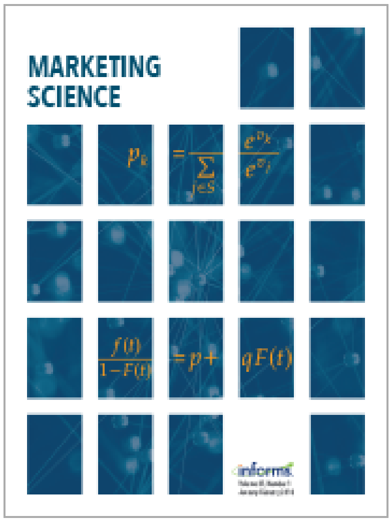


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**Invited Commentary**

# The Day After Tomorrow: Longer Run Issues in Theatrical Exhibition

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*History*: This invited commentary was received June 28, 2005, and there was no revision; processed by Steven Shugan.

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The authors do an excellent job of summarizing issues and trends that will play out in the very short run, perhaps the most pressing topics for immediate research. In addition to expanding on some of their themes, I would argue that there remain a number of issues that will arise in the slightly longer run. Given the industry's history of stunted technology acceptance, changes when they come, may come quickly. Parallels with the music industry, facing similar challenges 5–10 years ahead of movies, can be especially insightful, and I will conclude with thoughts along that longer term time horizon.

Whether countries are overscreened from a profit or social perspective is of interest to both marketers and economists, and the authors fairly frame the trends in the data and the questions. This, however, seems to be an issue that could be greatly informed with more micro-level data. The authors point out that, while admissions grew by 17% from 1989 to 1999, the number of screens increased by 62% over the same period. It seems reasonable, however, to claim that dividing a 400-seat auditorium into two 200-seat auditoria (a common step preceding the multiplex) does nothing to capacity. Given that U.S. auditorium sizes have decreased with the shift to the multiplex and megaplex, the more relevant (if harder to assemble) measure would be the number of seats. How does this seat-versus-screen perspective affect our perception of the observed trends? Is a similar trend at work in European exhibition? While admittedly harder to answer with readily gathered data, these questions seem fundamental to understanding this aspect of the sector.

The authors touch upon the potential importance of "buzz," and theatrical distribution indeed offers rich opportunities to study information dynamics and advertising. Both opportunities stem from the typically short theatrical lifespans of movies. Consumer opinions about movies can presumably be inferred from how movies perform compared to prerelease expectations. Moul (2006) implements this intuition with a parsimonious model and shows that word of mouth explains about 25% of the variation and 33% of the serial correlation in the unobserved component of demand. Likewise, the extent of advertising variation over a single movie's theatrical life conceivably allows the identification of advertising's impact on demand that usually requires consumer-level data. Given the ever-changing set of available movies, the industry (as the authors state) appears to be an ideal context in which to consider these and other issues of informational economics.

In the longer run, it seems that file sharing and piracy will force radical changes in the industry. Blackburn (2005) supports this relatively bleak assessment. Using clear events in the Napster litigation history (e.g., the announcement of lawsuits against users and the subsequent revelation that only high users would be targeted) to identify the true impact of file sharing on album sales, Blackburn (2005) finds strong evidence of file sharing's deleterious effects on well-known artists. Blackburn (2005) also shows that estimating these effects without allowing for differing impacts between unknown and well-known artists biases estimates toward the conclusion of minimizing the impact of file sharing, explaining the findings of Oberholzer-Gee and Strumpf (2005) cited by the

Although invited commentaries are not formally peer-reviewed and represent the opinion of the author, authors were carefully chosen based on their outstanding expertise in the areas of thier respective commentaries.

authors. These results suggest that once broadband becomes sufficiently widespread, digital replication for home viewing will upend the industry's current business model of depending so crucially on video rentals and sales. History also suggests that technological measures to counter piracy will at most slow the erosion.

The most obvious implication of widespread replication is that video revenues to distributors/studios will decline in importance relative to domestic and foreign theatrical rentals. This should cause resources to be shifted from the replicable to the nonreplicable medium; namely, toward theatrical exhibition. Again, the music industry offers a parallel. Mortimer and Sorensen (2005) document evidence consistent with a comparable shift from albums to performances over time, as bands increasingly use their tours not to promote album sales, but as independent revenue generators. Increased resources to theaters will presumably accelerate the ongoing trends of theaters differentiating themselves from the home-viewing experience, a direction pointed out by the authors.

It is doubtful that things will stop there. The heightened importance of the theatrical window to the distributor will force many of the inefficiencies detailed by the authors from the distributor-exhibitor relationship. At a minimum, the contractual rigidities regarding exhibitor pricing will be relaxed, allowing for greater capture of the consumer's surplus by theaters and distributors. It is because of this greater need for efficiency that I am more optimistic than the authors about the prospect for cooperation between distributors and exhibitors and the consequent time line for widespread adoption of digital projection. The preeminence of exhibition also seems likely to increase the bargaining strength of theaters vis-à-vis distributors.

These shocks to the revenue stream will inevitably feed back to production. It seems likely that the growth in movie costs will slow and perhaps even reverse, though such an occurrence is unlikely to affect studios' relative emphasis on blockbusters. Indeed, the loss of a lucrative video market would seem to favor the production of event movies that "have to be seen on the big screen" as well as movies that translate well to foreign audiences (e.g., action movies). Consequently, ongoing trends in production will only accelerate as file sharing becomes more pervasive. The broader impacts of digital technology on the production side are less clear, but it seems reasonable to suspect that the market for nonevent movies will increasingly resemble those for publishing and music.

These comments then reinforce the authors' original choice of emphasizing theatrical exhibition. While timing is a notorious weakness in economic analysis, the authors' questions and my own should provide thoughts for research for the foreseeable future.

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