

# **Films**

A report on the supply of films  
for exhibition in cinemas in the UK



MONOPOLIES AND MERGERS COMMISSION

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A report on the supply of films for  
exhibition in cinemas in the UK

**Presented to Parliament by the Secretary of State for  
Trade and Industry by Command of Her Majesty  
October 1994**

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<sup>1</sup>These members formed the group which was responsible for this report under the chairmanship of Mr P H Dean.

## **Note by the Department of Trade and Industry**

In accordance with section 83(3) and (3A) of the Fair Trading Act 1973, the Secretary of State has excluded from the copies of the report, as laid before Parliament and as published, certain matters, publication of which appears to the Secretary of State to be against the public interest, or which he considers would not be in the public interest to disclose and which, in his opinion, would seriously and prejudicially affect certain interests. The omissions are indicated by a note in the text.

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Part I

# **Summary and Conclusions**

# 1 Summary

## Introduction

1.1. We have been asked to investigate the supply of films for exhibition in cinemas in the UK. When making this reference to us the Director General of Fair Trading indicated that his own enquiries into the industry had been prompted by complaints from independent cinemas about difficulties in obtaining popular films from distributors. He added that most of the major companies were vertically integrated and followed practices which could lead to the exclusion of independent producers, distributors and exhibitors from the market; and that although there had been changes in the market since the previous MMC report in 1983, he considered competition remained restricted to such an extent that a full investigation was appropriate. Our terms of reference are set out in Appendix 1.1. The EC Commission is also currently considering applications for clearance under EC competition law of certain joint ventures in the industry.

## Background

1.2. The theatrical distribution market was worth £103 million in 1993. The five leading distributors, Buena Vista, Columbia, Fox, UIP and Warner Distributors, all of which are affiliated to Hollywood studios, accounted for about three-quarters of receipts from film rentals in the period 1990 to 1993. Each distributor's shares fluctuate quite widely from year to year, reflecting the success of individual films. Several independent distributors, of which the largest are Entertainment, First Independent, Guild and Rank Film Distributors, make up the balance of this market. The leading distributors are mainly in business to distribute the films of their respective Hollywood studios, though most also distribute independently-produced films to a limited extent. The independent distributors compete to obtain independently-produced films.

1.3. In the exhibition market there are likewise five leading players: two owners of long-standing circuits, MGM Cinemas and Odeon, and three recent US-owned entrants specializing in the operation of multiplex cinemas, Natl Amusements, UCI and Warner Theatres. These five exhibitors account for almost four-fifths of the £289 million box office receipts in 1993, numerous independent exhibitors making up the balance. All the leading exhibitors except Odeon have some ownership link, direct or indirect, with a Hollywood studio, but these links are not as close as those between the Hollywood studios and their respective distribution affiliates.

1.4. The relationship between the distributors and the exhibitors is complex and symbiotic. Neither side currently dominates the other, though independent exhibitors are at a bargaining disadvantage *vis-à-vis* the leading distributors, as are independent distributors *vis-à-vis* the leading exhibitors.

1.5. The industry has been transformed since our 1983 report and is still undergoing change. By July 1994 71 new multiplex cinemas had been built and others are under construction or planned. Exhibitors have also invested heavily in refurbishing older cinemas and converting them to multi-screen use. There has been a substantial increase in the number of cinemas which show popular films on first release. Advertising and publicity budgets have risen strongly. Audiences have doubled after many years of continual decline. Cinema admission prices are not excessive. In contrast to the

resurgence which has occurred in cinema-going, however, British film production during the last ten years has languished.

1.6. A large and growing proportion of the revenues from the exploitation of films comes from the rental and sale of video cassettes and from various forms of television broadcasting. But while the cinema now represents perhaps only a quarter of total revenues, it remains highly important because the success of a film in the cinema is seen as the key to its success in these other markets too.

### **The monopoly situations**

1.7. We find that one scale monopoly situation and one complex monopoly situation exist within the meaning of the Fair Trading Act 1973. The scale monopoly situation involves MGM Cinemas, which over the period 1990 to 1993 made just over a quarter of exhibitors' total rental payments for the licensing of films for exhibition in UK cinemas.

1.8. The complex monopoly situation involves the five leading distributors, the four independent distributors named in paragraph 1.2 and the five leading exhibitors, and is based on our finding of the existence of a number of uncompetitive practices in the industry. The more significant of these are discussed below.

### **Public interest issues**

1.9. The scale monopoly situation does not in itself raise concerns for the public interest. The market share of MGM Cinemas is only just over 25 per cent, and there are other strong players in the exhibition market whose market shares are not far below.

1.10. We find two of the practices inherent in the complex monopoly situation to be against the public interest. The first is alignment: the practice whereby, in the first instance, a distributor normally offers its films to, and discusses the timing and release strategy for those films with, its aligned circuit, ie either MGM Cinemas or Odeon. In locations where both circuits operate directly competing cinemas, aligned distributors normally supply films to their aligned circuit but not the other. This practice, by reducing competition for screens among aligned distributors and reducing pressure on the two circuits to compete for films on merit, makes the market less responsive to consumer preferences. We condemned it in our 1983 report, but stopped short of making a recommendation because of the then parlous plight of the industry. The industry is now stronger and we make recommendations intended to bring this practice to an end.

1.11. The second practice which we find to be against the public interest concerns minimum exhibition periods. Distributors sometimes insist on lengthy minimum exhibition periods—perhaps four weeks or longer—as a condition of supplying exhibitors with prints of popular films. This practice creates problems particularly for single-screen cinemas or those with few screens, reducing their freedom to respond to consumer demand, and adds to the difficulties faced by independent distributors in getting their films shown. We recommend that minimum exhibition periods should be restricted to a maximum of two weeks on first release and one week subsequently.

1.12. Relevant to the exhibitors' complaints which led up to this inquiry is the issue of refusal to supply. The established arrangements for calculating rentals, which command industry-wide support from both distributors and exhibitors, have the effect of reducing distributors' receipts if a given audience is divided between two cinemas. Distributors therefore refuse supply in circumstances where to supply another cinema would split the potential audience and reduce their profits. Given the extent of competition in both the distribution and exhibition markets, we consider it reasonable for

distributors to determine supply with a view to maximizing profits on individual films. We propose, however, the establishment of some independent machinery to consider exhibitors' complaints.

1.13. Another issue is vertical integration, to which critics of the film industry frequently point as distorting the market and creating barriers to entry, particularly for British films. All the Hollywood studios rely upon their respective affiliates to distribute their films in the UK. Given the state of competition among the studios and in the distribution market generally, we do not object to this practice, which is common world-wide. Four of the seven Hollywood studios also have ownership links with UK exhibitors. We have examined whether these links result in dealings between distributors and exhibitors being other than at arm's length. Our analysis shows a slight degree of preference between vertically linked parties at the margin, but the evidence does not warrant an adverse public interest finding. We suggest nevertheless that certain indicators should be monitored by the Office of Fair Trading so that the matter is kept under review.

## **Overview**

1.14. Film production is an expensive and very risky business. Profitability depends on the success of a small number of films. The Hollywood studios account for a high proportion of box office receipts in the UK, but there is vigorous competition between them and no one studio dominates.

1.15. We regret that the proportion of culturally British films to be seen in UK cinemas is low, but we do not attribute this to any conspiracy or other improper behaviour on the part of the Hollywood studios or their UK affiliates. The Hollywood studios are skilled in producing and promoting films that the UK public wants to see. They have the advantage of operating in the much bigger US market, which enables them to make films with high production costs and hence to attract the most popular stars. In deciding which films to release in the UK and how to promote them, the studios benefit from the experience of prior distribution in the USA. Exhibitors are eager to show films which have proved popular in the USA and which are heavily promoted, and the shared language makes the UK market particularly receptive to US films.

1.16. We do not therefore under-estimate the problems which British film-makers face in competing against Hollywood. But UK exhibitors are interested in showing any films which they think will have popular appeal, irrespective of origin, and recent examples demonstrate that it is possible for British films to compete successfully for screen space. In so far as British film-makers produce popular films our recommendations, if implemented, may incidentally facilitate the showing of these in UK cinemas. But the main difficulties faced by the British film industry are beyond the scope of this inquiry.

1.17. The transformation of the industry over the last decade has worked well for consumers. Further changes may be expected. Today, apart from the practices we have criticized, competition in the markets under investigation is effective.