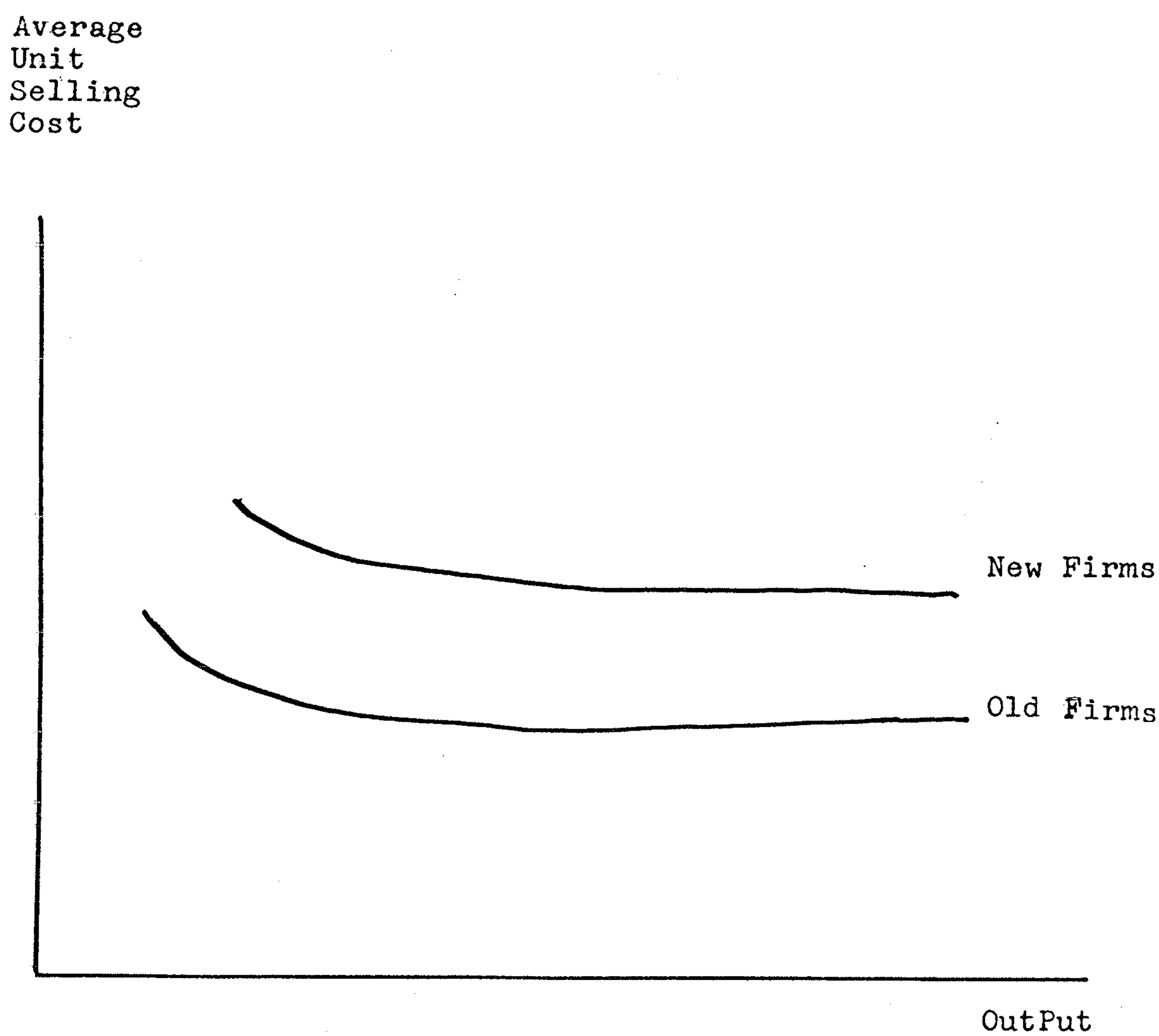

Fig.3-2 Product Differentiation As a Barrier to Entry.

to be critical for a small new entrant to survive. Should a new firm decide to enter with a scale large enough to reap the benefit from the pecuniary economies of sale promotion, it may run into another complication of having to meet a higher capital requirement.[7]

Such are the possible difficulties a new firm may have to face in an industry where image differentiation is very important. To a certain extent, entry may be discouraged and established firms could be able to raise price without inducing entry. This is the way product differentiation could work as an agent of entry deterrence. However, in passing it should be noted that product differentiation could work the other way too. As long as a new firm could offer some superior new product such as by innovation, it is possible that it could overcome the high advertising barrier and be able to establish itself in the industry.[8] The history of some American industries offers many such examples.

Absolute Cost Advantage Consideration

Another type of barrier to entry is found in what has been termed as absolute cost advantages enjoyed by established firms. This refers to situations where new

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7. Comanor and Wilson, op. cit., p.426.

8. F.M. Scherer, op. cit., pp.230, 341.

entrants in general have to face a higher unit cost curve than those of established firms in every scale of their production and distribution operations.[9] This cost disadvantage of the new firms could be shown in Figure 3-3.

It shows that for any level of output, the established firms would be able to produce at a much lower cost. Should there be a significant gap between the unit costs of the old and the new firms, it would mean the established firms will be able to charge a price and reap a profit while the new entrants would not be in a position to recover their costs at such a price. If it is the case, new entrants would certainly be discouraged from entering.

Some of the potential sources giving rise to this advantage enjoyed by established firms have been identified.[10] They are the control of superior production know-how, factor market imperfection and capital market imperfection.

i. Control of Superior Production Know-how

Every kind of production depends on a certain degree of technological know-how such as managerial and production skill. To enter an industry and to compete successfully with established firms, a new firm should command a level of

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9. Bain, Barrier, p.144.

10. Ibid., pp.144-145.

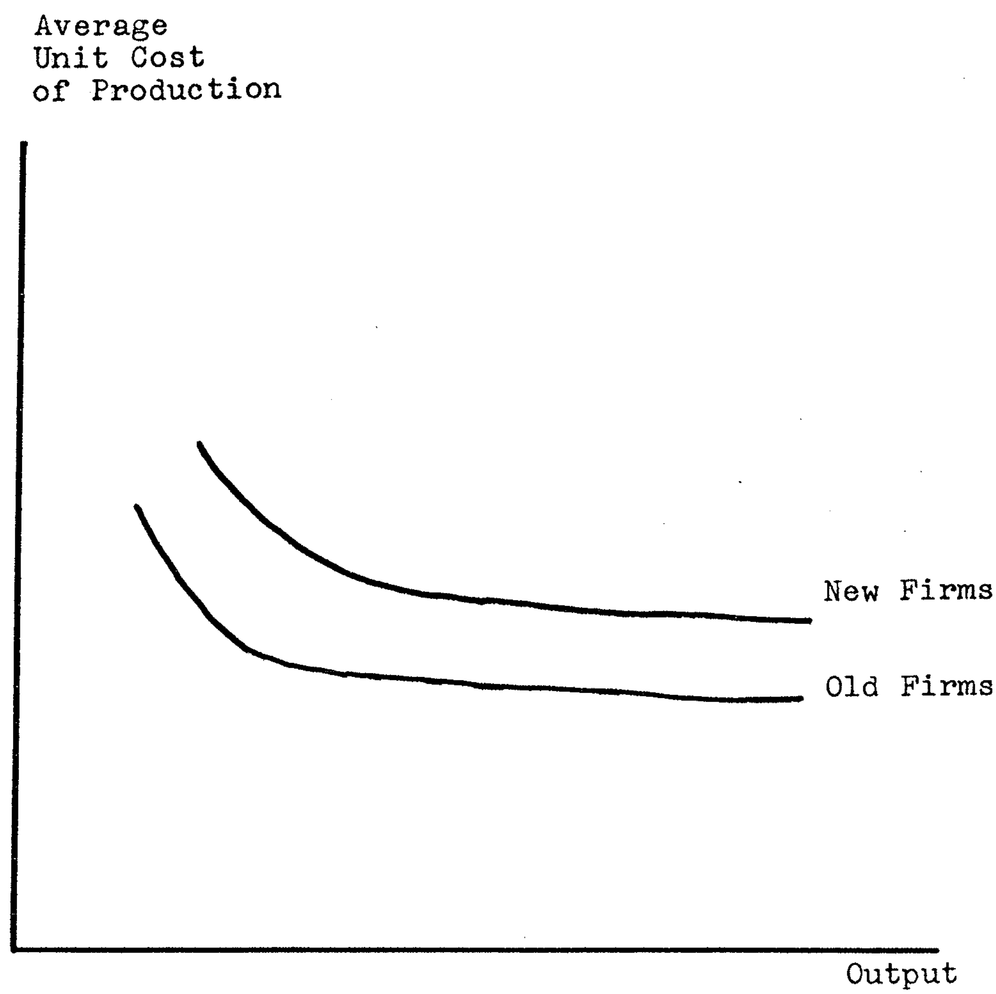

Figure 3-3. Absolute Cost Barrier to Entry

technology at least as advanced as the old ones. If however the old firms manage to control some superior production technique or equipment and at the same time manage to deny outsiders their use, either by patent protection or by secrecy, the new entrant would probably have to operate relatively less efficiently and suffer some cost disadvantage.[11]

ii. Factor Market Imperfection

One of the most fundamental requirements of the new entrants to an industry is of course the accessibility to the factors of production. They have to pull together such factors as labor and raw materials before they can start the production process. However, these factor markets may not be perfect and the new firms in most cases have to pay a higher price than the old firms in order to secure the needed factors. It is especially true in the case of getting natural raw materials. Industries based largely on natural deposits of metallic or non-metallic ores are good examples. If once the established firms own and control the superior quality of these materials, the new firms may be unable to get hold of the resources or have to use some lower grade inputs. This market imperfection further aggravates the cost disadvantage of new firms.

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11. Richard Caves, American Industry : Structure, Conduct and Performance (Englewood Cliffs: Prentice Hall, 1964), p.26.

iii. Capital Market Imperfection

Another major factor that has been perceived to be important in contributing to cost disadvantage of the new firms is the absolute capital requirement needed for investment in a new production. This comes mainly from the imperfection in the capital market and from situations where a large amount of capital has to be committed to enter. Generally this difficulty tends to become more serious when economies of scale are involved in the production activities.

Firstly, risks are often involved in the business world and information may not be perfect. It is conceivable that financers would tend to be more cautious about financing a new enterprise than an established one. Thus it is not uncommon for a new prospective producer to be unable to find a financial backer. Certain difficulties are imposed on new entrants in raising funds.[12] This disadvantage is deepened further by the fact that major established firms often gain access to internal financing while at the same time outside financing is available on relatively favorable terms. For the new ones, if they ever secure the needed finance, it would probably be true that they would pay a much higher interest rate than would the established firms.

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12. Roger Sherman, The Economics of Industry, (Boston: Little Brown and Company, 1974), p.239.

These difficulties to entry would certainly be increased when the scale of operation becomes larger.[13] In the first place, it would discourage newcomers who otherwise may enter if small scale operation is possible. The large scale capital investment simply prevents them from any experiment. On the other hand, the large amount of capital needed presumably would raise the effective interest rate and could added to the problem of fund availability. In both cases, it takes a higher profit incentive before entry could be induced.

B. Barriers as a Result of Market Conduct

It should be noted that the factors determining the relative ease or difficulty in entering a certain industry as delineated in the previous section are primarily results of structural organization within an industry. Thus those may well be the consequences of some objective economic facts in the environment producers have to live with. But not all the problems of entry barriers are necessarily a result of objective economic facts. Indeed there are outstanding barriers to entry which are of completely different nature than those we have discussed. These are barriers as a result of market behavior of established firms.

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13. Bain, Barriers, p.146.

In a free market enterprise system, given the individual firms' profit motivation, it is conceivable that once the established firms have achieved some kind of superior position, they will tend to undertake measures to preserve their advantages. However, such measures in most cases would result in some undue restraint on trade and give rise to practices of unfair competition, both for existing and potential competitive firms. It is to these market conduct aspects that we would like emphasize in this section.

In general these barriers come as a result of existing trade practices, the consequences of which are often ambiguous. Some of the trade practices may have business justification but also may have restrictive effects. It appears that the ultimate effect will depend on the market environment upon which these practices exist.[14] The important point to remember is that while these measures may appear innocent, they can also be a subtle device for market control.

Pricing Strategy

There are some pricing strategies which are employed by existing firms to bolster their own market postion and which could be detrimental both to existing rivals and potential

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14. Richard Caves, op. cit., p.51.

competitors. Examples of these pricing strategies include predatory pricing, price discrimination and price restraints of existing firms.

i. Predatory pricing

Predatory pricing refers to price cutting employed by some financially powerful firms in an industry to warn aggressive rivals or to drive them out of business. With such a tactic, the powerful firm would keep on cutting the price over a period of time to a level where it would no longer be profitable for the rival or sometimes itself to keep up the production process.

Certainly this tactic is employed with great cost and targeted at the existing competitors. However, it could also create harmful effects on potential competitors. In an industry where coercive practices are pervasive, either in the past or present, additional risks of retaliation by existing firms are added to prospective entrants. A lot of times the prospective entrants have to add these risks into their consideration in making a decision on whether or not to enter. They have to gamble as to what response established firms would make as a result of their entry. This is especially true if some large scale of entry is required for an efficient entry. In most cases, new entrants would either be discouraged or enter only with a much sub-optimal scale of operation.

ii. Price Discrimination

Price discrimination may well be defined as the sale or purchase of different units of goods and services at a price differential not directly related to cost.[15] There are several forms in which it appears. 1. Commodities of the same kind are sold at different prices to different consumers. 2. Different commodities with different cost functions are sold at the same price and 3. Two different commodities are sold at prices very much deviated from their costs.

As an anticompetitive force, price discrimination would have an adverse effect on the prospect of entry. Firstly, where there are big firms which can charge very low prices in some segmented markets, even if other barriers to entry are low, entry would be discouraged as a result of unprofitable prospects in these markets. Secondly, it is apparent that price discrimination could create some strong seller-buyer ties as a result of their preferential dealings. If price discrimination practices are prevalent, ties between buyers and sellers would result in entrenchment of established firms in their market postions. Most probably the market would be fragmented leaving little profit opportunity for the new entrants. Thus price

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15. F.M. Scherer, op. cit., p.253. See also Carl Kaysen and D.F. Turner, Antitrust Policy, (Cambridge: Harvard University Press, 1959), p.179.

discrimination could have very discouraging effects on entry. Finally, if price discrimination can be employed in such a way that the input costs for a larger firms could be reduced to a level lower than those secured by the smaller ones, it would have the same effect of raising the absolute cost disadvantage of prospective firms.

Tying deal, Exclusive Dealing and Contract Requirements

Another type of market conduct which is harmful to the competitive forces is the practice of sellers requiring buyers to refrain from dealing with other sellers. These practices cause market foreclosures by existing firms.

Market foreclosure could be done by such practices as tie-in arrangements, exclusive dealing and contract requirements. Again there always seems to be some economic rationale for such practices.[16] But for our purpose here, it would suffice to point out that these practices could create serious barriers to entry.

Degree of Integration in the Industry

Another aspect of market behavior that could help to raise the barrier to entry is the degree of vertical integration undertaken by established firms.

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16. For a detailed discussion on the benefits of such practices, see E.M. Singer, Antitrust Economics (Englewood Cliffs: Prentice-Hall, 1968), Chapter 6.

Vertical integration can be taken as the combination in one enterprise the functions of customers and suppliers.[17] These combinations can take the form of either 'backward integration' to include the production of its input materials or 'forward integration' to include the distribution outlets for final products.

One conventional explanation for firms' tendency to integrate is the desire to achieve economies of scale in the whole production undertaking. The source of these economies may be technical or pecuniary which comes as a result of avoiding using the price mechanism involved in the production activities.

One effect of integration is to raise difficulties for potential entrants. If many existing firms of an industry undertake vertical integration, entry into one horizontal stage would become very difficult, at least by the extra amount of capital needed for the related activities in order to compete successfully. This is essentially the result of large scale operation and high absolute cost problems.

But it should be noted that not all vertical integration is economical. Even if vertical integration can bestow consumer benefit when the market is not competitive, the fact remains that it can be abused to exploit market

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17. Kaysen and Turner, op. cit., pp.119-120.

power. This practice is closely related to what is termed as 'squeeze operation'.[18] It is based primarily on the fact that by vertical integration, the fully integrated firm could drive the non-integrated firms into a situation where they are either foreclosed from the source of the input supplies or from the final market. They could also force a price-squeeze on non-integrated firms.

In an industry where certain firms move to integrate their operation, fear of raw material or market foreclosure may drive others to follow suit. Should smaller firms find themselves unable to do so, their survival would be threatened. The same analysis could be applied to potential competitors. Thus it is possible that entry into vertically integrated industries would be more difficult than into those non-integrated ones.

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18. Richard Caves, op. cit., p.51.

Outright Legal Restriction

For some industries, the entry into and exit from the market are controlled by governmental regulations. Entry into such industries can be restricted. Quite often the government grants franchises to only one or a few entities. A classic example is utilities business. The most common rationale behind such restriction has been that of 'natural monopolies'. Actually, for these industries, even without government restriction, the barriers to entry as a result of economies of scale are very high. By government regulation and restriction, it is hoped to reconcile the need of large scale production with that of public interest. However, even with industries such as transportation and radio communication where some competition seems possible, restrictions are also imposed.

II. FACTORS AFFECTING ENTRY INTO FEATURE FILM PRODUCTION INDUSTRY

Having done a survey on barriers to entry in the manufacturing industry, we will try in this section to identify some of the factors that would hinder entry into the film production industry.

A. Economies of Scale

As we have seen in industries where economies of scale are significant, certain disadvantages are created for potential entrants as a result of the 'percentage effect' and the need for higher amount of capital.

In the feature film production industry, economies of scale do not appear to be a critical factor. On the contrary, studies have shown that large scale in film production could produce undesirable effects. This is because of the unique characteristics of the industry. As one study puts it[19]:

> While there are economies of scale achieved in some other industry, where product is stand-dardized, this is not true in motion pictures. There are obvious limitations on the numbers of really different pictures that can be made by any one company. The very fact that they are presumably not alike means that mass production methods cannot be used with the same measure of success as in some other industries.

In other words, emphasis on the appeal of each film product renders standardization of film production very difficult. The net effect is that economies of scale effects might not work too well in this industry.

Especially because today's film industry is only one of several competing recreational industries and its audience's taste is more selective than it has been, each film product is evaluated according to its own merit. Thus the success of a film depends much on its production effort. It also

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19. Howard Lewis, The Motion Picture Industry (New York: VanNostrand, 1933), p.97.

means that undesirable effects might be experienced if films were to be mechanically mass-produced. It is under this consideration that another study on the optimal production scale in film industry has concluded[20]:

> Available data indicate that the minimum optimal scale of operation is the production unit organized to produce a single motion picture. Since the production inputs and process of each picture are unique, the optimal technical unit and the optimal managerial unit both appear to be the production of a single picture.

As a matter of fact such a conclusion is very much supported by Hollywood experience. During the heyday of Hollywood, the American film industry was dominated by several major companies which had control over the production, distribution and exhibition interests. In order to have a high volume output and also to fulfill the screentime requirement of their own theatres, these major companies had attempted large scale production programs. Their production studios were organized in assembly line manner maintaining a whole stable of star performers, writers, directors and other artists and technicians. With this type of organization, the major studios each was able to churn out some forty to fifty pictures annually.

The result was that during the 1920s and 1930s these major companies produced many low quality films, judged

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20. Michael Conant, op. cit.

either by box-office receipts or any other standards. Since then, reforms were urged throughout the industry.[21] By the early 1950s, as a result of the post-war development of the industry and as a result of the antitrust action of the U.S. Government, the companies in the production branch of the industry were no longer under pressure to mass-produce in order to meet theatre requirements. This led to the reduction of production scale of the major companies and the rise of independent producers. Usually the new production units are organized to produce one film and disbanded after the completion of a picture. Today many independent companies tend not to own any studio overheads. Instead they rent studio facilities whenever there is a production need. This seems to be more efficient because it helps to cut down overhead costs and at the same time possible because there are firms specializing in the studio business.

The above discussion tends to indicate that small scale operation in terms of output may be more beneficial in the film production industry. In such a case, the 'percentage effect' of the economies of scale should not create undue difficulties for potential entrants. In fact, studies have shown that even in the 1930s, when film companies were organized in a scale directed to dominate the industry, the

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21. Howard Lewis, op. cit., p.96.

five major companies could only produce half of the total output needed in the market.[22]

All these considerations tend to show that the economies of scale per se should not be an important factor working against the entry of new producers. Markets would probably not be preempted by the so-called 'percentage effect'. If there should be difficulties for new entrants into the film production industry, it may be a result of other factors.

B. Product Differentiation Considerations

In connection with product differentiation, there are several observations which can be made in relation to the film industry.

Firstly, as we have noted earlier, the film industry is an entertainment industry. Competition takes place not only within the industry; it comes also from without. When producers decide their movies ticket price, emphasis is put more on consumers' time than money. Price consideration is therefore not a very important issue in the industry. The general phenomenon is that price may vary according to the quality of the pictures and the public acceptance. Price variation is not necessarily related directly to company

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22. U.S. Temporary National Economic Committee, The Motion Picture Industry: A Pattern of Control (Washington D.C., 1941).

brand names in the film industry. It is simply because consumer allegiance in this industry would probably be more to the picture (such as the genre and star names) than to the production unit. It is especially the case today since audiences are more selective in their taste for film appreciation. Thus very specialized films would also find audiences.

Secondly, in terms of promotional activities, there seems to be no particular advantage enjoyed by established producers over new ones. It is true that film promotion is almost a must for every film if it wants to be a success. The ultimate goal in film promotion is to create 'words of mouth' which will sell a picture. The usual way to promote a picture is by maintaining a publicity department in the company and by heavy advertisement in the media. This of course involves an enormous amount of expense. And it could be expected that an existing major producer may have an edge over an independent in these activities. But if a newcomer ever gets a film made, most probably it is because he has already secured some agreement with a distribution company. More often than not this distribution agreement comes from a major distributor who has good bargaining power in dealing with the advertising activities in comparison with other distributors. Thus, pecuniary economies in advertising competition among film producers may not be a very important factor.

Furthermore, it is generally recognized that in the film industry, the outcome of an advertising campaign is largely undeterminable. This appears to be more like an exercise in topology.[23] Experience shows that a rigorous advertising campaign can produce picture hit such as Funny Girl, Last Tango in Paris and The Exorcist but it can also overkill a picture such as the Great Gatsby.[24] These examples indicate that even though huge advertising campaigns are necessary for a film's success, the outcome is far from guaranteed. For this reason, it may be argued that no differential advantage would be bestowed on a certain company. Financial results of two different pictures coming from the same producer may be completely different. Thus the consideration that product differentiation via promotion costs could put a new producer at a disadvantage may not be relevant in the film industry.

But one adverse effect product differentiation could impose on prospective entrants into the film industry is the tremendous upward pressure on the capital requirement for production, since the selling cost could be formidable.[25]

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23. Alex Madsen, op. cit., p.117.

24. See "Building a Dowry for Funny Girl", <u>Business Week</u>, Sept. 28, 1968;also Alex Madsen, op. cit., p.119.

25. Garth Drabinsky, op. cit., p.149. For a rough indication of the expensive nature of the media advertising in cities such as New York and Toronto where pictures are usually premiered, see pp.154-155.

For some pre-opening and first week advertising, it is not unusual that promotional expenditures run between $40,000 and $50,000. This adds more risk to the production.

Finally it should be noted that product differentiation in the film industry could actually encourage entries through innovation.[26] This is possible because of the highly differentiated and ever changing film product pattern of the industry. Thus even for the established firms, every production is a new beginning. The outcome is overshadowed with uncertainty; once again, success may not be guaranteed. This fact alone is a great help to the new producers. As long as the new producers can offer pictures that are superior or simply more tailored to the tastes of the audiences, their chance of success in the trade is enhanced.[27] In the history of the industry, there are many such stories of success of the new producers in gaining entry by offering innovations both in terms of film producing technique and content.

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26. Michael Conant, op. cit., p.37.

27. Kenneth Macgowan, Behind The Screens (New York: Delta Book, 1965), Chapter 10.

C. Absolute Cost Considerations

Finally, we come to factors affecting film entry that can be loosely termed as absolute cost aspects. These include such things as the riskness of the business, producers' expertise, input for film productions, financing and distributing problems.

Riskness of the Business and Producers' Expertise

As it has been said, the film business being a show-business, is very much like a gamble. The investment outlay is huge. But it could bring high rewards as well as financial disaster. For a person seeking normal return, undertakings in the film production industry may not be appealing. Possibly only people with creative talent and urge, or people who like the glamour of the industry and are willing to take the gamble might wish to enter.

Even then, for a successful entry, there are certain conditions required of a potential producer. In the first place the producer should have an ability to secure the right story and the right creative talents such as actors and directors for his project. His credibility to the financers that he can make the whole film within budget is also required before he will get any financial backing. In certain ways film production is actually a profession that needs to be mastered. Furthermore, such knowledge of the business has to be combined with the producer's talent which has to be a combination of being an idealist and a politician. Thus, like many other professional services, a big surge into the industry by new producers is discouraged as a result of the professional expertise involved. This is a major difficulty new producers have to overcome in order to enter successfully into the industry.

Inputs for Production

The basic ingredient of a film is the script. The main source for scripts is novels, stage plays or original screen plays. There seems to be no lack of such supply. However, the main problem for a producer is to find a script which is suitable for the movies and which has international appeal. The situation in this continent is that there is inflationary pressure on script costs since the very early days of the film industry. It is the result of producers' struggles to out bid each other for relevant materials. The result of this is a marked increase in the absolute cost of production which contributes to the risky aspect of making a picture.

As to creative and technical talents, there seems to be no lack of these factors in both the U.S. and Canada. Quite often the opposite is true in that access to employment for these talents is limited. It should be pointed out, however, that, formerly, most of these talent and technicians were under contracts with the major studios and their availability to an independent producer was restricted.[28] But this is no longer the case today when most of the talent is freelancing. They are willing to work for any producers as long as there are suitable projects. Thus the availability of talent should not be a factor working against entry into film production.

The foregoing statement, however, needs to be qualified. It is the problem of the so called 'bankable' talent that are available. The supply of this talent appears to be very limited. To employ talent which is riding the tide of success is very expensive. But this talent is often needed to minimize the uncertain outcome of the picture. Should glamourous talent be used in the production, the end result will be a much higher budget for the picture.

In all, the input for the film production would not be a serious impediment to the entry of film producers. The factors are open to employment for most producers. The main problem lies in the absolute cost in using these factors. The expensive nature of these factors is exactly the cause of high budget cost required of a good quality picture. Since a significant amount of the budget is spent on the

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28. Robert Brady, "The Problem of Monopoly", Annals of the American Academy of Political and Social Science, November 1947, p.127.

factor costs, factor inputs help also to raise the absolute cost requirement. For example, the average cost for a picture made in the United States in 1976 was estimated to be around $4 million.[29]

Film Financing

The high absolute cost of film making is an important entry barrier. It is primarily due to difficulties new or unknown film producers have in securing the necessary operating capital. Because of the high costs, more often than not producers have to resort to some form of bank financing. However, for this industry such financial resources are limited. The amount of financial resources is especially limited for an independent production. There may be several explanations for this.

Firstly, because of the inherent risky nature of the industry, few commercial banks in the United States have ever been involved substantially in any picture making activities.[30] To do so would require certain business expertise on the part of the bankers before they could feel secure enough to get involved in these ventures. It is for this reason that no more than a dozen banks have lent to the film industry in the United States. It is also exactly as a

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29. See International Motion Picture Almanac, 1979.

30. Patrick McGilligan, "Bank Shot", Film Comment, Sept-Oct, 1976, p.20.

result of this lack of expertise that Canadian banks and other financial institution generally shy away from film financing.[31]

Secondly, even those banks which have the skill and tradition in the film financing business are still very cautious in their approach to film finance procedures. The bankers tend to look for security measures instead of risky gambles. One way to achieve loan security is to grant loans only to established film companies which have a track record of success. Only in rare occasions when a producer could offer large security in marketable collateral would the banks finance an independent production.

Of course there are also banks which would finance independent production on an individual picture basis. But even in such a situation the banks would deal mostly with established producers. This is because the bankers believe a producer's past work is a better guarantee than their dazzling ideas in a new project. Instead of relying on a producer's aesthetic judgement, a bank would check out a producer's record before any loan is granted. In this way funds that would be available to a potential producer are limited. Consequently, potential entry into the film production industry is reduced.

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31. Canada, Department of Supply and Services, Bureau of Management and Consulting, Film Study (Ottawa, 1976), p.126, (hereafter cited as BMC, Film Study).

Finally, the general tendency in the industry to link financing activities with distribution guarantees imposes further undue difficulties onto a prospective producer in getting his production financed. As was noted, one of the basic requirements for a production loan is a distribution guarantee from certain distribution outlet. This guarantee is usually viewed as a good security for the loan since it will insure a certain return to the production cost. The unfortunate effect of such a requirement is that it imposes a higher barrier to entry into the industry, since potential producers could be screened out as a result of failure to gain access to established distribution facilities.

Distribution Aspects

As mentioned above, the close tie between financing and distribution of a film production results in a higher barrier to new entrants in the film industry. The adverse effect of the conjunction of these two functions on the new entrant could be made more explicit if the structure of the distribution branch of the industry is examined. To begin with, it may be restated that a film distributor is primarily a wholesaler serving as a go-between for the producers and the exhibitors. This function is carried out by a marketing organization consisting of sales offices called 'film exchanges' in the trade. The distributor is responsible for the promotion and the arrangement of playing dates in the theatres. Since the financial return to a picture can be minimized by booking it into as many theatres as possible, an efficient distribution of a picture should cover a large geographical area. In America, the beginning distributors have resorted to a system of employing many local exchanges to handle the selling of films. But since the 'exchanges' are performing similar promotional function for different films, it could be that economies of scale might be achieved if a company expands its production scale. This consideration thus leads one to believe the optimal scale of film distribution may be one that is built on a nation-wide basis. Indeed one study has made the following conclusion[32]:

> The minimum optimal scale of plant for of motion pictures seems to be a nation-wide marketing organization with a system of local sale offices. Duplicating the same marketing function in 20 to 30 major centers can be planned on a national basis. Scheduling of the movement of picture and co-ordination of local with national advertising is done best by a national distributor.

In the film distribution industry, there also seems to be a substantial plant capacity in a nation-wide distribution system. Furthermore, there is an innate pressure on such a system to distribute as many films as possible. This is because the larger the quantity of films distributed, the more it will help to offset the heavy overhead cost of the

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32. Michael Conant, op. cit., pp.118-119.

system. These costs in the mid-1970s amounted to three to four million dollars annually.[33] It has been found that this national distribution system can actually be fully utilized by promoting some 30 to 40 pictures a year.[34]

Even during the heyday of Hollywood, only some four to five hundred films were needed in the market. Since the 1950s, the demand of final product in the film market is further curtailed to less than four hundred pictures a year. For this reason, it is easy to understand that a significant 'percentage effect' of large scale operation is operating in this branch of the industry. Looking at the film distribution in the North America, it is no accident that in both Canada and the United States, film distribution is dominated by a few major concerns. This dominance by large firms can be shown by the fact that in 1954, the domestic rental of ten top distributors did 97% of the whole market's businesss.[35] An equivalent percentage share existed about a decade earlier. In the early 1970s, the major ten distributors still control over 90% of the American market. This is shown in Table 3-1. The market shares thus left for the minor concerns are very small. Mainly because of the concentration existing in

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33. Lee Beaupre, "How to distribute a film", Film Comment, Jul-Aug, 1977, p.48.

34. Michael Conant, op. cit., p.119.

35. Ibid., p.118.

Table 3-1

Percentage Share of American Distributors' Grosses

Major Film Companies

Company	1972	1971	1970
Paramount	21.6	17.0	11.8
Warner Brothers	17.6	9.3	5.3
United Artists	15.0	7.4	8.7
Columbia	9.1	10.2	14.1
Twentieth Century Fox	9.1	11.5	19.4
MGM	6.0	9.3	3.4
Universal	5.0	5.2	13.1
Walt Disney	5.0	8.0	9.1
National General/ Cinema Center	3.2	8.0	8.0
ABC/Cinerama	2.7	3.6	3.0

Source : Variety, as quoted in David Gordon, "Why the Majors are Major", Sight and Sound, Autumn 1973.

distribution, this branch of the industry could be viewed as the bottleneck of the industry.

Effect of Distribution Concentration on Production

Now, should a producer want to enter the film production industry, two alternatives may be open to him. He could decide either to enter into production while utilizing the existing distribution facilities in the industry. Alternately he can establish his own distribution outlet for his products.

i. Using Existing Distribution Facilities

Presumably, it could be to the advantage of a new producer to enter production without establishing his own distribution facilities and utilize the existing distributors as a sale force. The advantage would be a lesser capital outlay. But if a producer should decide to use the major distributor, he would suffer one obvious disadvantage, which is the possibility that he might have to pay a higher distribution fee than the integrated production unit of the distribution companies. This is due to the lesser bargaining power of the new ones as a result of their not yet established credibility.

At the same time because of the need of a distribution guarantee for the financing of a picture and a desire to get the best deal out of the distributor, the new producers would be hard pressed to find access to the major distributors who would be in a better market position to promote the pictures. However, to get a distribution agreement from these major companies, it is not a matter of routine. This is in fact an arena where much controversy in the industry has taken place. The problem is that film distribution is also a high risk business. Even when major companies promote an independent production, the distributor would still want to control the quality of the picture. Since the distributors are responsible for most of the advances on the outlay for publicity expenses, they therefore also share much of the risks in the project. Thus they do not necessarily accept every proposed project that comes before them. Even for those projects they accept, the distributors often reserve the right to intervene. This means that the new producers have to rely on the goodwill of the distributor. Thus we come back again to the adverse effect of the tie between distribution and financing and see the potential regulating power of the distributors on entry into the production field.

ii. Building One's Own Distribution Outlets

Possibly a new producer can go into production while integrating a distribution arm with the production activities. This would involve more capital outlay. But even if it is assumed that the potential producer has a desire to do so and has access to the extra amount of capital, the approach may still not be viable.

At the very least, both launching and the running of a distribution unit is very costly, if it is to be at the optimal scale. For example, for what is called a 'minor company', the Allied Artists in the United States has to spend an annual operational cost of more than $3 million just to maintain twelve sales offices and a number of executives. It is estimated that, in the 1970s, to launch a new distributor the initial capital outlay needed would certainly be not less than $5 million.[36] Obviously, a tremendous amount of money is involved here.

But for such operation, the companies need a steady supply of film products. This is needed to offset the high cost of operation. But there seems to be no easy solution. As we have observed, the 'percentage effect' of an efficient system of distribution is quite large. When several majors are handling some thirty to forty pictures each, annually, both the film supply and the market would be pre-empted very quickly. In the past the general lack of film product is the very reason why distribution had been foreclosed by the major companies.[37] Thus because of the concentration in the distribution branch, it made entry into film production

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36. Lee Beaupre, op. cit., p.48.

37. John McDonough and Robert Winslow, "The Motion Picture Industry: U.S. Vs. Oligopoly", <u>Standford Law Review</u>, 1949, no.1, p.398.

together with a distribution arm a questionable option.

In the United States, there were many examples of futile attempts to enter film production with a distribution unit. Two instances may suffice for the purpose of example here. In the 1940s, an independent producer, David O. Selznick, who was known for his picture "Gone With the Wind", attempted to distribute his own films by establishing a distributing arm, the Selznick Releasing Organization. At one point this organization had a staff of 26 in 31 exchange offices. However, over a period of four years and having only distributed half a dozen pictures, the organization was drastically reduced and finally closed with arrangements made again for Selznick's pictures to be distributed by the major companies.[38]

Another example occured in the early 1970s. A producer Tom Laughlin set up his own organization to distribute his films. According to Laughlin himself, his organization was made up of 110 employees, with six offices across the United States. The overhead was $375,000 a month. That was over $4 million a year.[39] However, the outcome of this undertaking was disastrous. He finally had to abandon the operation and transfer his films to the company he had complained

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38. Ibid., p.398; see also Lee Beaupre, op. cit., p.48.

39. Beverly Walker, "Billy Jack Vs Hollywood", Film Comment, July-August, 1977, p.30.

earlier of having mishandled his products, Warner Brothers.

These two instances are good examples of the difficulties in establishing a film distribution business. In both cases, it should be noted the producers were already established in the film trade. Even then they could not avoid failure in their distribution endeavors.

Market Conduct Barriers

As observed earlier, barriers to entry could be a result of market conduct of the existing firms. In the history of the American film industry, the practices of existing firms to secure market control appeared to be more a norm than exception. Thus the film industry had been noted for its tendency toward monopoly.

In view of the complexities in the behavioral barriers and the fact that this belongs more to the antitrust area, it may be appropriate for us just to highlight one important barrier in the film industry that is related to the action of the major companies. This is the attempt at market control through integration.

Soon after the development of moving pictures into an industry at the end of the last century, the industry was noted for the attempt to control the market by existing concerns through patent wars and interlocking arrangements. The first movie trust, the Motion Picture Patent Company

(MPPC), was established. By 1910, instead of a restoration of competitive forces, the industry witnessed some large scale economic warfare between powerful organizations attempting to monopolize the motion picture business. These battles took the form of both vertical and horizontal mergers directed toward the control of the distribution outlets.

i. Vertical Integration

In 1912, the only remaining film exchange outside the MPPC was the Fox Film company, a company operating both in distribution and exhibition. Finding no film supply from members of the 'trust', Fox reacted by going back into production. This was one of the earliest vertically integrated companies in the industry.[40] The integration was complete from production to exhibition. It was obvious that this integration was necessary for the Fox Company since this was the only way it could secure both the supply of film products and a market for its film outputs. This integration thus looked legitimate. However, excuses for vertical integration that took place later appeared to be dubious.

In 1914, out of the need for a new distribution system to promote the newly developed feature films, the first

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40. Benjamin Hampton, History of the American Film Industry (New York : Dover Publication Inc., 1970), p.102.

nation-wide film distributor, the Paramount Picture Corporation was formed. It consisted of eleven state-wide distributors. The policy of the Paramount was to advance capital to finance some affiliated independent producers in order to secure a steady supply of feature films and to distribute these products. To promote quality pictures, Paramount's original founders believed in the separation of the three branches of the industry. Thus Paramount held contracts with affiliated producers for the right to distribute their films for a term of 25 years.[41] Included in such contracts were two important feature film producers, the Famous Players Film Co. Inc., of Adolph Zukor, and the Jesse L. Lasky Feature Co. Inc.

The years around the First World War proved to be a booming period for the film industry. Tremendous growth was experienced and profits were high. By 1915, around two hundred or more producing and distribution firms were engaged in the industry.[42] Then in 1916 significant structural changes began. A new Famous Players-Lasky Corporation was incorporated by merging the Famous Players Co., the Lasky Theatre Company and twelve smaller producers.[43] And in order to achieve higher profits, the

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41. Ibid., p.152.

42. Ibid., p.4.

43. Michael Conant, op. cit., p.22.

Famous Players-Lasky Corporation also acquired 50 percent of the capital stock of the Paramount Company. This merger was made to snatch the majority of the profit retained in the distribution branch of the film business.

Having integrated the production and distribution operations, the Famous Players-Lasky Corporation began to turn out a large number of films that could fill an exhibitor's screen for a whole year. To sell these products, 'block-booking' was instituted. Under this plan, the exhibitors were required to take the films in 'blocks' if they were to get any films at all.

ii. Horizontal Integration

As a result of the dominant position of the Famous Players-Lasky Corporation position and its aggressive policy in selling their products, hostility was generated among the exhibitors. They resented having to buy pictures in blocks and the fact that they had to suffer economically from the low quality films. This dissatisfaction among the exhibitors thus led to the formation of a large theatre circuit.

In March 1917, 26 leading exhibitors operating quality theatres in key cities combined together to organize their own distribution channel, the First National Theatre Circuit. This organization was formed to combat the high prices and selling policy of the Famous Players-Lasky

Corporation. Their goal was to buy individual pictures with free choices, depending on the merits of the pictures. The organization was in fact used to achieve bargaining power in dealing with films. Furthermore in order to secure the better movies, the First National also offered financing to independent production units for the right to distribute their pictures.[44]

iii. Scramble for Theatres

The rise of the First National and its entry into financing the production of pictures had significant consequences for the industry. The control by the First National of some 3400 theatres between 1919-21, many of which were important first run houses in key cities, posed serious threats to the larger producer-distributors. Without access to these bigger and better theatres, the market for the producers would be threatened. As a result, Famous Players-Lasky Corporation embarked on a program for the control of theatres. From early 1919 onward, this company pursued a rigorous policy of buying and building theatres. Some of the purchases were aimed at the members of the First National.[45] By June 1926, Famous Players had interests in 368 theatres in the United States.

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44. United States Temporary National Economic Committee, op. cit., p.5.

45. Benjamin Hampton, op. cit., chapter 12.

The Famous Players-Lasky Corporation's entry into the exhibition branch finally meant the complete integration of the three branches of the industry. The net result was that other major companies were forced to undertake the same ventures. Vertical integration became a must for the rival companies to stay competitive. Loew's Inc., a theatre operator, for example, had to integrate backward by merging with the Metro Corporation to secure its production and film supplies in 1920. Then in 1924, Loew's went further into the production activities by buying two more production companies, the Goldwyn Picture Corporation and the Louis B. Mayer units.[46] With these purchases, Loew's became a fully integrated company. The First National was also forced to buy its own production unit and became an integrated company known as the Associated First National.

iv. Overall Effect of Integration in the Film Industry

With the three branches of the industry being fully integrated, the industry by the late 1920s had developed into a complicated operation. It was characterized by heavy financial requirements.

Unlike the major companies, most independent concerns did not have access to capital financing from Wall Street. Since the cost of undertaking the three branches of the

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46. See Tino Balio, The American Film Industry (Madison: University of Wisconsin Press, 1976), p.114.

industry involved more capital outlay, many independents were thus forced out of business. Thus, by this time, the industry underwent a dramatic structural change from a relatively competitive industry to an oligopoly. From then on the industry was to be dominated by five major and three minor companies.[47]

These major companies by working together for their own interests in a semi-compulsory cartel fashion were able to carry out their restrictive practices and to monopolize the industry.[48] For the next two decades competition was virtually eliminated. In 1948 the structure was loosened by a court-ordered divesture of theatres from production/distribution operations.

III. CONCLUSION

In the studies of industrial organization, barriers to entry could be classified into two main categories : those resulting from structural elements of an industry and those resulting from market conduct of existing firms.

Structural barriers may result from economies of scale, product differentiation and absolute cost advantage considerations. In manufacturing industries, studies have

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47. Tino Balio, op. cit., pp.213-214.

48. Robert Brady, "The Problem of Monopoly",<u>Annals of the American of Political and Social Science</u>, November 1947, 254, pp.125-136

found that economies of scale and product differentiation play a more important role than the absolute cost advantage. In the area of market practices, barriers could arise as a result of existing firms' pricing strategy, legal measures, exclusive dealing and the degree of vertical integration.

Applying these general theoretical tools to the study of the film production industry,we have some interesting observations. Firstly, in contrast to manufacturing industries, economies of scale and product differentiation may not be too critical as barriers to entry into this service industry. Absolute costs, in terms of restricted availability of capital to new or unknown producers as a result of risk factors in the industry, and inaccessibility to distribution, turn out to be the overriding factors in regulating entry into the production sector of the industry.

At the same time, using the United States experience as an example, barriers as a result of market conduct are important in so far as the degree of vertical integration is concerned. The tendency toward monopoly has led American companies to undertake complete vertical integration from production to exhibition. In this way the entry-discouraging aspect of the distribution stage is carried backward to the production stage. Also vertical integration reinforces the difficulties created by the large capital requirement for entry. In the U.S. this entry limiting effect was remedied only when in 1948 complete vertical integration was ruled illegal.

Chapter 4

An Overview of the Canadian Film Production Industry

A brief introduction to the characteristics of the film industry was made in Chapter 2. In this chapter, attention will be focused on the Canadian film industry. The review will start out by looking at the final market, i.e. exhibition and distribution in the Canadian feature film industry, including the characteristics of the industry's audience. The types and origins of film products that are shown in Canadian theatres will be examined. Finally, the structure of film exhibition and distribution companies in Canada will also be discussed.

Having looked at the final stage of this Canadian industry, a section will be devoted to its early stage, the production sector of the industry. In this section will be a survey of the units and agencies that are involved in film production in both the public and private sectors. Here will be identified the structural elements of the production units as well as the characteristics of their output.

The chapter will conclude with a look at feature film production from a historical perspective and identify some of the difficulties for Canadian entry.

I. THE FINAL MARKET : EXHIBITION AND DISTRIBUTION

In Canada, movie going appears to be one of the most popular leisure time habits. At least ten percent of the expenses spent by an average family on leisure time goods and services goes to the movies. Like most other countries, the frequency of movie attendance here is also a function of age and education. Evidence again bears out the fact that the film industry is operating in a youthful market. Table 4-1 shows the percentage of people in each age bracket in Canada that attends movies.

Table 4-1

Estimated Movie Attendance in Canada

By Age Group

Age	% of Attendance
14 and under	52
15-16	58
17-19	65
20-24	63
25-34	46
35-44	33
45-54	26
55-64	17
65-69	12
70 and over	6

Source :
Bureau of Management Consulting, Film Study, 1976, P.54, Table 2.

From Table 4-1, it is evident that people in the younger age group have a much higher tendency to go for the movies than the older groups. Generally, the strongest attendance patterns exist between the age 14 and 24. Well over half of the young people in these age groups attend movies. From the age group 25-34 onward, the incidence of movie attendance decreases as the age increases. The conclusion that the film industry works primarily for the young thus seems valid.

In comparison with other countries, the tendency of Canadian to see movies appears to be moderate. This is shown in Table 4-2 below.

Table 4-2

Comparative Average Annual Attendance

Canada and Other Countries

Countries	Average Attendance
U.S.S.R	19
United States	5
Canada	4
United Kingdom	3
Sweden	3

Source :
Bureau of Management Consulting, Film Study, 1976, p.52.

A. Market and Audience Characteristics

Market Size

For the country as a whole, the average of attending movies four times a year among Canadians has a significant effect. This means that Canada has a very limited base for industrial support. Having only a population of about twenty-five million, as compared to that of around two hundred and thirty-seven million in the United States and fifty-four million in the United Kingdom, Canada thus has a relatively smaller market for the industry than the other two English-speaking countries.

Unfortunately, this small domestic market is further fragmented into two distinct markets. These are the English-speaking Canadian film market and the French-speaking Canadian film market. In Quebec, the French-speaking Canadian filmmakers are pretty successful with their enterprises since their films are almost guaranteed a readily accessible market. This is a result of the protection they have because of their cultural difference from the English-speaking competitors, especially those from the south. However, outside Quebec, these films generally cannot do as well in the rest of the country. On the other hand, with the Quebec market preoccupied with French language film products, English film products from other parts of the country also lose some of the demand in the national market. Indeed, it was found that the English films made outside of Quebec seldom reach the market there.[1] The net effect of this fragmentation of the national market is a reduction in profit potentials for an English-speaking film and an increase in the risk factor in its production. As we shall see later, the small domestic market in Canada poses an important problem in the development of a Canadian film production industry.

The Audiences

As we have seen earlier, there was a constant drop of Canadian audiences in the theatre attendance in past decades. This of course is not unique Canadian phenomenon. The same development has taken place in both the United States and the United Kingdom. The significance of the drop is the effect on the composition of the audiences. Gone are the days when movie going was treated as family entertainment or as a common social event. With the rising popularity of television programming, it was found that most elderly people would rather opt for a quiet night at home than spending their time out in a cinema.[2] In time television developed into a mass medium taking over some of

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1. Canadian Films, Vol.VI, nos. 4/5, February/March 1975, p.3

2. The elderly people over 55 is reportedly viewing television more often than the average adults. See BMC, Film Study, p.75.

the role movie-theatres had played before. Left behind are people with more selective tastes. This helps to explain the youth orientation of the whole industry.

Table 4-3 shows an historic trend of cinema admissions and admission receipts. The table shows that by 1960 the industry had an annual admission of about 117.7 million which was about half of the number of admissions in 1950. The decline was pervasive all through the decade of the 1960s, dropping to about 90 million by the end of the decade. Since then admissions stablized somewhat around that level. However, when compared to the figure of some 236.6 million attendances in 1950, the 97.0 million turn-outs in 1975 is a dramatic 230% decrease.

But an even more remarkable aspect of the film business in the past decade was that despite the tremendous decline in attendance, after-tax box office receipts had actually been increasing. This is evident from Table 4-4. There were steady annual increases from early 1960s to the year 1975. The increase was from $69.9 million in 1961 to some $211.4 million in 1975.

The increase in admission receipts had been possible only because of a steady rise in admission prices. The evidence, as one might surmise from Table 4-3, suggests that demand for movies has been inelastic. This also falls into line with the conclusion that modern day moviegoers are a

Table 4-3

Canadian Cinema Admissions and Receipts

Year	Number of Total Admission in Million *	Admission Receipts After-Tax in $ Million
1950	236.6	85.0
1960	117.7	72.2
1961	107.4	68.9
1962	100.8	67.7
1963	97.9	71.6
1964	101.7	78.3
1965	99.9	85.1
1966	98.9	94.4
1967	97.6	103.6
1968	97.3	112.7
1969	90.2	118.0
1970	92.3	128.7
1971	-	-
1972	91.8	140.0
1973	89.0	150.6
1974	90.4	172.7
1975	87.0	211.4

Note : * Include regular theatre and drive-ins.

Source : Statistics Canada, Motion Picture Theatre and Film Distributors, nos. 63-207.

Table 4-4

After-Tax Admission Receipts in Canada, 1960-74

Constant Dollars

Year	After-Tax Receipts $ Million
1960	72.1
1961	72.4
1962	73.4
1963	74.8
1964	76.6
1965	79.1
1966	82.6
1967	85.9
1968	88.9
1969	92.6
1970	96.9
1971	100.0
1972	104.9
1973	111.7
1974	128.4

Note: Deflator - Prices of Personal Expenditure in Canada, 1971=100.

Source: BMC, Film Study, Vol. I. p.59.

group having very selective preferences.

Market Trend

Table 4-3 shows a steady increase in the after-tax receipts from 1960 to 1975. These numbers give an annual growth rate of 8% in the industry. However according to one government study,[3] the real growth of the industry over this period was actually 4% if the receipts were to be adjusted into constant dollars (using a deflator with 1970=100). The adjusted figure on admission receipts are listed in Table 4.

As we have seen, the data in Table 4-3 show a steady drop of paid admissions in absolute numbers. This had been the trend for the two decades 1950-1970. A stablized level of attendance was reached in the early 1970s. Without any radical development in the industry, it is therefore reasonable to expect only a marginal growth in paid admissions. In addition it should be noted that currently the industry is facing stiff competition with the development of new video equipment. This new technological development is fostering a new type of entertainment - home movies. Home movies could mean a further curtailment of the number of people willing to attend cinemas. How well the industry can maintain its business depends on its adjustment

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3. BMC, Film Study. See Volume I. Section 2.5.

to this new type of competition.

B. Origins of Film Supplies for Theatres

To substain the industry at the level we have described, the exhibition and distribution branches of the industry had to secure a good number of film products annually. The annual demand for film by exhibitors may range, for example, from a low of 623 films in 1967 to a high of 970 in 1977. Over the period between 1965 and 1977, an annual average of 728 films were actually distributed to Canadian cinemas.

One outstanding characteristic of films shown in Canada is their original sources. Most of the films are noted for their foreign origin. Tables 4-5 and 4-6 show the source of film supplies by country of origin. Respectively, Tables 4-5 and 4-6 show the absolute numbers and percentage of total feature films released in Canada over the past decade. From the two tables, it is apparent that well over 96% of the films were of foreign make, primarily coming from countries such as the United States and western European countries. Canada contributed a meager amount of about four percent.

Another important aspect of film supply which is shown by Tables 4-5 and 4-6 is the fact that the United States has long been the leading supplier of feature films in the Canadian market. Between 1965 and 1975 the United States

Table 4-5

Film Supplies in Canadian Cinemas, 1965-1975

By Country of Origin

Year	Total	U.S.	France	Britain	Italy	Canada	Others
1965	676	284	169	41	94	12	76
1966	637	228	157	62	108	11	71
1967	623	210	148	70	106	8	81
1968	649	314	121	52	80	8	74
1969	669	253	34	165	98	10	109
1970	786	291	90	131	131	53	108
1971	-	-	-	-	-	-	-
1972	791	294	134	71	116	35	69
1973	811	356	137	61	83	33	141
1974	901	355	152	67	57	32	238
1975	739	315	124	52	79	24	145

* not Available.

Source : Compiled from Statistics Canada, Motion Picture Theatres and Film Distributors, Nos. 63-207.

Table 4-6

Film Supplies in Canadian Cinemas, 1965-1975

Country of Origin in Percentage

Year	U.S.	France	Britain	Italy	Canada	Others
1965	42.0%	25.0%	6.1%	13.0%	1.8%	11.2%
1966	35.8	24.6	9.7	17.0	1.7	11.1
1967	33.7	23.8	11.2	17.0	1.3	13.0
1968	48.4	18.6	8.0	12.3	1.2	11.4
1969	37.8	5.1	24.7	14.6	1.5	16.3
1970	37.0	11.5	16.7	14.4	6.7	13.7
1971 *	-	-	-	-	-	-
1972	37.2	16.9	9.0	14.7	4.4	8.7
1973	43.9	16.9	7.5	10.2	4.1	17.4
1974	39.4	16.9	7.4	6.3	3.6	26.4
1975	42.6	16.8	7.0	10.7	3.2	19.6
Average	39.8	17.9	10.7	13.0	3.0	14.9

* Not Available.

Source : Derived from Table 4-5.

had been enjoying roughly a ten year average of 40% of the Canadian market. These data therefore confirm the conventional wisdom that Canada is one of the important foreign markets for the United States' film industry. Canada had indeed by 1974 become the top market among Hollywood's fifteen major foreign markets.[4]

The heavy consumption of foreign film products in Canada has one significant consequence in the heavy film rental payment to foreign suppliers. This causes a large outflow of Canadian funds. The total film rental payments abroad amounted to some $31.3 million in 1969. By 1973 this amount has risen to $40.5 million. A majority of these payments went to the United States. The amount it received amounted to almost 96% of the total film rental remittances. This is shown in Table 4-7 which gives a detailed breakdown of Canadian payments for 1969 and 1973.

In terms of revenues, Table 4-7 shows the dominance of the American film industry in the Canadian market. While the American films played in Canada never exceeded 50% of the total films consumed over the ten-year period 1965-1975, as shown in Table 4-6, it would still be safe to deduce that film rentals going to the United States during these years would have been over 90% of the total. This statement may

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4. Variety, June 25, 1975, as quoted by BMC, <u>Film Study</u>, Vol. I, p.65.

Table 4-7

Canadian Foreign Film Rental Payments

1969 and 1973

	1969		1973	
	($ Million)	%	($ Million)	%
United States	28.9	92.3	38.8	95.8
E.E.C.	-	-	0.9	2.2
United Kingdom	2.0	6.4	0.4	1.0
Others	0.4	1.3	0.4	1.0
Total	31.4	100.0	40.5	100.0

Source :
BMC, Film Study, Vol. I, Table 7 for absolute numbers.

be warranted because the film rentals earned by the United States during the period 1963-1973 actually increased. This rising trend is shown by the figures in Table 4-8. Together with data in Table 4-7, Table 4-8 gives an approximation of the dominant role played by the American film business in the Canadian market.

Structure of Canadian Film Distributors and Exhibitors

i. Numbers of Firms and Employment Patterns.

According to Statistics Canada, in 1975 there were some 1488 theatres and 85 film distributing establishments in Canada. Of the 1488 theatres, 1173 were regular four-walls and 315 were drive-ins.

The exhibition and distribution business as a whole employed 17,114 people. The distribution of people employed was as follows: 12,786 people in regular theatres, 3250 in drive-ins and 808 in film distributing exchanges. These figures included both the full-time and part-time employees. The salaries thus paid to all the employees in the distribution and exhibition end of the film industry amounted to $56.9 million a year.

Thus in terms of numbers of employees, and also in terms of salaries paid, the distribution branch requires a much smaller operation scale than the exhibition branch. This conforms to the experience of film industries in other

Table 4-8

U.S. Gross Revenues in Canadian Film Market

Year	$ Million
1963	16.8
1964	21.2
1965	23.2
1966	26.4
1967	28.1
1968	30.0
1969	27.7
1970	27.4
1971	29.4
1972	38.7
1973	39.2

Source : BMC, Film Study, Vol. I, Table 68.

countries. Table 4-9 summarizes these data to give a clearer picture of the difference in the scale of operation between two sectors of the industry.

ii. Type of Companies

In Canada, companies engaged in film distribution and exhibition activities can be roughly classified into two main types. They are the small independent theatre operators/distributors and the major theatre circuits/distributors. The structure of firms in this industry can be termed oligopolistic.

(a). Exhibition

In theatre operations, there is always a tendency toward larger circuits of theatres. In some cases this is a result of the companies' desire to achieve a degree of bargaining power in their dealings with film distributors or producers. In other cases, the holding of a large number of theatres may be a means by which exhibitors endeavor to control the final market of the industry.

The tendency toward large circuits of theatre operation is still evident today in this Canadian industry. Among the somewhat over a thousand theatres, several companies hold circuits of theatres. In 1965 these major circuits operated over 75% of all theatres in Canada and took in around 75% of box office receipts. The figures for today would likely be

Table 4-9

Aggregate Scale of Operation

Distribution and Exhibition

1975

(a) Absolute Numbers

Branches	No. of Establishment	No. of Employees	Salaries Paid
Exhibition	1,488	10,308	$ 48,517,000
Distribution	85	808	8,386,000
Total	1,573	11,116	56,903,000

(b) Percentage Distribution

Exhibition	94.6%	95.3%	85.3%
Distribution	5.4	4.7	14.7

Source : Absolute statistics are from Statistics Canada, _Motion Picture Theatres and Film Distributors_, no. 63-207. Percentage distribution is derived from (a) above.

about 85% of the total.[5] The remainder of the other theatres is made up mainly of small independent houses. Thus in the final market of the Canadian film industry the existence of several major theatre chains again made the structure more oligopolistic. Table 10 lists some of the most important theatre companies and shows the number of theatres held under each chain.

Table 4-10

Major Circuits of Theatres in Canada

Company	Number of Auditoriums
Famous Players Ltd.	403
Odeon Theatres(Canada) Ltd	123
Canadian Theatres	65
Theatre Holdings	65
Prairie Allied	60
Total	816

Source : BMC,Film Study, Vol. III.

Table 4-10 reveals that out of a list of five theatre circuits, there existed two most important theatre chains, in terms of auditoriums held. They are Famous Players Ltd. and Odeon Theatres (Canada) Ltd. Since it is unavoidable to talk about these two theatre companies when the whole structure of the Canadian film industry is concerned, it may

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5. BMC,Film Study, Vol.III, p.275.

be worthwhile here to give a brief look at these two companies.

1. Famous Players Ltd.

Famous Players Limited is one of the oldest theatre companies in Canada. It originated in the 1920s, the time when the major American film production companies were struggling among themselves for theatre outlets. It was originally owned by an American distributing company, the Paramount Pictures Corporation (Canada) Ltd. However, as a result of the ruling from the Canadian Radio and Television Commission in 1971, Famous Players was directed to divest some of its interest in television and cable companies. Because of this ruling the structure of Famous Players was reorganized. It changed into a subsidiary company with 48.4% owned by the Canadian Cable Systems and 51% owned by Paramount.[6]

During the period 1965-1975, as a result of shrinking business conditions, Famous Players adopted a rigorous policy of consolidating its theatre interests. This included buying outright, theatres which formerly had partnership relations. In the same period it also closed down a lot of theatres which were not economically viable.

The buying of theatres included the purchase of the

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6. BMC, Film Study, pp.275-276.

Unlimited Amusement Corporation which had 31 theatres in 1965, the United Century Group which had 33 theatres and the Consolidated Theatres Group which held several first-run theatres in Montreal.[7] As a result of the purchases, these new theatres then came under the direct control of the parent company, Famous Players Ltd. Films were booked and managed directly by Famous Players. With this aggressive policy Famous Players thus ended up with control of 403 theatre auditoriums in Canada. One of the main features of the film products shown in this theatre chain is their foreign origin. Almost 100% of the product were from Paramount Distributions, Warner Brothers Distributors and United Artists. Other important supply included pictures from Universal (one-third of its product) and Twentieth Century Fox (two-thirds).[8] In effect most of the films shown were products from the United States.

2. Odeon Theatres Ltd.

Even though the Odeon Theatres Ltd. is the second largest theatre operating company in Canada so far it has in comparison to the Famous Players a markedly smaller holdings of theatres.[9] In 1976 Odeon operated 123 theatres in total. With only seven exceptions nearly all theatres in

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7. Ibid., pP.276-278.

8. Ibid., p.278.

9. Ibid., p.280.

this chain were wholly-owned and operated. Again like the Famous Players, it is also foreign-owned. It belonged to a British company, the Rank Organization Ltd.

Actually the Odeon chain has been in existence since 1941 and since the Second World War it has been expanding. Its expansion was stopped with the coming of the television which depressed market conditions. It thus remained a relatively weak competitor to Famous Players. The Odeon Company also has a special arrangement with major distributors in securing its film inputs. The company is reportedly playing hundred percent of Columbia's products, two-thirds of Universal's and one-third of Twentieth Century Fox's. Thus the film products shown in this second largest theatre circuits in Canada are again foreign-oriented.

(b). Distributors

Statistically the number of distributing firms in Canada has been rising in the past decade. This is shown in Table 11. By 1975 there were eighty-three firms engaging in film distributing activities.

However, these firms could be classified into two main categories. They are the major companies and the independents. The majors are relatively small in number and operate on a bigger scale. They operate mostly on the national or international level. The independents on the other hand operate on a much smaller scale, specializing

Table 4-11

Canadian Film Distribution Industry *

Year	No. of Firms	No. of Exchange	No. of Employee	Salaries In $ 1,000
1964	60	129	807	4,082
1965	63	128	767	4,011
1966	62	126	803	4,425
1967	57	116	763	4,667
1968	56	120	761	4,733
1969	52	117	846	5,253
1970	53	112	737	5,305
1971 **	-	-	-	-
1972	63	121	681	5,787
1973	68	126	732	6,460
1974	82	142	726	6,980
1975	85	144	808	8,386

Notes : * Between 1964 and 1970, these figures reflect total numbers of both male and female workers. From 1972 onwards, it shows part-time and full-time employees.

** Not available.

Source : Statistics Canada, Motion Picture Theatres and Film Distributors, no. 63-207, 1970 and 1975.

mostly on a regional basis.

Essentially the major companies included two Canadian distributors and seven American distributors. Together they formed the Canadian Motion Pictures Distributors Association (CMPDA). The two Canadian owned companies are the Astral-Bellvere-Pathe Company and Bellevue Film Distribution (Avo-Embassy). The seven major foreign owned companies are Columbia Pictures of Canada, International Film Distributors Ltd, Paramount Pictures Corporation (Canada) Ltd, Twentieth Century-Fox Corporation, United Artists Corporation (MGM Canada Ltd), Universal Films (Canada) and Warner Brothers Distributing (Canada).[10] One outstanding aspect about the majors is their access to a steady supply of film products which primarily comes from the United States. This is possible because of their association with production companies, through either franchise or distribution agreements with parent companies in the United States. These companies are also noted for their mutual cooperation in matters such as sharing regional or branch office and employee salaries.

For the rest, the smaller independent distributors make up the remaining some seventy firms. Though large in number they operate on a much smaller scale, mostly on the regional or national level.

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10. BMC, <u>Film Study</u>, Vol. III, p.257.

The disparity of power between these two groups of firms is obvious when we compare their scale of operations. We can compare them in terms of employment and also the film rental receipts they received from exhibitors.

Statistics on employment and rental receipts for these two groups are listed in Tables 4-12 and 4-13. Apparently, in 1974, when these statistics were available the majors had a total of 250 employees while the rest of the independents had 381. Expressed in percentages, the majors employed about 40% of the total workers. However, in the same year, film rental going to the majors was $56 million, about 83% of total receipts in the distribution business. It also meant that only a meager 17%, about $12 million, was left to be shared by the independents. These statistical data therefore reveal the dominant position held by the majors over the independents. This oligopolistic nature of the distribution industry, as will be shown later, has had an unhealthy effect on the Canadian film production industry.

Table 4-12

Size of Distributors, 1974

	No. of Employees	% of Total
Members of C.M.P.D.A	250	39.6
Independents	381	60.4
Total	631	100.0

Source : BMC, Film Study, Vol. III, based on Canadian Motion Picture Distributor Association (C.M.P.D.A) survey estimates.

Table 4-13

Film Rental Estimates, 1974

By Types of Distributors

	No. of Films Distributed	Rentals in $ Million	% of Total Rentals
Members of C.M.P.D.A	637	56.0	83 %
Independents	264	12.0	17
Total	901	68.0	100

Source : BMC, Film Study, Vol. III, p. 273.

II. CANADIAN FILM PRODUCTION INDUSTRY

In the Canadian film production industry, there is a mixture of both public and private endeavors. In the private sector, in a sharp contrast to the distribution and exhibition activities, the Canadian producers are noted for their very limited size of operation. Even though this statement is essentially addressed to the feature film industry, it is also applicable to the whole spectrum of other film products. This includes the industrial, sponsored and educational films. For example, according to Statistics Canada, there were 280 establishments in the private sector engaged in the motion picture production and laboratory activities. These concerns as a whole employed 1562 people paying them total salaries of $17.1 million. During the same period these producers took in a gross revenue of $44.2 million.[11]

On the other hand, according to one federal government study, an estimated $111 million direct expenditures were incurred in 1975 in the public sector for the production of films. This included the production activities of the federal agencies and provincial agencies.[12] The public sector was therefore responsible for almost two-thirds of

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11. Statistics Canada, Motion Picture Production, 63-207, 1975.

12. BMC, Film Study, Vol. II.

the total expenditures in Canadian film production activities. Also, because of the governmental agencies playing both the role of being film producers and film purchasers (as represented by the Canadian Broadcasting Corporation), it has exerted a dominating influence on film production activities. Table 14 gives a relative comparison between the private and public film production volume in 1975. The data were collected by the BMC Report based on empirical studies.[13]

A. Public Sector

In Canada, governmental agencies which have taken up film production are found both at the provincial and federal level. The provinces are represented by various departmental agencies whereas the federal government is represented primarily by the National Film Board and the Canadian Broadcasting corporation.

Provincial Agencies

The contributing factor that motivates provincial

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13. Two observations should be made on the use of this table.(i) Because of the generally incomplete information both on revenue and expenditure in the private and public sector, the BMC studies has resort to use the revenue figures for the private sector while the public sector was measured by direct cost expenditure. (ii) The discrepancy between the $38.8 millions of revenue for the private sector as listed in this table and the $44.4 millions we quoted earlier from Statistics Canada was because, when the BMC studies was done, no actual number was yet available and thus an estimated number was used.

Table 4-14

Estimated Film Output In Canada, 1975

$ Million

Private Sector :		
CTV network	20.0	
Film Sponsored by NFB	2.2	
Industrial, Documentary and Commercial	6.0	
Educational	2.0	
Feature Films	8.6	
Total Private	38.8	38.8
Public Sector :		
Federal -		
CBC	65.0	
NFB	17.0	
Total Federal	82.0	82.0
Provincial -		
OECA		7.0
OFQ		12.0
Others		10.0
Total		149.8

Source :
BMC, *Film Study*, Vol. II, Table 2.

departments to come into the business of film production is their need for a medium for educational and informational purposes. Rather than relying on outside services, some of these agencies resorted to building up their own production facilities and allocating part of their budget for production expenditures. For example, the Ontario Educational Communication Authority (OECA), an agency of Ontario, was created in 1970 and by 1974 reportedly had an operating budget of $6,000,000 for film production.[14] In addition, it has developed a full network of television broadcasting of its products.

Similarly the Department of Agriculture in the Province of Manitoba has since 1960 produced close to 30 documentary films for relaying educational information to Manitoba farmers.

National Film Board(NFB)

The National Film Board was first created in 1939 as part of the Canadian war effort. It was placed under the control of the Secretary of State but in practice the NFB operated pretty much like an independent agency.

As a federal agency, the NFB was given a mandate primarily to represent the Government of Canada in dealing

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14. See Manitoba Department of Industry and Commerce, Development of the Film Industry in Manitoba, Appendix D.

with matters related to film activities. It was also mandated to produce and distribute films which would interpret Canada to both Canadian and foreign nationals.[15]

As a result of this authority, the NFB has since the early years become the producer of most documentary films on Canada and has won a world-wide reputation. With the advance of television in the 1950s, the NFB also expanded into production of films for television programming. In 1963 the NFB broke further new ground by moving into feature film production.

By the middle of the 1970s, as Table 4-14 shows, the NFB had grown to a level which included an estimated annual expenditure of $17.0 million. Its list of film products included documentaries, feature films, fictional shorts, television series, theatrical shorts, animated films, sponsored films community programs and multi-media products.[16]

However, in addition to the important role as a film producer, the NFB with its enormous holdings of advance studios and production facilities has over the years become the de facto training ground for Canadian film technicians and creative talent. It had been successful in producing

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15. See National Film Act, Section 9 for a detailed list of the mandate.

16. BMC, Film Study, Vol. II. p.176.

numerous film directors, cameramen and technicians who achieved international reputation.[17]

The Canadian Broadcasting Corporation

The Canadian Broadcasting Corporation is a federal agency which is responsible for a network of national television programming services. To this end the CBC has been playing the role of being both film producer and exhibitor.

In order to maintain a constant supply of film programs, the CBC has to maintain a stable of production staff and studio facilities over a network of television stations. These activities involve a relatively large amount of operating expenditures. Especially because of higher demand for Canadian content in its program the CBC has since 1968 experienced a substantial increase in its program production. By 1973 CBC was estimated to have spent an annual expenditure of $65 millions in film and videotape production.[18]

There are also occasions when the CBC would purchase or commission program production from the private sector. However its ability in doing so is handicapped by union

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17. William Litwack and Henry Mintzberg, Manpower Training in the Canadian Screen Industry (Montreal, 1973), pp.51-52.

18. BMC, Film Study, Vol. II, p.171.

agreements with its broadcast staff and technicians. It is estimated that a very limited amount of $8 million a year was spent by CBC on outside production[19].

Effects of Public Production on Private Sector

As a result of extensive involvement by public agencies as described above, over the years there have been two main undesirable effects felt by the private sector in the production end of the industry. Firstly, there is unfair competition. This comes about because of the fact that the public agencies are not obligated to make profits. With the support from public funds, the public agencies are, able to price their products far below the prices charged by private producers. Given this disadvantage, it is not surprising that the private sector can hardly compete with the public agencies.

Secondly, the market demand for film production from the private sector is further reduced as a result of the flooding of the market by products from the public sector. Because of the general "make" policy pursued by the CBC, a large part of the television market is inaccessible to the private producers. In the field of educational films and sponsored films, the abundant supplies of NFB films in the school systems also effectively reduces the need of films

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19. Ibid.

from outside.

For such reasons the Canadian film producers in private sector have long been overshadowed by the public sector and contribute a minimal share of output, as shown in Table 14.

B. Private Sector

Because of stiff competition from the public sector and foreign producers, the Canadian film production activities in the private sector can really be termed very small by any industrial standard. By the mid 1970s it was estimated that the annual production expenditures would usually not exceed $50 million.

Total Number of Firms

The number of film-producing firms in any year is influenced mainly by the cycle of demand. Any increase in demand would tend to increase the number of firms. The opposite is true also . For this reason the numbers of firms is always in flux. But according to the BMC Study, by the end of this period, there was only a core of 150 film production units which had been actively engaged in the industry.[20]

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20. BMC, Film Study, Vol. II., p.123.

Size of Private Units

According to statistics available on the film industry from current literature, the private producers have been operating on a very small scale either in terms of output, employment or investment.

(i) Output

The measurement of output in the film production industry can either be the physical product in terms of feet-length of screening time or dollar value of revenue figures. However statistics on the latter index has been more readily available than the former and therefore are more useful for practical purposes.

According to Statistics Canada, in 1976 there were 271 establishments engaging in motion picture production or laboratory operations. Of these 271 establishments, 203 fall in the class of units having an annual revenue of less than $250,000. In other words, almost three quarters, or 74.9% of the units in the industry, belonged to this class. Only 21 units, or 7.7% of the total, have an annual revenue above $1 million. These statistics thus portray an industry which has a large distribution of small scale producers with only a few sizable ones. Table 4-15 shows the detailed breakdown of firm size distribution by revenue in 1976.

Table 4-15

Distribution of Private Production Units

Canadian Film Industry

1976

Revenue Group	No. of Firms	% of Total
Less Than $50,000	109	40.2
$50,000-$99,000	36	13.3
100,000-249,000	58	21.4
250,000-499,000	26	9.7
500,000-999,000	21	7.7
1,000,000 and more	21	7.7
Total	271	100.0

Source :
Statistics Canada, Motion Picture Production, 63-206, 1976.

(ii). Employment

The pattern of employment again paints a picture of the film production industry being occupied by a large number of small scale production units. In 1976, the 271 units employed a total of 1609 permanent employees. Thus the average number of permanent employees within the industry is about 6. But an outstanding feature of the statistics was that in the class of firms having revenue less than $50,000, a total of 154 people were employed by 109 firms. This reveals the existence of a large number of single-person operations. Also, it has been found that three-quarters of the firms have less than 10 permanent employees and only 12

% have more than 20. The percent distribution of firms with number of permanent employees is shown in Table 4-16.

Table 4-16

Distribution of Film Units by Employees

Permanent Employees	% of Total Firms
Less than 5	38
5-10	37
10-20	13
20 and more	12

Source : Empirical studies from BMC, Film Study.

In addition to permanent employees, the industry also tends to retain the service of freelancers when market demand induces production increases. The practice of using freelancers is a natural response of the production units to the fluid environment and is a move to help reduce operational costs. Some 50% of firms was estimated to have retained up to 10 freelancers annually. Another 35% used between 10 and 20, and only 10% of the firms used more than 20.[21]

(iii). Investment and Entry

In the film industry, there has long been in existence a sector of service specializes in film production equipment and facilities such as studios and laboratories. Thus it is

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21. Ibid., Vol. II., section 3.

not a necessity for a film production company to enter the business with large investments in fixed capital equipment. Indeed most production units often resort to these special services and rely on the outside resources. For this reason, most production units have relatively low fixed capital investment by most industrial standards. It is estimated that 30% of the firms have $50,000 or less in investments. Another 30% have between $50,000 and $100,000, while 25% lie in the range of $100,00 and $250,000. Only 15% of total firms have an investment of more than $250,000 in their fixed capital.[22] Again statistics show a tendency of small scale operations within the film production industry.

Thus, in conclusion, there seems to be a correlation between output, employment and investment in the private sector of the Canadian film production industry. All in all they point to a private industry that is characterized by small scale operations, both in the aggregate and in the individual sense.

Types of Film Output

The producers in the private sector are involved in production activities that span both the theatrical and non-theatrical market. The production units are noted for their diversification which covers such output as sponsored

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22. Ibid.

films, feature, documentaries, educational films and commercials. According to the BMC studies, only 8% of the toal units have restricted their operation to one single product.[23] The percentage distribution of film output in the whole industry is listed in table 4-17.

Table 4-17

Percentage Distribution of Canadian Films

Film Categories	% of Total
Sponsored Film	22
Product for Theatrical Market	16
Television - documentaries	21
- series and specials	9
Education Materials	16
Commercials	11
Others	5

Source : BMC, *Film Study*, Volume II.

Feature Film Productions

From Table 4-18, it is obvious that the majority of film production in the private sector was in non-theatre markets. Eighty-four percent of the industry's production effort was spent in that market. Only a meager sixteen percent of outpout was for the theatre market.

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23. Ibid., p.152.

Looking at the industry as a whole, Table 4-14 showed that in 1975 there was $8.6 million worth of feature film output out of an industry total of $149.8 million. This means that feature film's output from the private sector only contributed to 5.7% of the total film output.

These data thus confirm the impression that Canadian film producers depend mostly on the non-theatre products for their survival in the industry. The sponsored films and commercials had become what the industry termed as "bread and butter". Feature film on the other hand is generally avoided and becomes an occasional venture when some of the private producers could afford to take the risks. It was estimated that only about 35% of the film producers had at one time or another engaged in the production of at least one feature film.[24]

Table 4-18 showed the number of feature film output between 1964 and 1975. Realizing that an average of 728 films were distributed annually in Canada over the same period, one would agree on the limited contribution the Canadian producers have been able to make to the feature film market.

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24. Ibid.

Table 4-18

Number of Production Companies and Output

1964-1975

Year	No. of Companies	Total	Film Outputs Private	Public
1964	71	6	3	3
1965	74	2	2	0
1966	82	6	3	3
1967	93	7	3	4
1968	95	7	5	2
1969	89	19	8	11
1970	112	25	15	10
1971 *	-	-	-	-
1972	139	19	14	5
1973	143	32	31	1
1974	187	28	27	1
1975	280	36	34	2

Source : Statistics Canada, Motion Picture Procution, no. 63-206.

* Not Available.

C. Feature Film Production : A Historical Perspective

The scarcity of Canadian production of theatrical feature films is reflected in both Tables 4-14 and 4-18. Actually this phenomenon has been long standing in the industry. From a historical point of view, Table 4-18 also indicates a long trend of limited production. Indeed before the coming of government assistance on the feature film industry, the production of features, especially in the English language films, is almost unnoticeable.

From the very beginning there were always attempts to produce Canadian feature films.[25] But from the early 1910s to the 1940s Canadian film making was dominated by foreign companies making films about Mounties and the Canadian North. Later it was dominated by those so called 'quota' films to fill the British market. Canada being a member of the Commonwealth became the ideal location for the production of the 'quota' pictures. After the war, a Canadian feature film industry seemed to have begun in Quebec. Some sixteen features were made in a period of ten years,[26] which incidentally were mostly commercially successes, making their profit mainly in Quebec alone. But, with the advance of television, further development of these

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25. Peter Morris,(ed.), Canadian Feature Films (Ottawa: Canadian Film Institute), Part I, p.iv.

26. Ibid, Part II, p.iv.

endeavors was hindered for another decade. In the rest of the dominion there were always sporadic attempts to make English language films. However, most of these efforts ended with financial disaster to their backers.[27] The main problem is that few of these productions really gained wide distribution and few Canadians could see them.

In such an environment Canadian production of feature films was limited. Thus by 1967, out of the $22 million already spent by the private sector on film production, less than half a million dollars was spent on the making of feature films.[28] The virtual non-existence of a Canadian feature film production industry by the late 1960s began to stir up concern in the country. Both the private and public sectors felt a need to establish a Canadian feature film industry with its own identity. Efforts were made in that direction. These efforts finally culminated in the active government support of the Canadian feature film industry with the establishment of a crown corporation, The Canadian Film Development Corporation in 1967-68.

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27. CFDC, Annual Report, 1968-69, p.6.

28. Ibid.

III. BARRIERS TO ENTRY INTO CANADIAN FEATURE FILM PRODUCTION INDUSTRY

As we have observed, historically there was a lack of definable Canadian feature film production activities. In the decade that followed the establishment of the Canadian Film Development Corporation, large investment in film production was made with the public assistance as the spearhead for private productions. These investments however have not yet yielded a full-fledged feature film production industry that is strong and independent of further governmental assistance. It is therefore not surprising when one studies the recent literature on the development of this Canadian industry that one finds there is controversy and a sense of disappointment over the public policies. In order to facilitate a better understanding of what future options are available for public policies, it may be helpful to direct our attention to factors which have been acting as barriers to the Canadian entry into the industry. Only through a good grasp of these factors can a meaningful discussion on public policies be possible.

A general survey of the material written on the industry yields barrier factors that can be roughly classified into five main groups. They are (1) product differentiation and the aspects of American competition,(2) limited Canadian market size, (3) factor of production aspects, (4) financing difficulties and (5) inaccessibility to the distribution system.

A. Product Differentiation and American Competition

Since feature films belong to an area where each individual product is different from the other and the value of production depends on the merit of each individual film, one might expect the advantage of an established producer as a result of brand name preference would be limited. Indeed given the vacillating nature of film demand, there seemed to be no guaranteed formula for the success of an assembly of films even from a single producer. For this reason one would not expect product differentiation to be an important deterrent force working against potential Canadian producers.

However, to understand the current difficulties Canadian film producers have with product differentiation competition, one has to recognize the influence of American products. As one federal government study reports,[29] because of the similarities in language and cultures and because of a general absence of Canadian productions in earlier times, the Canadian demand for film entertainment

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29. The Social Survey Research Centre Limited, An Assessment of the Problems in the Distribution of Canadian Films. This study was done for the Film Distribution Committee in the Under-Secretary of State Department. (Hereafter cited as Survey Center, Assessment.

has been largely shaped by their earlier exposure to American films.

It is noteworthy that there were significant differences in philosophy between the Canadian and American film production. The American industry, since its beginning at the end of the last century, was a self-developed one following a competitive-commercial line. In addition to being 'artistic' American film producers have been termed 'commercial'. They are in fact noted for their care for 'international appeal'. One common way to achieve this end was to promote high quality films which usually means a film packed with stars and produced with a relatively high budget. Thus there were American films budgeted with tens of millions of dollars. According to industry estimates, the average feature production cost of the U.S. major companies in 1974 was more than $2.5 millions. By 1976 this production cost was reported to have risen to $4 millions.[30]

On the other hand, the Canadian production industry was started with a different perspective. Apparently around the late sixties, there were developments in the film industry that led to more independent films produced with low budgets. At the same time the most esoteric films found

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30. See the Statistics Section in the 1979 International Motion Picture Almanac (New York: Quigley Publishing Co. Inc).

receptive audiences. With these developments in the background, it was not surprising that the CFDC at the time of its establishment was excited at the possibility of promoting Canadian productions with low budget films.[31] Indeed subsequent development has witnessed the importance of this philosophy in influencing the Canadian films being produced. In 1973-74, for examples, 19 films were produced with CFDC assistances. Five of these CFDC financed films were produced with less than $100,000. While none of the films was budgeted above $750,000, the average cost of all the film produced was $374,000.[32]

Also, because of its mandate to promote Canadian culture, the CFDC in the first decade of its operation put more emphasis on Canadian artistic value in its assistance to private producers than on 'international appeal'.

Because of these significant differences between the Canadian and American feature film products, and also because of the long developed Canadian taste for American entertainment films, it is therefore not difficult to understand the part played by product differentiation in hindering the Canadian producers in breaking into the market. However, as stated earlier, feature films are an extremely heterogeneous product. It is not conceivable that

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31. CFDC, Annual Report, 1967-70, pp.4-5.

32. CFDC, Annual Report,1973-74, p.4.

Canadian producers would suffer a permanent disadvantage because of the competition from the American products. Given a change in production orientation it is possible for Canadian producers to make a successful break into the market. The development in the Canadian industry since 1978 has definitely demonstrated this possiblity.

B. Small Domestic Market Size

Like many other industries, the development of a truly Canadian feature film industry is also partly hindered by a relatively small domestic market. The existence of a small domestic market which is deluged with foreign products complicates further the difficulties of Canadian producer both in terms of output, costs and profits.

In the first place, according to film industry experiences elsewhere in countries such as the United States, France and England, it has generally been observed that one feature film could be produced for one million in population per year. Canadian experience so far has also seen production at this rate.[33] The significance of this observation is that it implies a very limited Canadian market that would be available to support a Canadian feature film industry.

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33. Bureau of Management Consulting, Evaluation of the Canadian Film Development Corporation, p.17.(hereafter cited as BMC, Evaluation.)

Of course matters are further complicated by the fragmentary nature of the Canadian film market. The division between the English-language and the French-language sector practically means that about a 6 million audience is available to the French language product and 16 millions for the English language product.[34] The potential market size thus has a very restrictive effect on the annual output of the industry. There is therefore a pressure on the push for an international market to support a full fledged Canadian film production industry. This is especially true for the English language film products.

In addition, the difficulties created by a small domestic market are further compounded by problems of competition from foreign countries, specially those from the United States. These two elements together have a very important influence on the cost and profitability of Canadian films.

The American film product generally has a much higher production budget (average production cost in 1974 was $2.5 million) and at the same time it enjoys an advantageous position in terms of promotion campaigns because of spilled-over effect of advertising. Even though a large budget does not necessarily guarantee the success of a film, experience does show that up to a minimum of a million

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34. BMC, Film Study, p.192

dollars is needed for a major project to ensure certain degree of production success.[35] With the presence of American films, there is tremendous upward pressure on production costs if the Canadian films are to be competitive with the American films.

However, in the feature film business, it is recognized that for a Canadian production to break even it takes a revenue that is about five times as much as the costs. Herein lies a paradox for the Canadian producers.

In order to make the Canadian product more competitive, producers may choose to go for a higher cost production. But the existence of a small domestic market makes the business more risky and profitability more questionable. Or, alternatively, they can choose to minimize the budget in order to maximize the potential profit margin. This latter approach however could mean production of low-budgeted films which might not stand up to the foreign products.

The strategy Canadians have adopted so far in promoting production activities is apparently the second approach. As mentioned earlier, most of the films produced have not exceeded a budget of $750,000. In fact over a period of eight years since the set up of CFDC, 180 films have been

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35. See Position Paper Concerning the Motion Picture Distribution Industry in Canada, presented by the Canadian Motion Picture Distributors Association.

produced at an average cost of about $279,000. As one study pointed out, this approach indeed had caused the uncompetitiveness of Canadian feature films and thus severely has undermined the financial situation of most Canadian producers.[36] It is also in this light that one can understand one of the major reasons why the CFDC has so far been experiencing a great loss in its investments.

In either case, there is a strong indication that in order to make the Canadian film production commercially viable, there is a need to break not only into the Canadian domestic market but also the international one. This also would imply the need of products that have more international appeal rather than just 'Canadian content'. This is an option which is not favored in an important sector of the industry.

C. Creative and Technical Inputs

In the production of a film, its success is dependent on its artistic and technical qualities. Technical and creative talents are therefore essential inputs for a film output. In Canada, it is generally recognized that technicians with the necessary expertise are readily available.[37] The quality of these technicians is further

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36. Survey Centre, Assessment, pp.2-4.

37. Ibid., p.9.

recognized as comparable to international professional standards.

However in the field of feature film production, Canada has been hindered by a lack of certain creative talents. In this regard, there are two main areas of concern. They are the lack of good producers and script writers.

Producers

In Canada, the general lack of good producers is a result of insufficient experience in major film production. Most producers are simply not well trained. As one study puts it,[38] the overall problem is that Canadian producers lack a good sense of business. Often they fail to objectively evaluate the marketability of the film property at the very early stage. Often these producers attempt to produce a film without audience objectives and try to cover other production functions such as directing and writing all by themselves. Thus they are more concerned about artistic successes and fail to recognize the commercial aspect of the production.The over-emphasis on production also makes them neglect the important function of film promotion. While pre-production promotion is common practice in American films, Canadian producers tend to ignore this aspect of production.

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38. Survey Centre, Assessment, p.14.

In all, the existence of non-commercially orientated producers could partly explain the difficulty of Canadian productions in achieving a higher market share. Until the arrival of more business minded producers, profit opportunities for Canadian production remain a serious problem.

Film Scripts

Another difficulty Canadian feature film production has been facing is the lack of well written script and story materials. There are two possible explanations. On the one hand Canadian producers have problems in getting access to relevant story materials such as stage plays or novels. Due to competitive bidding from the American industry, the costs of these story materials have been rising steadily.[39] Because of a lower budget constraint, the Canadian producers generally are not able to compete favorably with American producers for these materials.

On the other hand, there is also a lack of new professional screenplay created by Canadian film writers. Even though there are many experienced film writers in Canada, most of these writers seldom venture into the feature film business on a speculative basis. One of the reasons for this lack of interest is that many of these

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39. Council of Canadian Filmmakers, "Policy Statement on Feature films", Cinema Canada, March 1974, p.8.

writers have already found continuous employment in institutions such as the Canadian Broadcasting Corporation, the National Film Board, and private film companies that are involved in production activities other than theatre business.[40] This contributes partly to the scarcity of writing talents in feature film productions.

D. Financing Difficulties

One of the major barriers to Canadian producers' attempts in feature film production is insufficient finance available for working capital. Before the establishment of the CFDC, there were fewer than three films produced annually. After the setting up of the CFDC, production has jumped to an annual average of twenty films. This fact manifests the high hurdle a lack of financing can create in preventing the development of a Canadian feature film production industry.

The lack of funds for Canadian film production is due to a combination of several factors. They are (1) inaccessibility to financial institutions for film projects. (2) limited investment from private investors and (3) insufficient production funds within the industry.

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40. CFDC, Annual Report, 1974-75, p.4.

Inaccessibility to Financial Institutions

It has been noted that in the United States, because of the unique nature of the film industry, no more than a dozen commercial banks have developed the expertise in film financing.[41] In Canada, since the existence of a feature film industry is only a recent development, most Canadian banks have not been given the opportunity to gain the necessary expertise in film financing. Also because of some unfortunate experiences in film financing, it is found that most Canadian financial institutions shy away from film productions and are reluctant to lend any money for that purpose.[42]

Lack of Private Investment

Another factor that hinders fund availability for film production is the insufficient investment from private investors. Because of a lack of production in the past and because of a small domestic market already flooded with foreign products, risk and uncertainty become a very important consideration for potential film investors.[43] The riskiness of investment is further increased by the fact

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41. Patrick McGilligan, "Bank Shot", Film Culture, September-October, 1976, p.20.

42. See BMC, Film Study, p.168; see also BMC, Evaluation, Chapter 3, p.16.

43. Ibid., volume II, P.127.

that in Canada production is generally separated from distribution activities.

The risk factor in investment in film production, however, could be offset by the tax incentives offered to private investors. This is the accelerated capital cost allowance ranging between 60 to 100% allowed a private investor in film or video production. The ability to shelter part of an investor's income from taxation could have helped to attract private capital into film production. Unfortunately this incentive was not well publicized and most private and institutional investors were not aware of its existence.[44] In addition, it appears that these tax rules have been arbitrarily executed by Revenue Canada, who tended to resist deductions with regard to investment in film production.[45] These factors therefore tended to discourage more investment from private investors and thus helped to create financing difficulties to the film producers. For example, it was reported by the CFDC that a meager sum of $688,000 was contributed by private investors in the fiscal year 1975-76.[46]

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44. Survey Center, Assessment, p.12.

45. BMC, Film Study, p.166.

46. CFDC, Annual Report,1975-76, p.4.

Limited Production Fund Within the Industry

As we have seen in the last chapter, the distribution and exhibition end of the Canadian film industry is occupied by foreign concerns. The thriving final market helps only the operation of these two branches of the industry.

Also, as it was pointed out, the annual percentage of foreign film supplies between 1965 and 1975 was 97%. This created a serious drain of film rental funds from Canada to foreign countries. Together with the fact that most of the distributors are involved in film production in their home country, financing from distributors is generally not available to Canadian producers. For these reasons a very limited share of the revenue from the industry was recycled back to film production in Canada. In 1973, for example, a total of $111.7 million was grossed in Canadian theatres. Some $39.2 million was earned by U.S. distributors.[47] But only $2.3 million was invested in Canadian film production from the industry by laboratories, distributors and exhibitors in the fiscal year 1973-74, according to CFDC.[48]

In sum, the reluctance of commercial banks to fund film projects, the shyness of private investors in investing in Canadian film production and the drainage of film revenue to

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47. See Section I in this chapter.

48. See CFDC, Annual Report 1973-74.

other countries as a result of the distribution and exhibition structures, all have created undue difficulties for Canadian feature film producers in raising the necessary capital. This helps to explain the excess reliance of Canadian producers on funding from the CFDC. To achieve a fuller development of the Canadian film production industry, a solution to financing thus seems to be one of the top priorities.

E. Problem of Distribution

As discussed in the previous sections, the lack of past feature film production activities in Canada could be a result of financing difficulties. However, with the establishment of the CFDC, the financing difficulties were partially offset by the public financial assistance. Unfortunately, with the increase in Canadian production, experience has found a more handicapping barrier to the establishment of a strong production industry. This is the problem of access to the film market, both domestic and international. This is most commonly termed as the problem of distribution. There are several aspects to the distribution difficulties. In a broad sense, the problem could be categorized as (1) separation of Canadian production and distribution activities, (2) foreign domination of the distribution and exhibition branches of the industry, and (3) vertical structure of foreign owned film companies.

Separation of Production and Distribution

As discussed earlier, there is a general lack of expertise among Canadian producers as film promoters. This refers to Canadian producers' inexperience in film distribution realities.

In the film industry, it is recognized that distribution companies play a role more than just a plain middle-men or wholesalers.[49] Because of a concern for a steady flow of good film supplies, distributors are also involved in film financing. They are therefore more concerned with film products in which they have financial interests than with products from outside producers. Independent producers have tried to use the distributors as wholesalers. However experience in the United States showed that it never worked that way.[50]

Canadian producers , oblivious to this important fact of film distribution, tend to initiate production without prior commitment from a viable distributor. Thus by the time the producer completes his film, he finds himself in a relatively weak bargaining position in negotiating a distribution agreement. This also led to unhappy situations

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49. BMC, Film Study, pp.251-252.

50. David Gordon, "Why the Movie Majors are Major", Sight and Sound, Autumn 1973, p.194-196.

whereby producers found that their products have not received proper handling.

Perhaps it is also because of inexperience in the film industry, that separation of production and distribution was created at the very outset when public assistance to the private sector was established. As we have seen the CFDC was given a mandate to promote the industry. But apparently, the vision of the government at the time of the creation of the CFDC was that with public funds available, a viable production industry might be achieved. Operation of the CFDC thus has been based on this expectation. Even though it was aware of the importance of distribution the CFDC, limited by its resources, was not in a position to promote simultaneously production and distribution activities. The failure of CFDC to promote a better distribution system for Canadian products thus has become one of the strong criticisms the industry has of the CFDC.[51] In the absence of a well developed Canadian distribution system, producers have been forced to make use of whatever system is available. As experience shows this system has not been working out for the Canadian producers. The poor financial returns might well be a direct result of the inadequacy in the existing distribution system.

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51. BMC, Evaluation, p.31.

Foreign Control of Distribution and Exhibition

One of the difficulties Canadian producers have with the set-up of the existing distribution system is the fact that most of the distribution and exhibition channels are controlled by foreign concerns. As we have seen in the last chapter, because of its early development, American film companies have long since developed a well established distribution and exhibition system, which well covered Canada too. They thus control the largest two theatre circuits and the largest seven distribution companies in this country.

On the surface these American systems operate with a very different philosophy from that of their Canadian counterpart. American film industry, being the only film industry in the world that is without public assistance, operates on a commercial basis. It is found that most of these distributors have been very reluctant to handle Canadian films.[52] Somehow these distributors are convinced that Canadian films have a limited marketability. Citing this belief, the major distributors tend to turn away from promoting Canadian films. Even when occassionally they are involved with a Canadian film, they limit their investment and are concerned with minimizing their "losses".

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52. Survey Center, Assessment, p.20.

The net result of this control by a few foreign concerns over the system is that by the time when more Canadian feature films were produced, producers found that they could not get access to the market through the existing distribution system. They were thus forced to go to relatively smaller and unknown distributors. This is especially true when the U.S. and international market is involved. But even if they get access to such distributors Canadian producers would still suffer from unfavorable deals.[53]

However, from the perspective of some Canadian filmmakers, the difficulties of getting access to the distribution system is not just a question of "marketability" of Canadian films.[54] Rather they see the difficulties as more of a question of abuse of market control by the foreign companies through practices such as exclusive agreements and refusal to deal with independents. These views have been raised in legal complaints by Canadians against the major foreign concerns. At the same

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53. Ibid.

54. In 1976, for example, nine Canadian individuals filed with the Combines Investigation Branch of the Department of Consumer and Corporate Affairs an application for inquiry into market practices of foreign controlled film distribution and exhibition concerns in Canada. Another complaint was made by one independent theatre operator in Nova Scotia against the major American system. See statement by the Council of Canadian Filmmakers in Cinema Canada, March 1976, p.10; and Kirwin Cox, "Rocca's Big Fight", Cinema Canada, February 1976, p.22.

time one federal study has concluded that the reluctance of foreign distributors to deal in Canadian films could well be explained by the fact that they are more concerned with their commitment on other films.[55]

Vertical Structure of Foreign Companies

The criticism of other commitments raised an important question of the structure of the foreign film companies. More precisely, it is the question of vertical integration of the distribution and exhibition concerns in Canada. In the previous chapter we have laid out the close relationship between the two major exhibition circuits, Famous Players and Odeon, and the seven major American distribution companies. The most outstanding feature mentioned was the exclusive arrangement whereby all the film products from the parent companies of the distributors were played in the two major theatre circuits. Moreover it is well understood that most American film distributors nowadays are involved extensively in film production which, incidentally, does include independent American production. Based on these interlocking arrangements, the foreign exhibitors and distributors are therefore in fact vertically integrated in structure, extending from the production stage to the final market. This vertical integration of production, distribution and exhibition activities has had significant

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55. BMC, Evaluation, p.20.

effects in an oligopolistic market such as the Canadian film industry. At the very least, there exist the possibilities of retarding competition and raising costs for Canadian entrants.

i. Retardation of Competition

According to the federal report cited earlier, many of the Canadian filmmakers interviewed had made contact with the American owned distribution companies. However only one English language producer had ever obtained distribution from an American owned company at the time when the study was done.[56] This finding thus makes one question the real interests of the foreign companies vis-a-vis the development of a Canadian film production industry.

Throughout the history in the development of the American film industry, vertical integration had been an important method for the major company to dominate and control the final market. Through the integration of the three functions, the major companies were in a postion to foreclose the market and prevent independent producers to obtain an adequate distribution of their products. However, the vertical structure of the American industry was dramatically altered when in 1948 the U.S. Justice Department through a decade's antitrust effort gained a

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56. Ibid.

court decree, commonly known as the Paramount decree, for divorcement of theatre holding and distribution from production activities.[57] One of the important developments in the United States since this court case was the emergence of independent productions and co-operation between the independent producers and the major distribution/production companies. But, unfortunately from a Canadian producers' perspective, this decree only covers the operation of the film industry within the United States. The decree was not extended to foreign markets in which the major companies had interests. Indeed after the Paramount case, many major companies still kept their theatre holding in the foreign markets. Paramount's holding of the Famous Players in Canada is a good example.

Today many traits of a tight market control through chains of fully integrated companies is still evident in the Canadian film market. It is therefore not surprising that the problem of distribution bas become one of the most important barriers to a full scale development of the film production industry.

ii. Raising the Entry Barriers

Since the distribution channels are controlled by foreign companies, one way for Canadian producers to break

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57. Tino Balio, op. cit.; see also Michael Conant, op. cit.

into the market is by setting up their own distribution channels. In other words, Canadian producers, in order to be more competitive, have to integrate their production and distribution activities. But the necessity in integrating two functions of the industry only helps to increase the barriers to potential entry into the Canadian feature film production.

As mentioned before, film distribution nowadays is actually a large scale industry and there seem to be a certain degree of scale economies.[58] If Canadian producers choose to set up their own distribution system, they would need a much larger amount of capital to set up an optimal-scale system. This in turn would increase the difficulties in financing. Thus the vertical structure of the foreign companies helps to reinforce some other entry barrier factors such as the Canadian market size and financing problems.

IV. CONCLUSION

Most of the film products consumed in Canadian theatres are foreign imports, and most major exhibition and distribution companies operating in Canada are foreign owned.

The production sector consists of a mixture of public

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58. David Gordon, op.cit.

and private endeavor, oriented toward the non-theatre market. From a historical perspective, before the arrival of public support in 1968, there was practically no feature film production industry.

In view of these facts, it might be true to say that even though there is a fully developed theatrical film exhibition and distribution sector in Canada, Canada still does not have its own feature film industry. To remedy this deficiency, entry by Canadians into feature film production is needed to foster Canadian aspirations by promoting films that have more Canadian creative and technical contents.

However, to do that Canadian producers need to overcome several important entry difficulties which include problems in obtaining financing, lack of skillful producers, a small domestic market deluged with foreign products, and little access to a viable distribution system.

Chapter 5

Development of the Canadian Feature Film Industry

As was mentioned in the last chapter, Canada needs to develop a feature film production sector in order to create a film industry that would promote national-cultural values and add to the nation's economy. In this chapter we will examine the move toward that direction since the late 1960s.

The prime motivation of this move came mainly from the public sector. It was initiated by a direct approach to production activities with the creation of the Canadian Film Development Corporation (CFDC). Subsequently, an indirect approach to help the industry was introduced with the provision of a tax incentive for film investments in the private sector.

The achievements of these policies in promoting and solving the difficulties in production activities will be described and evaluated. A section will then be devoted to examine the outstanding problems that are still hindering a full development of the industry which, in this case, relate mostly to the problems of market access. A brief discussion will also be directed to future options in dealing with the film distribution problem.

I. DIRECT APPROACH TO FOSTERING THE INDUSTRY: ESTABLISHMENT OF THE CFDC

The lack of Canadian-produced feature films has long been a concern for people interested in the industry. Petitions, especially by filmmakers themselves, were made for government assistance. But most of these efforts were not well-organized. However, in early 1964, one of the most carefully planned petitions was made by an association of filmmakers in Quebec, the L'Association Professionelle de Cineastes, to the Secretary of State.[1] This petition was backed up by subsequent politicking. In the petition this film association demanded and raised several possibilities of government support for the industry. Some of the recommendations were (i) the establishment of a government body to regulate Canadian film-making activities, (ii) government support of feature production through loans to film producers, (iii) direct cash premiums on box office receipts and (iv) the design of economically coherent film policies between the federal and provincial governments.[2]

At the same time there were studies being done on the industry by both the public and private sectors. Apparently as a result of these lobbying activities from the private

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1. Financial Post, March 7, 1964, p.17.

2. Ibid.

sector, the Canadian government decided by late 1964 to support the feature film industry. In August, 1964, federal cabinet decisions were made to approve a policy of establishing a loan fund to foster and promote the development of a Canadian feature film industry.

Then in October, 1965, a public announcement was made by the Department of the Secretary of State about the government's intended policy of setting up a Crown Corporation to promote the industry. This corporation was to be vested with the responsibility for administering a $10 million revolving fund to promote production activities. This fund would make the new corporation, the Canadian Film Development Corporation (CFDC), a financing institution for feature film producers. This was based on the model of the Industrial Development Bank and the British National Film Finance Corporation. The latter's primary function is to help feature film production in the United Kingdom.

The government's policy was introduced in the House of Common in June 1966. The bill thus introduced was C-204 intituled as "An Act to provide for the establishment of a Canadian Film Development Corporation". After some discussion in both the House of the Common and the Senate, the bill was finally passed by the Senate without amendment on March 2, 1967. The Act was duly enacted into the statutes of the country. In April 1968, after appointments of the chairman and five other members of the corporation had been made, the CFDC finally came into being and met for the first time to start their business undertakings.

A. Motives of Public Assistance to the Industry

There are several factors for the government's decision to help film production activities and to support the establishment of a feature film industry. Broadly speaking these factors can be categorized into economic and cultural considerations.

Economic Aspects

Economically, the weak Canadian film production industry together with a final market demand for foreign film products has strong impacts on this sector of the Canadian economy. In terms of production factor, the lack of production activities means the idling of much Canadian creative and technical talent . By taking measures to help the film industry, at least the government helps to increase chances of employment and the possible enhancement of skills and talents.

On the other hand, the high demand for foreign film output had meant a large outflow of Canadian funds into foreign countries from this sector of the economy. If Canadians could establish a production industry to turn out Canadian feature pictures, it is possible for the country to reduce the flow of funds out of the country. Furthermore, the establishment of a viable Canadian feature industry could also understandably increase the export base of the country. This could therefore help the country generate more revenue abroad from the film products. If these things happened it could conceivably enhance the balance of payments situation of the country. Thus from an economic point of view this government assistance should be worthwhile.

Cultural Objectives

However, the government's venture into the promotion of the feature film industry has also a cultural dimension. As often cited, there may be an externality problem involved in a community of people viewing the same films. In the process of film appreciation , values, ideas, and other information are often conveyed to the audiences. If this is true, then, as some critics have argued, the high demand for foreign film would mean constant bombardment of foreign ideas and values upon Canadians. This would be a great disadvantage to the Canadian identity because not many Canadian films have been able to gain access to the Canadian audience. Thus the promotion of a Canadian feature film industry could help to reduce the impact of foreign cultures. Furthermore, the success of this industry could certainly help to foster the Canadian values among the people and contribute greatly to the unity of the country. The establishment of the CFDC and the subsequent government involvement in the feature film industry can be viewed as an orientation toward the promotion of Canadian culture and the alleviation of foreign cultural impacts, especially those from the south.

B. Operations of the CFDC

Since its establishment in 1968, in order to carry out its mandate, the CFDC has been extensively involved in most Canadian feature production activities. This has included a range of activities including investing in production projects started by private producers, helping pre-production preparation, making co-production agreements with foreign countries, setting up special investment programs to encourage young film-makers and dealing with promotional and distribution activities. Also since the CFDC was given the power mainly to promote features that have significant Canadian 'creative, artistic and technical' content, it has also to decide on how this aspect could be judged 'Canadian'.

Definition of Canadian Content in Feature Film Production

The basic elements the CFDC so far has chosen to use in determining the 'Canadian' content of a film is the employment factors in the creative, artistic and technical aspects of the films. On the artistic and technical side the CFDC seems to have had no problems in their decisions;

but it has had difficulties as far as creative contributions are concerned. For its operations, the Corporation now has adopted a principle that two of the three principal creative contributors to a picture, i.e. writers, directors and producers must be Canadian. Of course, exceptions are sometimes allowed. As to other creative contributors, such as the director of photography, the editor, music composers and set designers, the Corporation does allow one or two of these factors to be non-Canadian.[3] Conceivably, the tolerance of one or two non-Canadian elements here has the objective of enhancing the possibilities of international distribution.[4]

Investment policies

To promote the Canadian feature film industry, CFDC is given the power to invest in Canadian feature film productions in return for a share of the commercial profits. Also, the Corporation, under statute, is allowed to make loans to producers and to charge an interest. However, in its operation so far, emphasis has been put on investment rather than loans.[5]

One of the fundamental ideas of the government in

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3. CFDC, Annual Report, 1969-70, p.9.

4. Drabinsky, op. cit., p.126.

5. CFDC, Annual Report, 1969-70, p.13.

proposing the establishment of the CFDC was that the Corporation should be operated very much on business principles. This orientation is needed in order to preserve the very limited amount of funds.[6] As a result the CFDC as an investor is aware of the need for commercial viability of the projects in which it invests. Thus in investing in a certain project, one of the most important requirements the Corporation imposes on the potential producers who want the CFDC's financial assistance is that the producer should have a solid experience with the operation of the film industry. Except for some specially low budget projects, the CFDC thus generally avoids investing in projects that have inherently higher risks such as those proposed by beginners.[7]

To qualify for the CFDC's assistance, the Corporation requires applicants to secure a valid distribution contract with any distributor.[8] An Additional requirement on this distributional aspect is that the distributor will either (i) invest in the production cost of the film or (ii) guarantee or advance payment when the picture is delivered, or (iii) guarantee an amount of expenses for prints and

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6. The Senate of Canada, Complete Proceedings on Bill C-204, Intituled : 'An Act to Provide for the Establishment of a Canadian Film Development Corporation',(Ottawa, 1967), No.36, p.657. (Hereafter cited as Canada Senate, Proceedings.

7. CFDC, Annual Report, 1970-71, P.5.

8. Ibid., 1969-70 p.8.

advertising which will be mutually agreeable to all parties involved in the project. But even when the Corporation has approved assistance to a certain project it would limit its investment to only half of the production budget, with an unofficial ceiling of $300,000 in big projects.[9]

Special Investment Programs

The investment policies as described above applied mainly to big budget production and are geared to help experienced film producers. In order to train a new generation of young Canadian film-makers so that a stronger base for future development would be available, the CFDC initiated a special investment program in 1972-73.

Under this program a special fund of $600,000 was established for the production of low budget films. The low budget films are designed to have a maximum budget of $155,000 and the Corporation would participate with as much as 60% of the budget. This program is designed to help the young filmmakers to make their first feature films.For this purpose no distribution guarantee is required before the production and the private investors are allowed to recover their costs before the CFDC does.[10]

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9. CFDC, Annual Report, 1969-70, pp.8-12.

10. Drabinsky, op. cit., pp.127-128.

Pre-Production Assistance

In promoting production activities, the CFDC also undertakes pre-production assistance to potential projects. This involves giving financial support to producers in acquiring film properties, or engaging directors or writers to prepare the scripts. The Corporation will participate to a maximum of half the budget for the pre-production requirement. For such assistance, the Corporation usually requires a thirty-page synopsis of the story and the stated financial budget for such purposes.[11]

But the Corporation's experience with the pre-production activities has been very disappointing. By 1970-71, of 45 projects, only seven resulted in the completion of a film. Twenty-two projects had to be written off completely.[12] As a result, the Corporation over the years has been cutting back significantly on these ventures.

Co-Production Agreements with Foreign Countries

In encouraging film production, the government through the Department of State has long been interested in making co-production agreements with some foreign countries. These agreements are beneficial since, as the government puts it , they will provide Canada's film-makers with increased

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11. Ibid., p.127.

12. CFDC, Annual Report, 1970-71, p.5.

financial returns, a much larger audience, and the opportunity to work with producers abroad who are more experienced in feature films.[13]

Through the efforts made by the Department of the Secretary of State and the Department of External Affairs, Canada so far has entered co-production with France, the United Kingdom, and Italy. Since March 1976, the CFDC has been processing co-production applications on behalf of the Secretary of State.

Promotion and Distribution Activities

Since there really is no point in making movies if they are not exhibited, the CFDC thus also places much emphasis on the promotion and distribution of films produced with the Corporation's assistance. One of the main CFDC activities is its investment in promotional campaigns of Canadian films that are distributed by Canadian distributing companies. For such purposes, the Corporation may put up half of the cost of subtitling the films, i.e. making French-language films into English and vice versa. The CFDC may also put up half of the promotional expenses for these Canadian films.[14] The main condition for the CFDC's participation is that the film should have secured a guarantee of screen-time

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13. Ibid., 1968-69, p.12.

14. CFDC, Annual Report, 1969-70, p.10.

in the Odeon or Famous Players theatre chains in the metropolitan areas of Montreal, Toronto and Vancouver.

For international distribution, the Corporation since its very early days of operation has established in New York a consultant on distribution of Canadian films.[15] At the same time to further the international promotion and distribution of Canadian films the CFDC, together with other government departments and agencies such as the Department of Trade and Commerce, the Canadian Government Exhibition Commission, and the National Film Board, has been actively participating in film festivals which have world-wide reputation and which function as international film markets. The most notable one is the Cannes Film Festival in southern France which the CFDC has been taking part in since 1970. As the Corporation reported, these film festivals have been helpful for the promotion of Canadian films.

Domestically, the distribution of Canadian films has been very disappointing; there is a perennial problem of limited distribution. Concerned with this unhealthy situation, the Department of State through the CFDC held conferences with the two largest theatre circuits in the country in 1973. These meetings resulted in an informal agreement between these two theatre companies and the

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15. Ibid., 1973-74, p.7.

government on the voluntary quota system. By this system, the two theatre chains agreed to guarantee a showing of the Canadian English feature films, originally produced or dubbed, for a period of at least two weeks in each of the country's three largest cities, Montreal, Toronto and Vancouver. Further distribution would be assured in other cities for those films which do well in the three biggest cities.[16]

II. EVALUATION OF THE CFDC : THE INITIAL STAGES

As has been pointed out earlier, the Canadian Film Development Corporation was created to help promote the film industry. Thus to evaluate the achievement of Canadian efforts in building its own feature film industry would almost be equivalent to evaluating the success of the CFDC, at least in the early stage of its development. This section will scrutinize the achievements of the CFDC to see what its successes and failings have been.

It should be pointed out that an evaluation of the CFDC can be based on two main considerations : economic factors and cultural aspects. This is essentially a result of the dual responsibility bestowed on the CFDC by its creators. The CFDC was given the power to invest or make loans to Canadian film productions for a share in the financial

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16. Ibid.

returns or interest. At the same time, the CFDC was supposed to promote film projects that have "Canadian" creative, artistic and technical contents. In other words, both commercial viability and cultural achievement is expected of the CFDC.[17]

A. Cultural Aspects

Since our main attention here is directed towards the working of economic factors in the establishment of a viable Canadian feature film production industry, cultural considerations would be of no consequence to us had it not been for their importance in the public policies involved. As we have seen, cultural considerations have been an important factor inducing public involvement in this industry. Thus judgements on the cultural aspect of film products could affect the performance evaluation of the industry and thus the shaping of policies. It may therefore be fitting for us to leave the evaluation on the tie between cultural results of film products and public policies to the consideration of public policy alternatives. In passing, it may suffice for us to point out that because of cultural values upheld among different sectors of the Canadian

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17. For a good understanding of the government's intent in setting up the CFDC, see the statement made by the then Secretary of State, Judy LaMarsh, before the Standing Committee on Banking and Commerce, the Senate of Canada, for the proceedings on Bill C-204, during the first session, Twenty-seventh Parliament, 1966-1967, Proceedings, Number 36.

industry, there is no consensus on the degree of success of the effort in promoting a Canadian feature film industry. While some Canadian productions have achieved remarkable box office success, both domestically and internationally, they are still not considered by some critics of the industry as "Canadian". The net effect on the evaluation of film output are acrimonious debates on public policies.

A. Economic Considerations

While cultural aspects are too intangible for precise measurement, economic factors such as film output, production cost and financial returns can be subjected to statistical scrutiny. Roughly, they can be used to measure the general achievement of the public effort in promoting feature film production.

Investment and Output

To promote the growth of the Canadian feature film industry, the main strategy that was adopted at the very beginning was an emphasis on production activities. When Bill C-204 was considered before the Standing Committee on Banking and Commerce in the Senate in 1967, the then Secretary of State, Judy LaMarsh, stated that an initial $10 million would be appropriated for the CFDC.[18] However, instead of using this money directly to produce film by the

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18. See Canada Senate, Proceedings, pp.661-663.

CFDC itself, the $10 millions was expected to be used as seed money to attract another $20 to $30 million investment from the private sector for film production.

Since the establishment of the CFDC, the public agency's main orientation has been in helping producers in the private sector to get the production projects started. This includes assistance such as CFDC's investment in pre-production funds. The CFDC also helps by investing in certain portion of the production budget.

Subsequent to the establishment of the CFDC, the production of Canadian feature films witnessed a steady growth. For example, in 1970, three years after the establishment of the CFDC, Canadian private producers were able to turn out some 15 films. This was a 500% increase from the three films that were made in 1967. By 1975, annual output had risen to 34.[19] Indeed between 1968 and 1975 an average annual output of twenty films was achieved. Compared to the annual output of about three films prior to 1967, the increase in film production is remarkable.

Investment in film production also has skyrocketed. By fiscal year 1974-75, the CFDC reported that a cumulative $44.3 million outlay had been made on private production, which included $17.1 million from CFDC. Thus over a period

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19. See Table 4-18 in Chapter 4.

of seven years, the feature film industry was able to attract an average annual investment of about $6.3 millions.[20] Again these statistics proved to be remarkable since in the private sector there was less than $500,000 investment on feature film productions as late as in the year 1967.

There are several factors contributing to the increases in film production. However, one dominant factor is the public assistance the private sector has been receiving. This can be demonstrated by the figures listed in Table 5-1, which shows the overall assistance CFDC has given to the private producers.

Table 5-1 shows that in the eight years since its creation, the CFDC has invested $20.8 million in film projects which attracted another $29.4 millions from the private sector. In all, 180 films were produced with a total production value of about $50.2 millions. However, according to Statistics Canada, one can estimate that roughly 198 films were produced in Canada as a whole over the same period. These 198 films included production from both the private and public sectors. This means that the 180 films produced with CFDC's assistance accounted for almost 91% of total Canadian production in this period.

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20. See CFDC, Annual Report, 1974-75, p.4.

Table 5-1

Cumulative CFDC Assistance in Feature Film Production Since 1968-69 Fiscal Year

Fiscal Year As of	No. of Films Produced With CFDC Support	Total Budget of Films ($ Million)	CFDC's Share of Budget ($ Million)
1970-71	44	12.0	4.0
71-72	64	17.7	6.7
72-73	110	28.0	10.5
73-74	136	35.0	13.5
74-75	162	44.3	17.1
75-76	180	50.2	20.8

Source : Compiled from CFDC Annual Reports.

All these figures point to the primary role public support has played in bringing forth an infant industry. Indeed, according to one federal study, it was doubtful whether some of these films could ever have been made without public assistance.[21] It is also doubtful whether a viable film production industry can exist without the CFDC. The same feeling has been expressed by people in the private sector.

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21. BMC, Evaluation.

Employment Opportunity

Another important result of public involvement was increased production activities. In 1975-76, for example, production activities of 18 feature films provided some 75 assignments for Canadian creative talents such as writers, directors and producers. Another 1070 roles were created for acting performers while 308 technicians were also employed. Laboratories and equipment rental companies at the same time received $800,000 and $300,000 worth of business respectively.[22]

Thus, in eight years, production generated by public assistance has brought to the industry a grand total job opportunities as follows[23]: 783 for Canadian directors and producers; 9681 roles for actors and employment for 2766 technicians; laboratories and equipment rental companies earned $6.1 millions and $3 millions respectively. The main benefit of these increased work opportunities in Canada was that it helped to reduce the pressure on Canadian talent to move to the United States to seek employment there. Prior to the establishment of public support most Canadian talent had to try their luck in Hollywood if they were to succeed in the trade. Thus public support in the feature film

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22. CFDC, Annual Report, 1975-76, p.4.

23. Compiled from CFDC, Annual Reports, 1974-75 and 1975-76.

production had been warmly welcomed by most interested groups in the Canadian film industry.

Financial Returns

As we have seen, in the decade immediately following the creation of the CFDC, there has been a steady increase in Canadian feature film production. An infrastructure of the feature film industry, which includes Canadian talent, laboratories and equipment rental enterprise has also been developed. Considering the fact that there was close to nothing in feature film production prior to 1968, most observers agree that at least an infant production industry has finally been established. However, this result has been achieved only at a relatively high cost to Canadian taxpayers.

It should be pointed out that in setting up the public agency to foster the feature film industry, it was the government's expectation that public assistance will be rendered on a hard-headed business principle so that the $10 million revolving fund could be judiciously used to carry on needed activities.[24] However, experience in the first decade of this public support to the industry has shown very disappointing financial results.

Tables 5-2 and 5-3 show some financial aspects of

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24. See Canada Senate, Proceedings.

Table 5-2

CFDC Investment and Returns

Year	Capital Advances	Revenues	Returns *
	$	$	%
1968-69	366,639	-	-
69-70	1,541,228	17,817	(99.0)
70-71	2,393,276	399,681	(83.2)
71-72	2,506,242	300,178	(88.0)
72-73	3,657,105	339,745	(90.7)
73-74	3,115,997	786,028	(74.7)
74-75	3,564,169	864,000	(75.7)
75-76	3,832,976	833,998	(78.2)
76-77	3,825,885	847,247	(77.9)
Total	24,703,507	4,388,694	(82.2)

Notes:
* Figures in brackets signify losses on investment

Source :
(i) BMC, Evaluation, Vol. II, Table 11.
(ii) CFDC, Annual Reports, 1974-75; 1975-76; 1976-77.

Table 5-3

Annual and Cumulative Writeoff to Investment Ratio

CFDC, 1968-69 to 1973-74

Year	Writeoff $	Investment $	% writeoff
(A). Annual			
1968-69	-	366,639	-
69-70	124,455	1,541,228	8.0
70-71	672,377	2,393,276	28.0
71-72	1,426,599	2,506,242	56.9
72-73	2,078,974	3,657,105	56.8
73-74	2,997,099	3,115,997	96.2
(B). Cumulative			
1968-69	-	366,639	-
69-70	124,455	1,907,867	6.5
70-71	796,832	4,301,143	18.5
71-72	2,223,431	6,807,385	32.6
72-73	4,302,405	10,464,490	41.1
73-74	7,299,504	13,580,487	53.7

Source:
(i) BMC, Evaluation, Vol I.
(ii) Ibid., Vol. II, Table 11.

CFDC's ventures. During the first nine years of its operation the CFDC, in maintaining a production program, has been making capital advances to different projects such as script-assistance, language revisions and post-production activities. The capital advances have been in the form of either direct investments or loans to film projects. As Table 4-2 shows, the annual amount of these advances started from a low of $366,639 in the first year of its operation. In the eight years that followed this amount rose steadily, reaching a high of $3,825,885 in 1976-77. In all, the cumulative total outlay of production funds reached $24,703,507 in nine years.

During the same period, the CFDC received repayment on these advances for principal repayment, loan interest and even some profit from investment. However, the overall returns were dismally low. Even in the year 1973-74, during which the CFDC received the most revenue in the period, it witnessed a financial loss of 74.7% on investment. Comparing the total returns of $4,388,694 to the capital advances of $24,703,507, the CFDC actually has experienced a total financial loss of 82.2% on investment in a period of nine years.

Apparently, during all these years of operation, the CFDC was fully aware of the financial weakness of some of the projects . To recognize the little chance it would have in recouping the investments, the CFDC simply had been writing off part of the advances. Table 5-3 gives some statistics on the write-off aspects on CFDC's investments for the first six years of its operation. A cumulative figure of 53.7% write-off on investments certainly indicates the high risk and cost of public support to the feature film production industry.

In view of these financial aspects of the public assistance, it is therefore not surprising to find that in its fourth fiscal year, the CFDC had actually reached the limit of the $10 million fund committed by the CFDC Act. Only through further negotiations with the Treasury Board had the CFDC in December 1971 been able to secure a $10 million supplemental appropriation to continue its function.[25] Unfortunately this extra $10 million was again reported exhausted by August 1975. Another $5 million funding to the Corporation was approved by the Treasury Board after prolonged deliberation. By 1979 this additional $5 million was again being exhausted.[26]

In summary, within a decade of direct public assistance, an infant Canadian feature film production industry was developed. Over two hundred feature films had been produced and opportunities were open for employment and

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25. CFDC, Annual Report, 1971-72.

26. CFDC, Annual Report, 1978-79. See notes to Financial Statement, p.15.

development of Canadian talent and technicians. However, with market access difficulties unresolved, which will be discussed later, the success in building an embryonic production industry had proved to be very costly to Canadian taxpayers.

III. INDIRECT ASSISTANCE: TAX INCENTIVES AND SUBSEQUENT DEVELOPMENT

As stated in the last section, half way through the first decade of government assistance to feature film production, it had become apparent there were serious barriers to a healthy development of a full scale production industry. Financing was certainly one of the important hurdles. The situation had become such that over 90% of private productions relied on government financial support before their project could get off the ground. At the same time private investment was scarce.

Dissatisfied with the financing system in the industry, many filmmaking organizations began to voice their concern and petition the government to give more incentives to private investments.[27] Arguing that film production is a risky venture which should receive the same treatment as the oil exploration industry, groups such as the Council of

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27. See for examples the petitions in 1974 from the Council of Canadian Filmmakers to the CFDC on additional assistances to the industry, "Council of Canadian Filmmakers", Cinema Canada, June-July, 1974, p.64.

Canadian Film Makers called for a more generous tax incentive to private investors in film production.

The government on its part also recognized the high financial risk in feature film investments and agreed that incentives for legitimate investment in film is justified.[28] Also, possibly out of a desire to channel more private investment into the industry and cut down the heavy reliance on the public support, the government by 1975 decided to give a more generous tax incentives to private investors in feature film productions. The incentive was in a capital cost allowance treatment of taxation.

A. Tax Incentives : 100% Capital Cost Allowance

On August 5, 1975, the then Secretary of State, J. Hugh Faulkner announced a new income tax regulation which would allow investors in a Canadian film production to write off 100% of their investment as a capital cost allowance in one year.[29] This accelerated depreciation allowance thus provided a good tax shelter to people in a high income tax bracket. In addition, the 100% write off incentive, which formerly had been 60%[30], was made doubly attractive in the

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28. See CFDC reply to the CCFM petition, Cinema Canada, June-July 1974, p.66.

29. "Film News", Cinema Canada, July-August 1975, p.8.

30. Kaspars Dzeguze, "Listen, Baby: We can get you in the Movies", Canadian Business, November 1977, p.47.

May 1976 federal budget. This was because of the government's decision in withdrawing incentives from traditional shelters such as airplanes, boxcars and livestock.

To qualify for this new tax shelter, an investor had to invest in either (a) a certified Canadian production or (b) a certified co-production with a treaty country.

Under the definition of "certified Canadian films", as defined in subsection 1104(2)(h) of the income tax regulations, an investor was eligible for the capital cost allowance if the film in which he invests (i) is at least 75 minutes long, (ii) is produced by a Canadian citizen or landed immigrant,(iii) has a minimum of 6 points out of a possible total of 10 points allocated for Canadians on the basis of two each for director and screen-writer, one each for lead role, art director, director of photography, music composer and editor, (iv) pays Canadians 75% of the remuneration for all other personnel and (v) has at least 75% of the technical services performed in Canada.[31]

For a 'certified co-production', the films to be produced have to be under an existing film treaty between Canada and a foreign country. As long as the Canadian

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31. See "Film News", Cinema Canada, June-July 1975, p.8. See also W.G. Ivens, "Bankers Star in Supporting Roles", Canadian Bankers and ICB Review, April 1980, p.5.

co-producer makes sure that no less than 20% to 30% of the budget was spent in Canada and on Canadians, the film would be eligible for the 100% capital cost allowance, depending on the treaty involved.[32]

By providing this new incentive, the government hoped to stimulate private financial support to the industry. As it turned out, the development in the feature film industry after the introduction of this tax legislation was indeed extraordinary. Both the government and film people were surprised at the overwhelming response of private investors to the tax shelter. The tax provision in turn brought forth two very important developments. They were (a) a revolution in Canadian film financing and (b) the emergence of a new breed of producers.

B. New Financing System

With the introduction of the new tax regulation, investment in feature film production had become very attractive for Canadian private investors and the investing institutions. Whereas there was very limited investment from outside of the film industry, investment from the private sector since 1977 has accounted for over several hundred million dollars. Whereas there was no financial

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32. For examples, for a French coproduction a 20% will be required whereas for Britain and Italy, a 30% is required. See Kaspars Dzeguze, op. cit., p.47.

institution involvement in the industry before, investment houses and commercial banks were drawn into the industry with a newly developed system of financing.

Because of a large number of private investors seeking benefits from the tax shelter, and also because of the ruling by the securities commissions in regard to film investment, the history in Canadian film financing system was dramatically changed almost overnight. Public financing of film production was introduced for the first time in the entire continent of America. At the same time, new innovative approaches were developed by film producers to take advantage of the situation. These were the development of 'cross collateralization' and corporate approaches to film financing.

In this section highlights are given to the new methods of financing in the Canadian film industry, including such features as public offering and private placement as well as interim financing by financial institutions. Examples are also given to indicate the Canadian producer's innovative approaches to the new financial system.

Public Offering and Private Placement

A new system of public financing (or equity financing) was gradually brought into being after the 100% capital cost allowance was introduced. This system was established out of a necessity because of the policies of securities commissions. Once the tax incentive was in place, the securities commissions required film producers to file a prospectus when they sought more than fifty investors.[33]

In a prospectus, film producers by law are required to disclose a set of facts to the prospective investors. This information includes a detailed breakdown of the budget, a description of the film and the proposed principal artists and the way it would be financed. The prospectus is thus a device for the private investors to evaluate the proposed film project. Thus private investors are offered a chance of buying into the ownership of a film.[34]

With the existence of a large number of private investors who were ready to risk their money and partly because of high commission opportunities, brokerage firms and investment dealers were attracted into the new financing system. These factors all contributed to the rise of the

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33. Susan Cole, "Bay Street Gets into Movies",<u>Canadian Business</u>, August 1979, p.59.

34. Generally a film is sold in 'units', with each unit representing a portion of ownership of the final film product. By way of example, a film budgeted at $5 million could be sold to 500 investors with each unit priced at $10,000.In fact the first Canadian movie that was financed through the prospectus route was called 'Agency', produced by the Movie Corp. in 1978. The film offered $4.05 million worth of securities first in Quebec and then to provinces in the rest of Canada. In the same year seven prospectuses were filed with the Ontario Securities Commission.

new equity financing system in the industry on an individual film basis.[35]

A benefit of the new public financing system is better planning in film production activities. Because of the prospectus requirement, producers seeking public financing have to disclose a detailed plan for the proposed project, which would include information such as the budget, the story outline and the prospective talent. Also, since public money is involved, provincial securities commissions play an active role in scrutinizing each proposed project. In this process, film producers are forced to have better laid-out plans. For this reason, public financing, in addition to generating more capital for private productions, also helps to improve the internal efficiency (X-efficiency) of the film concerns which seek equity financing.

At the same time, producers have another option in raising their capital. This is the possibility of seeking out those big investors who are looking into film both as an investment and as a tax shelter. If a producer has access to a small group of investors who are willing and in a position to contribute to a budget of one or two million

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35. Examples of investment house involvement : $4 million was handled by Levesque Beaubvien Inc. for the film 'Agency'; $3.6 million was sold by Shearson-Haydon Stone (Canada) Inc. for the film 'Running'; $6.6 million was issued by Merit Investment Corp. for 'Changeling';$3.8 million offered by Greenshields Inc. for 'A Man Called Intrepid'. See Susan Cole, op. cit., p.60.

dollars, and as long as the number of investors involved is under the limit placed by provincial securities commissions, there is no need for the producer to file any public disclosure. The advantage of private financing is that legal and interim finance costs are generally lowered.[36] Good examples of private financing were the four films produced by the DAL Productions, a Quebec Company : Meatball($2 million), Happy Birthday to Me ($3.5 million), My Bloody Valentine($2.5 million) and Heartaches ($4.9 million).

Interim Financing

With the development of public financing came an ancillary financing program called 'Interim Financing'. Through this program Canadian banking institutions which had previously been cautious in being involved in the film financing business because of risk factors were now attracted to film production financing.

The development of 'interim financing' has mainly to do with the timing of the public financing being available. This is a system developed in the industry to bridge the financing gap existing between the beginning of a film production and the time when film units could be sold through the prospectus route. Generally, before a producer

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36. Howard Goldberg, "Reducing the Risk", Cinema Canada, March 1981, p.24.

could raise his capital through public issuing of securities on his film, he must come up with the development money for packaging the different elements of a film production, such as the screenplay, the name actors and director. The amount of this initial cost could be very high.[37] At the same time tax shelter investments in the industry are often skewed toward the latter part of the year. Thus there is a need for the producers to borrow interim funds at the beginning of the year when some production activities must be completed. This interim financing is available from both the CFDC and private commercial banks.

The CFDC first embarked on the interim financing program in its fiscal year 1978-79. Through this program the CFDC made loans to producers so that they could begin production early in the year before permanent financing become available later.[38] One condition on the interim loan is the repayment of fees and interest when the production funds are raised toward the end of the year when the tax shelter money is in full swing.

Commercial banking institutions, as noted earlier, had traditionally been shying away from financing feature film production because of the complexities and risks involved.

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37. According to one estimate this cost can be close to$200,000. See Susan Cole, op. cit., p.60.

38. CFDC, <u>Annual Report</u>, 1978-79, p.5.

However, since the development of equity financing in the industry and the rise of interim financing, commercial bankers' interest in the industry has started to pick up.[39] Given a proper guarantee, Canadian commercial banks deal with film producers on a short term debt financing basis. Usually they are the last to join in the financing but specify that they are to be the first to be paid off. The Canadian Imperial Bank of Commerce and the Bank of Montreal are two prominent examples of the bankers' new role in financing film productions.[40]

Innovative Approaches to Film Financing

Since the introduction of tax incentives large amounts of private money have been attracted to the film industry. This offers more production opportunities and enables the producers to learn more about the financial aspects of the trade. With increased experience and expertise, Canadian producers developed some innovative financial methods through which it was hoped that risks to the private investor would be reduced and thereby some stability brought into film investments.

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39. W.G. Iven, op. cit., p.6.

40. The Canadian Imperial Bank of Commerce and the Bank of Montreal were reportedly involved in $5 million and $1 million financing deals respectively in 1980 on two movies, 'Bells' and 'Utilities'. See Ron Base, "Why Bob Coopers Going Corporate", Canadian Business, December 1980, p.32.

At the very beginning of the feature film production industry, Canadian producers followed the independent production model which existed in the United States, i.e., production was organized on a film by film basis. As soon as a film was completed, the film production company would be disbanded. It had the advantage of minimizing the production cost. However, it also suffered a disadvantage of being a more risky venture and thus lacked the stability investors desired.

When public financing came into play, film production in Canada was still being financed on an individual picture basis. But by 1980 there were moves in the Canadian film community to move away from this model and follow approaches which would enhance private investors' confidence.

One of these approaches was 'cross-collateralization'. This is a scheme by which two or more films are offered to the investor in one package. By allowing the investor to buy into two or more films in one single unit it was hoped the investors will be able to spread the risks.[41] This would increase the attractiveness of the film investment and thus the producers' ability in raising production funds. For example, two Canadian production companies have followed this approach. Cooper-Rosenfeld sold units in two movies, "Bell" and "Utilities", all under one issue. So did

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41. Howard Goldberg, op. cit., p.23.

Filmplan International on three movies, "Gas", "The Fright" and "Comics".

An outgrowth to the "cross-collateralization" approach was the "corporate" method in financing films. The emergence of the corporate approach is a very logical development because it would offer more stability to both the investors/financiers and the industry at large.

In the corporate approach, the film company rather than an individual film product is publicly offered to the investors. In this way an effort is made to build an industrial base to the industry. Compared to the independent mode of production, this corporate structure of the new film companies offers a sense of permanence to the industry. Through this new structure, producers hoped to be able to raise the production funds first and then select film projects later which they believe would be commercially successful.[42] This new approach in turn would attract investment from the private sector by offering a viable stock in the market. It would also move the film producers from relying excessively on the tax-shelter money. For the banking institutions the new approach would offer a more healthy business venture.

By 1980, a group of companies had indeed moved away

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42. See "New Method of Film Financing is Premiered", Financial Post, May 17, 1980.

from the independent mode and organized their companies on a sound industrial structure. Examples of these companies include the Robert Cooper Productions, Famous Players Film Ltd., Seven Arts Studios Inc, and Jarnac Film Holdings.[43]

Emergence of a New Breed of Producers

Since the introduction of the tax incentive into the industry, a new type of film producer also emerged in the Canadian film community.[44] As noted before, most Canadian producers in the past had been over-emphasizing the artistic and creative side of film production. Their apparent lack of business expertise and realism had hindered a full-scale development of a commercially viable feature film industry.

Because of the new tax incentive, production of feature films had become a very rewarding enterprise financially. A new breed of producers, who are noted for a business orientation, are attracted into the industry. This group includes professionals such as lawyers and chartered accountants and enterprisers.[45] They see that their function in the industry is to "package" films in such a way

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43. Ron Base, op. cit., p. 34.

44. Kaspars Dzeque, op. cit, p.47.

45. By way of examples, Garth Drabinsky, producer for "Disappearance", "Changeling" and "Silent Partner", is an attorney by training; Robert Cooper, who is noted for his production of "Ticket to Heaven", "Running" and "Middle Age Crazy", is also a lawyer. David Perlmutter, who produced "Double Negative" is a chartered accountant.

that makes them marketable. They believe this can be achieved by promoting quality products and emphasizing the function of distribution.[46]

As a result of their business approach, these producers are noted for their ability in raising production funds and for making deals with distributors, both domestic and international. In film financing, many producers, in taking advantage of the tax incentives, offered different financing packages to attract the new tax-shelter money.[47] In addition these producers were innovative in raising their production funds, as we have seen in the last section.

Also, because of their stress in film distribution, some of the new producers were outstanding in their achievement in gaining access to major American distribution outlets. Several examples will suffice here. The producer of films like "Atlantic City U.S.A." and "Violette Noziere", the International Cinema Inc., for example, had been able to make a deal with Twentieth Century Fox through whom the films produced by the former would be distributed in the American market. Another company, DAL, producer of "Meatball", was able to make arrangements with Paramount to

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46. A good example of this orientation of the new producers is Pierre David, president of Filmplan International. See Wayne Grigsby, "Moguls Mastering the Role", Maclean's, September 1, 1980, p.52.

47. See Kaspars Dzeque, op. cit., p.98-99.

distribute another film "My Bloody Valentine". Garth Drabinsky's "Tribute", on the other hand, was distributed by Twentieth Century Fox in the United States. Robert Cooper's "Running" was aired by the American Broadcasting Company and distributed by Universal in the U.S. market.

These examples show the ability of the newly arrived producers in making films deals. They seem to have developed the business expertise which had been missing in the Canadian feature film industry.

Achievement of the Tax Incentive

With the introduction of the tax incentive, and the subsequent development of a new financing system as well as the emergence of a new type of film producers, the Canadian feature film industry in the latter part of the 1970s underwent a revolutionary change. By 1978 film production had achieved a new industrial level. At the same time the film quality also became more commercially appealing. This made the films a far cry from those produced just a few years back. Several distinct characteristics of the new industry can be observed.

Increased Private Endeavors

One notable development, as soon as the tax incentive was in place, was the increase in the number of film productions undertaken without the financial assistance of the CFDC. In 1976 thirteen such privately funded films were produced while in 1977 the number was fourteen. / These are significant figures since a total of 29 and 34 Canadian films were produced respectively in 1976 and 1977. These private efforts represent a little over 40% of the total productions.

As stated earlier, over 90% of Canadian feature film productions in the period prior to 1976 received some form of financial assistance from the CFDC. The increased private production thus was an important improvement in the industry in the sense that less dependence was placed on the public funds for production starts. As matters stand, the trends toward private production in 1976 and 1977 were only a harbinger of the revolution that was to come by 1978.

Film Output and Investment

By 1978, because of the generous tax-write off and new setup of film financing system, an abundant supply of capital became available to film productions. This had a profound effect on the working of the industry.

Table 5-4 gives some statistics on the industry between the years 1976 and 1980. It shows the annual output and investment during the period.

Table 5-4

Film Production 1976-1980

Year	No. of Output	Total Annual Budget Costs ($ Million)	Average Cost per Picture ($ Million)
1976	29	NA *	-
1977	34	NA **	-
1978	31	63.7	2.05
1979	55	150.0	2.72
1980	53	205.0	3.87

Source : Compiled from current periodicals.

Notes-

* Not available. But estimates on the total budget of the 16 films produced with CFDC assistance in fiscal year 1976-77 was about $12 million.

** Not available. Estimates on the total budget of 20 CFDC assisted films was around $5.5 million for fiscal year 1977-78.

Comparing Table 5-4 and Table 5-1 in this chapter, one can detect the significant increase in terms of both output and investment in the industry since 1978. Between the years 1970 and 1975, Canadian film output had been ranging between 20 to 30 pictures annually. However, with the increased capital supply, film production jumped from the 31 films made in 1978 to a little over 50 by 1980. More significantly though was the difference in the annual amount of money invested in film productions. Again from Table 5-1 one can estimate that over the first half of the 1970s the average annual investment in film production was around $7.6 million. Investment in 1978 was $63.7 million, a comparatively astronomical number. The subsequent increase in investment to $150 million in 1979 and $205 million in 1980 only helps to point out the tremendous push the tax-incentive gave to film productions.

Film Quality

Table 5-4 also portrays a change in the quality of individual movies, if one accepts the industry's notion of quality being commensurate with costs. In the three years since 1978, 139 films were produced with a total budget of $418.7 million. This means that the films produced during this period had an average cost of $3.01 million. Compared to the average budget cost of less than $300,000 for the 180 films produced in the first eight years of CFDC's operation,[48] the budgets of the new films are indeed impressive. While we have observed that in the earlier period there were few pictures produced with a budget over $750,000, some of the new films have been reported with a

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48. See section II of this chapter.

budget reaching over seven or eight million dollars. Indeed the trend toward big-budgeted movies was so prevalent that, by 1981, trade journals, when compiling statistics on some current films' budget, could handily list forty four films that cost over $1 million.[49] As the industry reported, by 1978 any film that was produced under $2.5 million ran the risk of being considered low-budgeted.

One observable result of the change in the budget cost of these new films is in the box office success. As one industry source puts it, in previous years there were scarcely any financially successful Canadian films. However, in just two years since 1978, one can cite at least ten or more commercially successful movies.[50] In fact, the successes of some films turned out to be overwhelming. "Meatball", for example, was produced with a budget of $2 million. Its box office receipt was $50 million. Other films such as "Scanner"(cost $3.8 million, received $12.4 million),"Prom Night"(cost $1 million, received $14 million) and "Running"(cost $3.6 million, received $7 million) added

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49. For example, "Quest of Fire" was reportedly produced with a budget of $9.5 million; "Heavy Metal" has $7.3 million and "Harry Tracy-Desperado" had a budget of $8.3 million. In the May 1981 issue of Cinema Canada, the breakdown on the distribution of recent films by budget size was as follows: 6 pictures at $1-2 million; 6 at $2-3 million;9 at $3-4 million; 10 at $4-5 million;7 at $5-6 million; and 5 over $6 million. See"Recent Features, Sales Information", Cinema Canada, May 1981, pp.28-34.

50. Ron Base, op. cit., p.35.

to the successful list.

Another significant implication of the change in budget costs is that it signaled a new strategy by Canadian producers in breaking into the market. As noted earlier, the initial approach by Canadian producers had been to undertake low-budgeted films that were geared primarily toward the Canadian domestic market. However, with the new-found financing resources, the new producers managed to package films in such a way that they offered strong competition to the American products and offered an equivalent international appeal. This was achieved by using some name actors in the American industry and high cost scripts. At the same time, part of this new international orientation was also due to the co-production between Canada and treaty countries.

Finally, lest we give a false impression that the recent trend in big-budgeted productions is a welcome direction in improving the quality Canadian films, it should be pointed out that there are serious debates on the wisdom of such an orientation. In fact some film critics are alarmed by the public support of production activities that are geared more to the international market than Canadian audiences. Because of the recent emphasis on using foreign named talent and story materials, most of the films produced since 1977 are not perceived as reflective of Canadian ideas, values and talent. Rather they are viewed as products through which slick enterprisers can make commercial gains in the continental market. Due to this cultural aspect, the achievements of recent production are seriously open to questions. It also brings into focus the need of a balance between the 'cultural objective' and the need of 'commercial viability' in the public support of film productions.

IV. MARKET ACCESS DIFFICULTIES AND COMBINE INVESTIGATIONS

With the introduction of the CFDC and the 100% capital cost allowance, public policies have successfully overcome entry barriers on the production side. Unfortunately, despite a surge of production activities, the full development of the industry remains hindered by the problem of market access.

As matters stand, the distribution system Canadian producers had difficulties with earlier, remains intact.[51] The new films that are produced with public assistance and tax shelter money still have to rely on the major foreign distributors for a viable distribution arrangement. In

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51. It was reported many of the fifty-five films completed in 1979 failed to gain any international distribution. The CFDC reportedly estimated that only one quarter of the films made between 1976 and 1979 will return any part of their investment. See Susan Cole, op. cit, p.62 and Patricia Best, "Struggling to make the Big League", Financial Post, May 16, 1981.

spite of a few examples of cooperation between some Canadian producers and major American distributors, the fact remains that most of the films produced did not have any distribution guarantee.

Both the public and private sectors made several attempts to overcome these distribution difficulties. So far, these efforts have met limited success. Two measures stand outstandingly among these attempts. They are the 'voluntary quota' system and the call for combine investigation of the distribution system operating within Canada.

As explained in an earlier section, the voluntary quota system was negotiated between the government and the two largest exhibition circuits in Canada. Through this agreement the two theatre chains agreed to show Canadian films for a minimum period of two weeks in their theatres in each of the largest three cities. By this agreement the government hoped that Canadian films would be guaranteed screen access. The dismal returns on most Canadian films shows that this system has not been effective.

On the other hand, in an effort to overcome the market access problem, nine citizens from the private sector of the film industry made a formal application to the Director of Investigation and Research, Combines Investigation Branch, of the Department of Consumer and Corporate Affairs. The application was for an inquiry into the market practices of the foreign-owned theatrical exhibition and distribution system in Canada. This was based on their belief that the major concerns had abused market control through practices such as tie-selling, exclusive agreements and refusal to deal with independents.[52] All these practices help to lessen competition in the supply of films and thus prevent Canadian films from having reasonable access to the Canadian exhibition market.

Because of the long-term nature of combine investigation activities, the main inquiry that stemmed from this application is still continuing at the present time.[53] However, in the course of the inquiry, the Director of Investigation and Research has found evidence of price manipulation among the distributors. This evidence was turned over to the Attorney General of Canada. Subsequently charges were made against several major distributors including Columbia Picture Industries, Inc., United Artists Corporation, Bellevue Film Distributors Limited and Warner Brothers Distributing (Canada) Limited. Except for Warner Brothers, all these distributors pleaded guilty. They were issued prohibiting orders against any future price

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52. See organization reports in Cinema Canada, March 1976, No.26, p.10.

53. Director of Investigation and Research, Combines Investigation Act, Annual Report, 1980, p.57.

maintenance and fined accordingly.

However, the combine investigation activities so far have not yet achieved the results the inquiry applicants had hoped for, which is the opening up of the exhibition and distribution system to the Canadian producers for more market access. This result will depend on the final outcome of the investigation.

V. POLICY ALTERNATIVES FOR MARKET ACCESS

With the increase in production activity, removal of the market acess barrier becomes a prerequisite for a fuller development of this industry.There are several plausible alternatives, each with its own merit and weakness. Here we will examine some of the major options which include the use of legislative quotas, vertical integration of the industry, alternate distribution media, and investigation of the current system.

Legislative Quotas

One of the popular alternative often cited as a solution in getting Canadian film production into Canadian cinema is the use of legislative quotas,[54] which would be stricter than the voluntary system currently in use. Proponents argue that the quota system has been used

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54. Council of Canadian Filmmakers, "Policy Statement on Feature Films", Cinema Canada, February-March 1974, p.50-51.

practically all over the world except the United States and is an effective tool to get a national product shown.

However, even though quotas can guarantee access to screen time for Canadian films, there are several considerations that would negate the benefits of such a system. In the first place adoption of a compulsory quota system might lead to retaliation from other countries. This might unduly restrict the market potential of the Canadian films and aggravate the difficulties imposed by the small domestic market size. Secondly, the quota system would run the risk of protecting mediocrity in film production. Since audiences could not be legislated to see certain types of films, the effectiveness of this system is doubtful. Finally there is the question of practicality. The jurisdiction over theatre exhibition in Canada is within the provinces. To carry out a national quota system would require cooperation from the provinces. But it appears that there are different objective among the provinces, which makes the quota system impractical and even dangerous.[55]

In view of these considerations, the benefit reaped from a legislated quota system may well be less than the cost involved. Such a system thus is not advisable.

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55. Jean-Pierre Tadro, "A Conversation with Hugh Faulkner", Cinema Canada, May 1976, p.34.

Vertical Integration

An option which would help to increase the market access of Canadian films is the creation of a completely Canadian-owned distribution and exhibition system. This means a move toward vertical integration of the industry and an extension of the current production activities into the distribution and exhibition branches of the industry.

The benefit of such a vertically-integrated operation would be a reduction of the risks in film production .With the assurance of a viable outlet and proper promotion , the risks of a Canadian production could significantly be reduced. This is due to the fact that such an operation could give the Canadian concerns the ability to achieve risk spreading by offsetting losses against profits reaped in the exhibition field. Furthermore, involvement in the distribution and exhibition activities would assure that the revenues from this market stay in the country and possibly return to further production.

But to achieve such an integrated operation, it would be necessary to create new or to purchase existing distribution and exhibition facilities. The cost for such a business move appears to be prohibitive.[56] In view of the

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56. As one federal studies concludes, the investment need for such an operation would be in the order of several hundred million dollars. See BMC, <u>Evaluation</u>, Vol. 1, p.44.

large amount of resources involved, serious doubt exists as to the advisability of such a move. As has been stated in a previous chapter, there appear to be substantial economies of scale in the distribution of films. Inherent pressure exists for distributing as many pictures as possible in order to reduce the cost. Given the small market base in Canada, there will be a forced dependence on the international market. At the present time when there is still serious debate between 'commercial viability' and 'national cultural value', increases in the allocation of resources toward this industry would be open to doubt.

Alternative Distribution Media

If the creation of a Canadian-owned distribution structure in the theatrical market does not seem appealing, there remains one possible alternative for getting the Canadian production to the Canadian public. This is distribution through television and the new technologies such as pay-television and video cassettes.

As has been discussed earlier, network television screening of movies during prime time has been a significant revenue-generating factor for film productions since the 1960s. Because of program demand, there are at present film productions primarily geared toward television showings and in which the CFDC is involved. It appears, though, that the move toward primary distribution through television is not necessarily well received among critics in the film community.[57] However, in view of the difficulties in the access to the Canadian theatrical market and the fact that there are well-established Canadian television networks, both public and private, the television market would be a feasible and practical solution for Canadian productions. A re-orientation toward the television market might require little additional resources for a viable distribution outlet. In this way television networks such as the Canadian Broadcasting Corporation could play a significant role in enhancing the production industry.

More importantly, the recent development in the pay-television and video cassette industry might open up a more lucrative market for film production . With the ever increasing popularity in home movies through both pay-television and video machines, a more convenient and less costly distribution method is open to Canadian producers. It is therefore important, especially in the establishment of a pay-television system in Canada, that these new facilities should be kept under Canadian control so that the readily available market will help to reduce the risks and thus enhance future investment in Canadian productions.

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57. It is primarily due to their beliefs that there is a distinct difference between a film for television and feature film which is ultimately shown on television. See Council of Canadian Filmmakers, "Policy Statement on Feature Films", Cinema Canada, February-March 1974, p.51.

Investigation of Current Market Structure and Conduct

A re-orientation toward alternative communication media, on the other hand, should not be construed as the abandonment of the theatre market. For a viable film industry, the theatre market is still needed for successful Canadian production. While distribution through television showings could be a relatively short-term solution, a long-term approach to the problem of theatre market access might be a detailed investigation of the industry's market structure and practices.

As mentioned before, the foreign distributors have been reluctant to handle Canadian productions essentially because of their commitments elsewhere. More recently, some of these major concerns have been found guilty of price manipulation in the distribution of films. These findings point out the existence of anti-competition forces within this sector of the market. The Canadian producer may have been unfairly shut off from their own market.

Because of the difficulties experienced by Canadian producers, a thorough examination of the legal and economic aspects of this distribution/exhibition sector of the industry might be warranted. Since most companies in this sector are working on an 'international' basis, this study should be conducted on an 'international' context. The primary object should be to see whether the structural element, especially the vertical structure, and the conduct of these foreign concerns, have bestowed upon themselves a market control that is detrimental to Canadian interests. Through such studies, it is hoped that the causes of the Canadian difficulties in this market could be determined. Only then could remedies be possible.

VI. SUMMARY

In an effort to promote a feature film production industry, Canada adopted two important public policies : the creation of the CFDC and the 100% Capital Cost Allowance.

The CFDC invested in production projects undertaken by private producers. By providing financial and pre-production assistance, the government hoped to stimulate interest in feature film production. The tax-shelter incentive, on the other hand, was used to attract more capital from the private sector for productions.

As a result of these two policies, Canada has witnessed a steady increase in feature film output. It jumped more than 15 times from 3 films in 1968 to more than 50 in 1980. The growth is remarkable. Employment opportunities thus increased for Canadian technical and creative talents.

In the course of this development, Canada has undertaken different approaches to solve the market problem of a small domestic market overwhelmed by foreign competition. In the beginning, the CFDC invested in films that had relatively low budgets but which were noted for their orientation toward Canadian subject matter. It was hoped that the costs could be recouped from the domestic market. A more recent approach led to the production of films that had a budget comparable to quality pictures from abroad, in the hope of recovering the costs from the continental market. Therefore, there usually has been more international appeal than Canadian value in these films.

It should be noted that, primarily as a result of public policies, barriers in the production area have mostly been removed. Creative financing systems were set up with the development of a new class of producers. Interest was also generated among banking institutions which now would readily participate in 'interim' financing systems.

But the development of the industry during this decade has still been hindered by difficulties in the market access area. The CFDC, in helping with the distribution of films, has funded promotion campaigns and other international festivals. Negotiation was undertaken with the two major theatre circuits, leading to a voluntary quota system for showing an annual minimum amount of Canadian films in their theatres.

Apparently, the emphasis on solving the distribution difficulties has not been enough. Canada still does not have a viable distribution structure of its own. The exhibition and distribution sectors are still dominated by foreign concerns. This may have been partly responsible for the lack of financial success of Canadian productions.

To bring this industry into a more advanced stage of development, a solution has to be found for getting the Canadian film to its audiences. Several options are possible. However, legislative quotas would unduly restrict the market potential of the Canadian films in an international context. Establishment of Canadian-owned distribution facilities seems infeasible because of huge additional resource requirements. A reorientation toward other distribution and exhibition media, such as existing television networks, the coming pay-television system and home video machines, seems to be the most welcome option. But a change to alternative distribution media should not signify complete abandonment of the theatre market. In depth investigation of market structure and conduct among foreign distribution and exhibition concerns operating in Canada should be conducted. If necessary, legislative or executive remedies should be prescribed so that Canadian producers will have a fairer share of the domestic market.

Chapter 6

Conclusion

In the course of this study, it has been found that scale economies and product differentiation are not critical entry barriers in the feature film industry. However, because of the unique nature of this industry, product differentiation is an important attribute to marketability. The inherent requirement for heterogeneous products makes the film production industry a highly risky and uncertain business.

In Canada, there are several important factors hindering entry into feature film productions. On the production side they are the general lack of financial resources and skillful producers; on the market side, foreign competition, a small domestic market, and inaccessibility to distribution facilities. This last factor is further aggravated by the vertical structure of the exhibition and distribution sector of the industry.

In the production area, financing difficulties are due to three main reasons. Firstly, there is deficiency in investment from private investors because of few track records of success in the production of Canadian feature films. These investors are further discouraged by the high risk nature of the industry. Secondly, producers have little access to banking institutions, partly due to the lack of experience and expertise on the part of bankers. Lastly, because of high consumption of foreign products, most of the admission revenues from Canadian cinemas are remitted abroad in the form of film rentals. Not enough money is reinvested into production of Canadian films.

On the market side, the combination of a small domestic market and strong competition from foreign products leaves little room for spreading losses, making the business even more risky. However, the most critical element is the lack of access to a good distribution system. This is essentially due to the fact that most distribution and exhibition concerns in Canada are foreign-owned. They are tied to production activities abroad and less inclined to handle Canadian products.

The above-mentioned factors contributed to the lack of feature film production before the arrival of public assistance. Since the late 1960s, however, there has been remarkable development in the industry. Within a decade of public support, production output increased almost some fifteen-fold. Employment opportunities also have been increased for Canadian talent. This change has been brought about primarily by public assistance aimed at overcoming the production difficulties through two different approaches.

A direct approach was the creation of a federal agency, the Canadian Film Development Corporation, which is funded and mandated to invest financially or make loans for the production of feature films that have significant Canadian artistic and technical content. An indirect approach was through a tax incentive in the form of 100% capital cost allowance for Canadian feature film production. This tax-shelter approach has been used to encourage more private investment in order to help the industry overcome the barrier of deficient production capital.

As a result of these governmental policies, difficulties in the production area have essentially been removed. Seed money for new production become available through the CFDC. The tax incentive spurred a vigorous response from private investors. Films are now financed by prospectus for the first time. Interest has also been generated among banking institutions in participating in an 'interim' financing system. New entrepreneurs has been attracted, forming a new class of producers who are more business-oriented and skillful.

Unfortunately, for full development of this industry, market access remains to be an area of great concern. At the early stage of CFDC's operation, low-budgeted films with relevant Canadian content were produced; they were expected to recoup the production costs within the domestic market. A more recent approach has been to produce films with higher budgets and more international appeal, aimed at gaining profits in a continental context. Both approaches attained dubious results and are open to debate.

At the same time, even though there is a voluntary quota system, and some combine investigation activities, Canadian films still have difficulties in receiving proper distribution. The fact remains that the distribution and exhibition facilities are still controlled by foreign interests. No viable distribution structure exists yet for Canadian production.

As production is not an end in itself, the market weakness has shown that Canada has failed to put enough emphasis on removing the distribution barriers. To develop a better feature film industry, this barrier has to be dealt with more effectively.

There are several possible options in dealing with market access difficulties; they include the use of a compulsory quota, vertical integration of the industry, distribution through alternative media, and investigation of the distribution/exhibition structure.

A compulsory quota does not appear to be advisable, since it may lead to foreign retaliation, resulting in undue restriction on the market potential of Canadian films in an international context. Also the question of practicality would also restrict the effectiveness of this system.

Vertical integration of the industry through purchase or creation of a new distribution/exhibition system would guarantee access to the audience. However, this approach seems doubtful because of the huge additional resources required and also because of the scale of operation involved.

The most feasible alternative in solving the market access problem might be a re-orientation toward other communication media such as television and home video machines. Because of the existence of Canadian-owned television networks, this approach might require little additional investment. The potential market resulting from new video technology also makes this alternative attractive to Canadian productions.

But the use of alternative media should not mean the abandonment of the theatre market. In this regard, a long range approach to the access problem would be an in-depth investigation of the market structure and practices of the existing distribution/exhibition sector of the industry. The object of such a study should be a determination of whether unreasonable market restrictions have been imposed by foreign concerns on Canadian productions. Legislative and executive remedies should be prescribed when necessary.

Finally, a review of the overall governmental objective of fostering a Canadian feature film industry may be warranted at this time. As we have seen, one of the main goals of public assistance to this industry was to promote cultural values and awareness in the country. However, the government also assumed that this industry would be commercially viable. The development of the industry in the past decade has certainly demonstrated a certain degree of incompatibility between these two objectives. This conflict is illustrated by the fact that the early productions, with relevant Canadian content, proved to be financially disappointing, while the more recent financially successful films are characterized by their 'international' appeal and diminished Canadian relevance. A balance between the two values has to be found if governmental objectives are to be fulfilled.

However, in a broader perspective, the wisdom of restricting public support to feature film production is also questionable. Given that theatre-going nowadays is less than a universal hobby, the effectiveness of using this medium to promote national cultural values is debatable. One may ask whether it might not be more beneficial to diversify public resources into other communication media such as non-theatre films, television, broadcasting and publishing. With large amounts of resources already expended in the past decade bringing marginal cultural achievement, it does appear that a reallocation of public resources from the feature film industry to alternate media is highly advisable. But in the process of reducing public involvement, measures should be taken to protect to a reasonable degree the private interests that have developed in the industry.

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