

Exhibitor Orange Sky Golden Harvest continues to expand



## High cost of admissions

Explosive growth in screen numbers is driving up box-office revenues in China, but such rapid expansion could present risks for some exhibitors. **Liz Shackleton** reports

From the outside looking in, Chinese exhibition appears to be one of the sweetest spots to be operating anywhere in the world today. China's box office grew by 30% to hit \$2.7bn in 2012 and won't be slowing down any time soon. The number of screens increased by around 3,800 last year — reaching a total of more than 13,000 — an average of more than 10 new screens a day. The dynamic growth is driven by well-heeled cinema investment companies racing to meet demand from an increasingly wealthy population with time on its hands to watch movies. Or so the story goes.

'Cultivating virgin territory has been the secret of our strategy'

**Fang Bin, Dadi Cinemas**

But while this is true to some extent, the spoils are not being shared evenly in the Chinese exhibition industry and it is a tough business even for those with substantial resources. Competition has become fierce as cinema operators have prioritised expansion over profitability in the race to grab market share. And as the number of screens has exploded, per-screen revenues and admissions, especially in the first-tier cities, have started to decline.

The market is also reaching saturation point in major cities such as Beijing, Shanghai, Guangzhou

and Shenzhen, while costs for construction, rent, labour and marketing are rising rapidly.

"We believe there are probably too many cinema operators in China to sustain over a long-term basis," says Rance Pow of Shanghai-based consultancy firm Artisan Gateway. "The growth rate of new cinemas will slow as the focus shifts to riskier second and third-tier markets. Failures will increase as the market reaches saturation point and increased competition will expose the weakness of some operators."

By the end of 2012, China had 3,680 theatres with 13,118 screens, of which 93% are digital and 72% are 3D-enabled. All urban cinemas are required to join one of 40 government-approved chains, which arrange film bookings and take a 1%-6% fee from box-office revenues. A few private companies, such as Wanda and Dadi Cinemas, have been allowed to establish their own chains. Although foreign players are restricted to a 49% market share in cinemas, Korean exhibitors such as CJ CGV, Lotte and Megabox have made some headway in rolling out new cinemas in the market.

According to local market research firm EntGroup, the five biggest chains take more than 70% of box-office revenue, leaving 35 chains to scabble for the remaining 30%. The intense competition, especially in big cities, has resulted in ticket price wars and group sale discounts, which drive down profitability. Taking into account these pressures and rising operating costs, many exhibitors say they now regard their big-city theatres as a branding exercise, while they look to second and third-tier markets to turn a profit.

Moving into smaller cities where costs are lower and audiences have never before experienced a multiplex seems like a no-brainer. "We opened an eight-screen multiplex in Xining in the west of China that became profitable in the second month," says Crystal Wang, director of strategic planning at Orange Sky Golden Harvest.

Some exhibitors, such as Dadi Cinemas, even started out by focusing on smaller markets, although they later moved into the big cities. "Cultivating virgin territory has been the secret of our strategy, although we've also opened cinemas in Shanghai and Beijing," says Dadi Cinemas general manager Fang Bin. "We have been successful in identifying the right sites and attracting audiences that didn't previously have a convenient venue to watch films."

However, cinema operators are also taking a risk in these smaller markets. Ticket prices need to be relatively high to cover start-up costs, but local audiences are used to consuming films cheaply and illegally online. "There is a risk because you're introducing a social habit to audiences for the first time," says Pow. "The interest in the content is proven but it becomes a value proposition. Do I spend \$5.60 (RMB35) on a ticket or continue to consume movies the way I've been accustomed to?"

In other words, you have to cultivate the audience in second and third-tier markets, and that takes time. Feeling the pressure to stake out territory and grab market share, cinema operators are pushing into riskier and more remote markets, even though they will not be making money in all of them for some time. And even if you are the first cinema in town, you will not be alone for long.

With such fierce competition, it becomes more important to differentiate your services, and while

China's box-office growth shows no sign of slowing down



most new cinemas are excellent technically, they lack experience in customer service and marketing.

Lumiere Pavilions has taken a different course, rolling out slowly and focusing on customer relationship management (CRM). "In addition to state-of-the-art audiovisual equipment, we use sophisticated CRM systems and target high-end customers with superb services," says Lumiere chairman and CEO Jimmy Wu. The company has a direct relationship with some of its most loyal customers to ensure they can book their favourite seats.

However, the best technology and service in the world does not mean a thing if you don't have good movies to show, and despite the expansion of China's import quota to 34 revenue-sharing films a year, patchy product flow has become Chinese cinema operators' biggest headache. It is not that China cannot produce huge hits. Over the past year, four films — *Lost In Thailand*, *CZ12*, *Journey To The West: Conquering The Demons* and *Painted Skin: The Resurrection* — have grossed more than \$100m. But these blockbusters are clustered around summer or the Chinese New Year holiday period and leave long dry spells in between.

"Quantity is no problem — last year China was the world's third biggest producer with more than 700 movies, but each year there are only a small number of hits," says Wanda Cinema Line general manager Ye Ning.

"Feng Xiaogang only makes one film a year, and there's only one sleeper hit like *Lost In Thailand*, so it's not enough. We need great content every week — at least two blockbuster titles every month. But there are only a few film-makers who know the rules of the game."

Some cinema operators have started to experiment with alternative content, including 3D sports, concerts and operas, but government censors such as the State Administration of Radio, Film and Television (SARFT) have not formulated clear policy for screening this kind of product. Lumiere Pavilions screened some games from the 2010 FIFA World Cup and 3D operas *Carmen* and *Madam Butterfly*, co-produced by RealD and London's Royal Opera House. But Chinese cinema operators are not allowed to sell tickets for such screenings, so the audience attended for free and the costs were offset by commercial sponsors.



'We target high-end customers with superb services'

**Jimmy Wu, Lumiere Pavilions**



'Failures will increase as the market reaches saturation point'

**Rance Pow, Artisan Gateway**

TOP 10 EXHIBITION CHAINS IN CHINA BY BOX OFFICE 2012						
Rank	Cinema chain	Box office	% change on previous year	Admissions	% change on previous year	No. of screens
1	Wanda International Cinemas	\$389.5m	+38%	58,416,700	+43%	998
2	Shanghai United Circuit	\$261.7m	+27%	44,676,200	+18%	1,128
3	China Film Stellar Theater Chain	\$256.9m	+18%	43,877,000	+14%	1,094
4	China Film South Cinema Circuit	\$210.3m	+22%	34,637,799	+21%	1,010
5	GZ Jinyi Zhujiang Movie Circuit	\$186.3m	+38%	30,593,600	+36%	801
6	Guangdong Dadi Theatre Circuit	\$175.2m	+63%	38,501,299	+64%	1,382
7	Beijing New Film Association	\$130.9m	+8%	22,062,100	+5%	576
8	Zhejiang Time Cinema	\$113.6m	+29%	19,584,800	+26%	691
9	The Pacific Ocean Sichuan Theater Chain	\$95.6m	+29%	16,483,899	+21%	450
10	HG Entertainment	\$90m	+62%	17,133,200	+56%	637

Source: EntGroup

Lumiere is now working hard to lobby SARFT to allow alternative content to be shown in cinemas. But in the short-term, the authorities' focus is likely to be on developing the local film industry, rather than encouraging different kinds of competing product.

The good news is that Chinese films are improving and becoming more market-oriented. Recent developments such as Beijing Galloping Horse's acquisition of Digital Domain should also lead to improved production values. The big issue is one of timing: how long can existing cinema operators wait for a steady product supply and for consumers to change their habits and become regular cinema-goers?

Only the most efficient, service-oriented or deep-pocketed players will be able to sit out these tumultuous early stages of China's

film industry development. And with competition and costs increasing, the currently fragmented exhibition sector is likely to go through a period of consolidation over the next few years. Already big players such as Wanda, which has the advantage of owning most of the real estate that houses its cinemas, are starting to eye acquisition targets.

In the meantime, it will be difficult for new players to find a foothold in the market, even though there is undoubtedly room for many more screens.

"We believe it may be too late for new entrants," says Pow. "We are looking at the tail-end of multiplex development and anyone coming in now is late to the game." **S**



(Left) Painted Skin: The Resurrection