The Drivers of Hollywood's Competitive Advantage

3.1 The Economic Drivers of Hollywood's Global Competitive Advantage

From an industrial economics standpoint, Hollywood's drivers of the current worldwide competitive advantage can be explained utilizing Porter's theoretical framework of the "national diamond" (Porter 1990). This theoretical framework explicates competitive landscapes and markets where an intense competition appears to be a positive factor in determining competitive advantage, especially if the competitors share geographical proximity. Under this framework, four conditions, the "determinants of national advantage" (p. 71), have to be considered, jointly and severally: factor conditions, demand conditions, strategy/structure/rivalry conditions, and relating/supporting industry conditions.

The combination of these elements contributes to the competitive advantage and generates a virtuous cycle where each element helps build and maintain the leadership of the industry *vis-à-vis* external competitive factors and entities. Other examples of these clusters of industries, geographically situated with global competitive advantages, are the Japanese consumer electronics industry and the Italian fashion industry. Similarly to Hollywood's strategy, these clusters, although geographically situated in specific regions where they can benefit from "national diamond" conditions, operate globally taking advantage of opportunity arising in different parts of the globe.

3.1.1 Factor Conditions

For the US entertainment industry geographically concentrated in Southern California, factor conditions refer to the existing established presence in the region of specific skilled labor, ranging from the "below the line" crews to the "above the line" talent operating in the industry, comprising veteran professionals in the different activities needed in the creation, production, and distribution of entertainment. It also includes the role of prominent film schools, such as the ones at the University of Southern California (USC) and the University of California at Los Angeles (UCLA), and the American Film Institute (AFI). These institutions located in the region contribute to Hollywood's leadership as they attract individuals with potential talent from all over the world, providing them with state of the art training and ultimately facilitating their entry into the industry. In addition, the mild and sunny climate of Southern California with its diverse landscape, ranging from deserts to mountains, valleys, and the Pacific Ocean, allows diverse outdoor scenes all year round. This element is considered one of the main drivers of the original moves from the East coast of the United States to the region for the producers/distributors which eventually formed Hollywood in the early twentieth century.

3.1.2 Relating and Supporting Industries

Relating and supporting industries conditions refer to the existence of specific industries, also geographically concentrated in Southern California, whose know-how help develop the industry's competitive advantage. They are an integral part of the Hollywood system as previously defined: They are the talent agencies, the music and recording industries, the trade industry press and specialized research firms, and the entities comprising the creative community and the industry labor. Over time Hollywood studios have built long-term, established relations with all these entities, to the point where there seems to be a phenomenon of a certain degree of osmosis among different players operating in the entertainment industry in Southern California. It is not infrequent that talent agents become studios executives and vice versa, tightening the different professional backgrounds in the industry and the consequent relations. This complex system, with an impressive level of industry know-how and talent developed over decades, is hardly replicable anywhere else in the world. The existence of this phenomenon in and of itself helps build and maintain the global competitive advantage of the Hollywood system as a whole.

3.1.3 *Strategy, Structure, and Rivalry*

Strategy, structure, and rivalry conditions refer to the specific elements constituting the cluster of the US entertainment industry. These conditions of the cluster underline the competitive landscape of the US entertainment industry, analyzed previously in the chapter. Historically, as described by Gabler (1988), Hollywood studios have fiercely competed and rivaled one another on certain aspects of the business. At the same time, however, their competition did not constitute a destructive factor for the industry as a whole, as the major players would agree on key issues regarding the industry, such as the production codes, rating systems, and generally how the

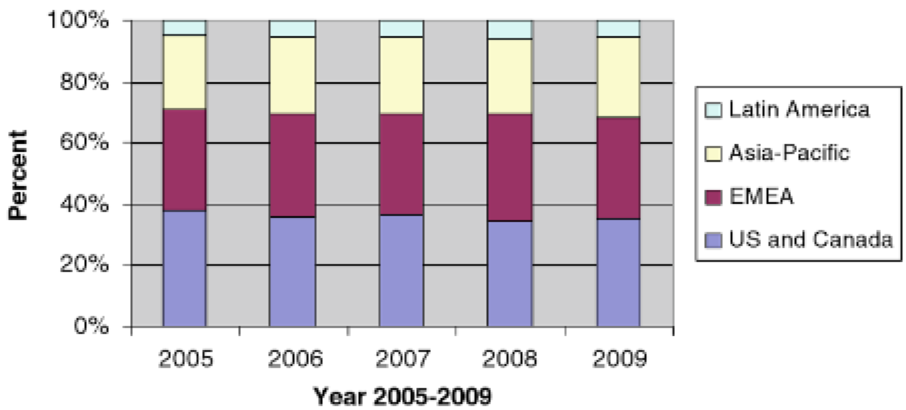

Fig. 3.1 International theatrical market 2005–2009. Source: MPAA (2011)

industry would operate and evaluate itself through entities like the MPAA and the Academy of Motion Picture Arts and Science (AMPAS), awarding the Oscars for excellence in the different facets of the creation of motion pictures.

As a result, this particular kind of competition has been producing a global competitive advantage for the industry players, as opposed to "zero sum game" of other industries, where the competitive strategies of the industry players contribute to undermine the very existence of the industry itself by attempting to eliminate key players of the industry or undermine their long-term prosperity. Historically, the studios have prospered in the second half of the twentieth century expanding on the one hand the global market for their entertainment products, while at the same competing to increase their individual market share.

3.1.4 Demand Conditions

Demand conditions refer to the size of the accessible domestic market available for the industry's products. For the Hollywood studios it represents the demand for entertainment generated within the United States by customers willing and able to pay for media entertainment. The US domestic market (including Canada) is by far the largest in the world in economic terms, with on average more than 1.4 billion tickets sold per year and approximately US $9B generated at the box office per year in the period 2000–2009 from the theatrical release of feature-length motion pictures alone (MPAA 2010, pp. 5–6).

In general, as shown in Fig. 3.1 for the period 2005–2009, in the worldwide theatrical market the United States represents the most significant revenue stream, followed by the EMEA region (Europe, Middle East and Africa). The evolution over time of revenues stemming from the other markets shows an evolving landscape. The percentage coming from the Asia-Pacific region has been increasing in the recent years (and it is estimated to increase further, as the huge markets of the People's Republic of China and India, with combined populations exceeding 2 billion individuals are slowly opening up to foreign-produced entertainment content). In contrast, Latin America represents a smaller percentage of the international theatrical market in economic terms.

The most relevant market in terms of gross box office receipts (not in terms of admission tickets sold, however) is the US domestic market, and has been so in the past decades. This market has been clearly dominated by the oligopoly comprising the Hollywood studios (as shown in Fig. 3.2). Each studio has been providing over time a consistently successful offer to American movie goers, generating a diversified portfolio of feature-length motion pictures on an annual basis, where the loss of one product is compensated by success of another.

In the period 2003–2010, Hollywood studios and other entities affiliated with them consistently exceeded 80% of the American domestic theatrical market. As a result, they can fund expensive projects, having the domestic market as the first target for recouping their investment. When they then compete internationally, very few other entities, if any, can afford similar budgets for entertainment products, due to the limited size of their domestic markets compared to the US domestic one. As a result, Hollywood products have high production value compared to other international entities, which cannot tap into entertainment markets with similar dimensions.

This phenomenon helps create a virtuous cycle, where Hollywood's artifacts have a higher production value since they have access to a large domestic market. This element increases their competitive advantage internationally increasing their global market share, which in turn further increases their competitive advantage. As a result of this international market dynamic, Hollywood studios have successful access to global markets and they can increase their investments in entertainment.

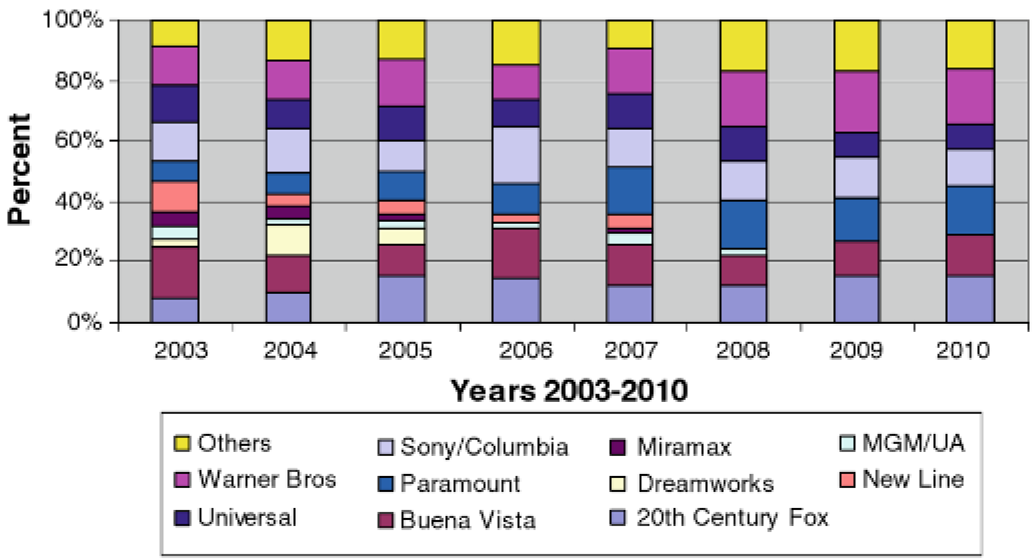

Fig. 3.2 US domestic box-office 2003–2010. Source: Boxofficemojo (2011)

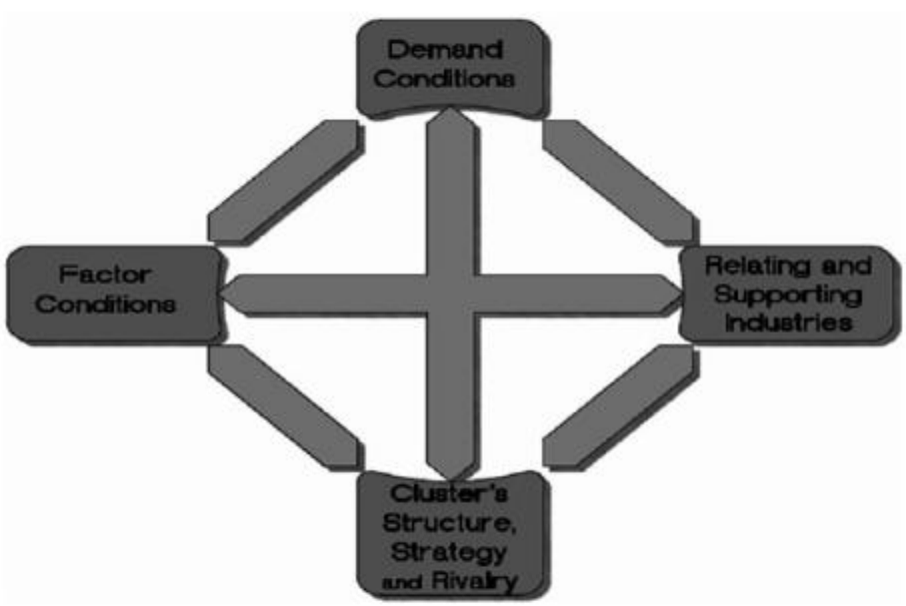

Fig. 3.3 US entertainment market dynamics and competitive advantage: The "national diamond" (Porter 1990)

The end result of this mechanism is that Hollywood studios can afford to fund even larger projects, whose investment can be recouped internationally. The increased size of the investment raises the economic barriers for potential new entrants in the industry, which are already significant, as shown in the previous analysis of the "five forces," making it extremely risky and difficult for foreign entities to compete at a global level. All these conditions operate to generate and maintain the global competitive advantage of the US entertainment industry, as shown in Fig. 3.3, where the "national diamond" is represented with its four determinants.

This "diamond" is a "mutually reinforcing system" (Porter 1990, p. 72) where the different determinants, generated by diverse entities, work together in synergy to create and sustain the global competitive advantage of the specific industry cluster. Porter also points out that, in general, other elements have to be factored in when analyzing the competitive advantages of specific industry clusters: chance and governments. Historically, events out of the control of the entities operating in the industry have conditioned the path of the industry itself stemming out of uncontrollable or unpredictable sources.

In addition, the governments of nation states still play a role in the diffusion of the flow of international entertainment, as national sovereignty remains through rules and regulations. In the age of globalization of markets driven by transnational corporations and international financial institutions, states still matter, as they ultimately "hold the power to pass legislation that affects domestic media industries" (Waisbord and Morris 2001, p. xi). Specifically, cultural policies can be enacted to protect indigenous media producers, through the imposition of "domestic content" quotas in different media, ranging from movie theaters to the different TV platforms, in order to develop the local cultural industries (as in the case of Brazil, Mexico, the EU for example).

There can be also attempts to close off international entertainment flows altogether (as in the case of Iran and the People's Republic of China for example). Generally, international trade policies are developed to promote cultural export of domestic products internationally (vs. trade liberalization) through fiscal incentives or financial support to stimulate or facilitate the production and distribution of entertainment, directly or indirectly (Gerse 2004). Domestic barriers created by local governments can therefore alter the flow of entertainment content from the large US market to small local markets internationally (Wildman 1995). Overall then, the combined action of the "diamond's" determinants plus the roles of chance and government, utilizing this theoretical framework, play a pivotal role in explicating the current and longstanding leadership of Hollywood in the global entertainment landscape.

3.3 The Potential Threats to Hollywood's Global Primacy in an Evolving Landscape

As Hollywood studios have long discovered, they do not operate and compete solely in the movie business, but in the larger entertainment business. When in the 1950s, the new medium of TV disrupted the media and entertainment landscape, focusing only on the movie side of the business represented a "marketing myopia" (Levitt 1975) for the Hollywood studios, as the industry and the competitive landscape had to be considered as a whole. The Hollywood studios initially missed the opportunity to expand their business by being too product-oriented (and considering themselves only as movies makers) as opposed to customer-oriented (and therefore position themselves as entertainment providers).

As a result, Hollywood studios have been diversifying their investments in the entertainment industry since then, establishing a significant presence in the TV business in addition to their original core business: movies. Also, the international dimension of the entertainment business has been a key element in establishing and maintaining Hollywood studios' leadership, as the revenue streams generated by foreign markets are oftentimes essential to recoup the original investment to create and produce content domestically.

Historically, they have successfully adapted to the evolving global landscape, able to incorporate the new entertainment phenomena, as they arose, in new revenue streams, both in the creation and the distribution sides of the business. Similarly to the exploitation of entertainment content in the different "windows" of exhibition in the entertainment business, the Hollywood studios are organized to better capture the value created in the entertainment landscape and to effectively compete globally. As a result, they operate with different divisions, ranging from theatrical, television, home entertainment, animation, digital distribution, and ancillary revenues, including licensing to consumer products distributors, domestically and internationally.

At the turn of the twenty-first century, however, they face new challenges with the potential of altering the existing status quo, and specifically the global primacy of the Hollywood system, whose center lies in the oligopoly comprising the studios. On the one hand, the rise of non-scripted entertainment in prime time schedules of broadcasters around the world has introduced new competitive entities in the global arena, with specific competences and know-how. On the other the ICT revolution, as it unfolds, is revealing its potentially disruptive force on the existing business practices in the creation and distribution of entertainment.

Moreover, in the consumption of entertainment content, audiences also appear to be willing to have a say in its outcome. As shown in "reality TV" show votes, audiences appear to want to determine the outcome or modify existing content (through the

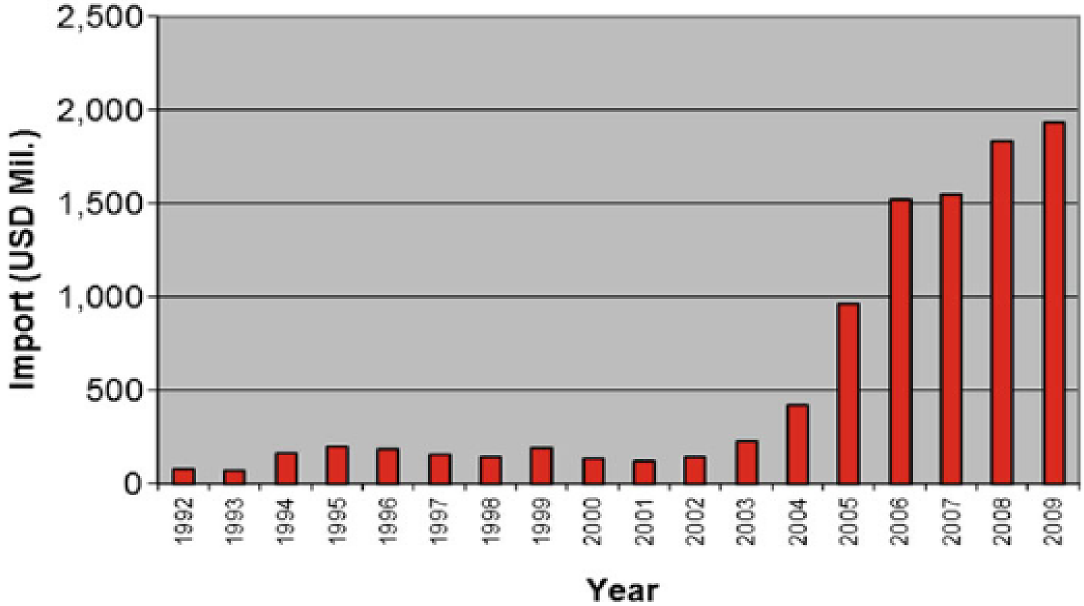

Fig. 3.4 USA film and television tape rentals – Import 1992–2009. Source: Bureau of Economic Analysis (2011)

processes of remixing, YouTube videos and adaptations for example) or to plainly interact as they appropriate the entertainment content (as in video games). As a result, the combined action of these elements is affecting the entertainment landscape, with non-scripted entertainment appearing to lend itself to the digital landscape better than traditional scripted entertainment.

There are signs of changes occurring in the US market. According to the US Department of Commerce's Bureau of Economic Analysis (Koncz and Flatness 2007, p. 115), while receipts for film and television rentals generated from export still vastly exceed those generated from import, the latter have registered a much more significant increase in recent years. Figure 3.4 illustrates in particular that the import for the category has increased from US $76M in 1992 to US $1.9B in 2009. This shows that while the imbalance between US import and export for popular culture goods still remains, there are signs of contra-flows of entertainment in a more dynamic landscape (Thussu 2007). It is worth pointing out that the significant increase of imports commenced to take place in the year 2003, and it appears to be continuing to unfold at the time of this writing.

In an evolving global entertainment landscape, new entities, mainly from Europe, as Endemol and FremantleMedia are successfully competing with Hollywood studios worldwide in providing prime time TV content to broadcasters, mainly non-scripted entertainment, as "reality TV" shows and game shows. These entities have been able to compete and make inroads also outside their original domestic markets, and specifically, to establish a significant presence in the United States, the largest entertainment market in the world, with all the existing barriers to entry notwithstanding.

The rise of the new wave of non-scripted entertainment and of the European entities leaders in producing and distributing the genre has enormous implications above and beyond the flow of entertainment content within the Atlantic corridor between Europe and the United States. One of the determinants of Hollywood's global competitive advantage in the "national diamond" framework analyzed in this chapter (the demand conditions) is being challenged by these European entities, able with this genre to successfully penetrate the American TV entertainment market. In so doing, they can effectively hamper the virtuous cycle originated by Hollywood's predominance in its domestic, and world's largest, market.

Furthermore, the genre has successfully reached all the relevant domestic markets worldwide, introduced in the different territories with local adaptations of global formats. It is worth noticing that the revenue streams generated from television represent a significant aspect of the leading media and entertainment conglomerates' operations. Analyzing the "sultans of the small screens" (the diversified conglomerates Time Warner, Viacom, Walt Disney and News Corp.), Thussu (2006, p. 16) points out for example that the percentage of total revenue generated by TV in 2004 ranged from 39 to 67%.

As television is a relevant feature of the entertainment landscape, the global success of the aforementioned non-US entities has the potential to challenge Hollywood studios' global leadership by competing in the increasingly relevant genre of non-scripted entertainment, both in the United States and internationally. Non-scripted entertainment appears to lend itself to local adaptations better than scripted entertainment by proposing a global format to local culturally situated audiences around the globe with local hosts, contestants, and situations, in a way not possible for example for TV comedies or drama series. Also, it can be argued, the narrative transparency is higher in non-scripted entertainment, as local audiences oftentimes are not even aware that these programs have been ideated elsewhere, rather they believe to be watching local fare.

As a result, many of the elements utilized to explicate Hollywood's global leadership with the previous interdisciplinary analysis, as narrative transparency, are clearly present on an even bigger scale in the local distribution of non-scripted entertainment global formats. In addition, cultural proximity, if not even national pride, can be triggered by these shows whose local adaptation are so central in the development of the program that they appear to be completely generated locally, as in the case for example of the currently most successful show in the US TV landscape, *American Idol*, which is a local adaptation of the global format *Pop Idol*, generated originally by FremantleMedia in the United Kingdom.

The specific rise of non-scripted entertainment has then to be analyzed, with specific emphasis on the aforementioned European entities, their background and business practices, and the overall differences with scripted entertainment generated in the Hollywood system both in the creation and distribution processes and Hollywood's reaction to the phenomenon. This analysis enables the study to explore an emerging institutional trajectory challenging Hollywood's global predominance: the rise of non-scripted entertainment global leaders. These entities, mainly from Europe, have successfully made inroads in the US prime time schedules, somewhat reversing the