IBEF
INDIA BRAND EQUITY FOUNDATION
www.ibef.org

IBEF INSIGHT

CORPORATISATION OF INDIAN FILM INDUSTRY

A REPORT ON THE PROGRESS OF THE INDIAN FILM INDUSTRY AND THE IMPACT OF CORPORATISATION

NOVEMBER 2013

INDIA BRAND EQUITY FOUNDATION
www.ibef.org

CONTENTS

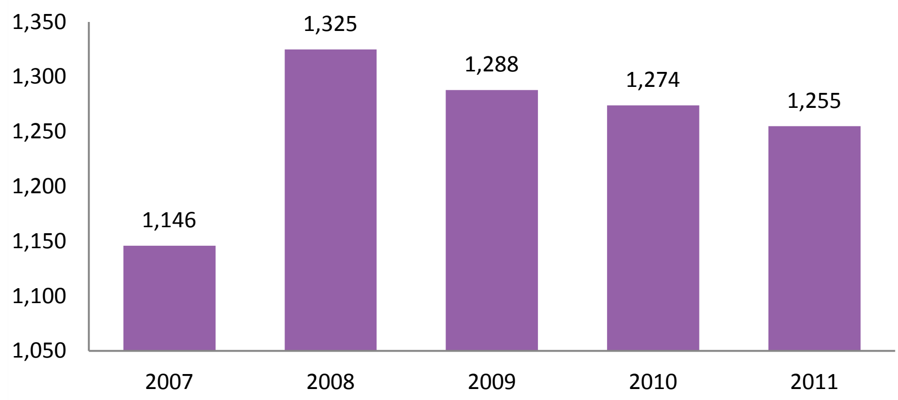
CORPORATISATION OF INDIAN FILM INDUSTRY

A REPORT ON THE PROGRESS OF THE INDIAN FILM INDUSTRY AND THE IMPACT OF CORPORATISATION

1. INTRODUCTION

In 2013, the Indian film industry completes 100 years of film production and exhibition as an industry. From the days of the 1900s of black-and-white and silent movies, where a small group managed the entire process of film making, acting and exhibiting, the industry has come a long way. Today, it is a highly evolved and professionalised industry with multiple players offering specialised services in different areas of film making – from script writing, casting, recruiting technicians, sourcing technology and equipment to editing and post-production activities, marketing, distributing films and exhibiting on theatres, multiplexes and internet. As expected in 100 years, Indian cinema-makers have undergone a steady learning curve to arrive at the present status of an industry that is recognised world-wide. Today, it is well known that the Indian film industry is the largest in the world in terms of number of films produced and released in a year, with 1,255 films produced and released in 2011.

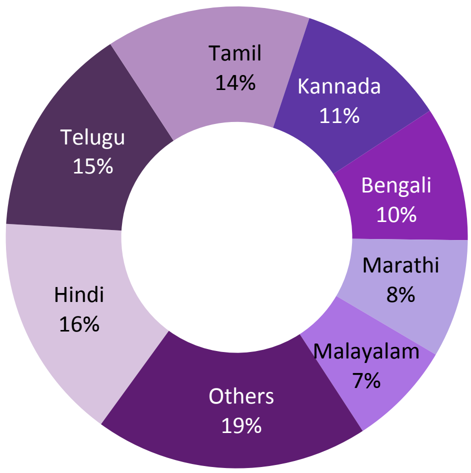
Figure 1
Films produced in India (no)



Source: Central Board of Film Certification, India; IMaCS analysis

In the early years, the industry was dominated by producers and studios of Bombay and Chennai. Since the 1950s, it has spread across several regions of the country; with movies being produced in Hindi, Tamil, Telugu, Bengali, Assamese, Kannada, Oriya, Punjabi, Marathi, Malayalam and several other regional languages. Although Hindi films dominate mainstream cinema in India, popularity of films in regional languages has also been growing both within and outside the country. In fact, the south-Indian-film industry, which comprises Tamil, Telugu, Kannada and Malayalam; accounts for around 47 per cent of the total number of films released in India.

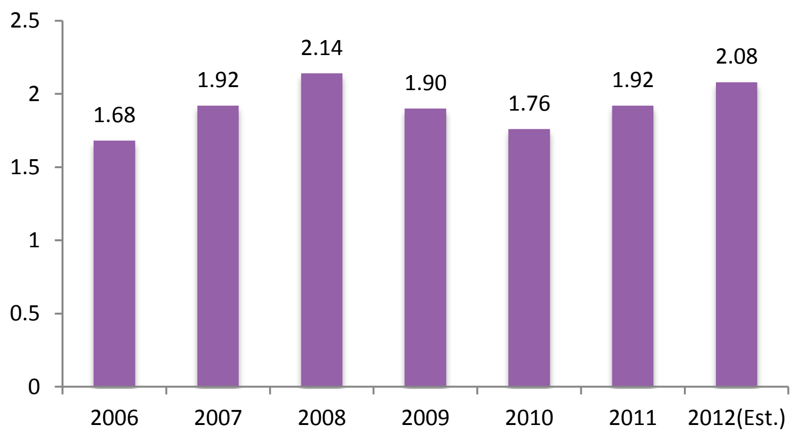
Figure 2
Language-wise distribution of films released in India



Source: Central Board of Film Certification, India, 2011

In terms of revenue, the industry has grown at a rate of 2.6 per cent per annum from US$ 1.7 billion in 2006 to US$ 1.9 billion in 2011. After the slowdown post-2008, the industry's revenue growth has picked up since 2010. Total revenue growth was 9 per cent in 2011 over 2010.

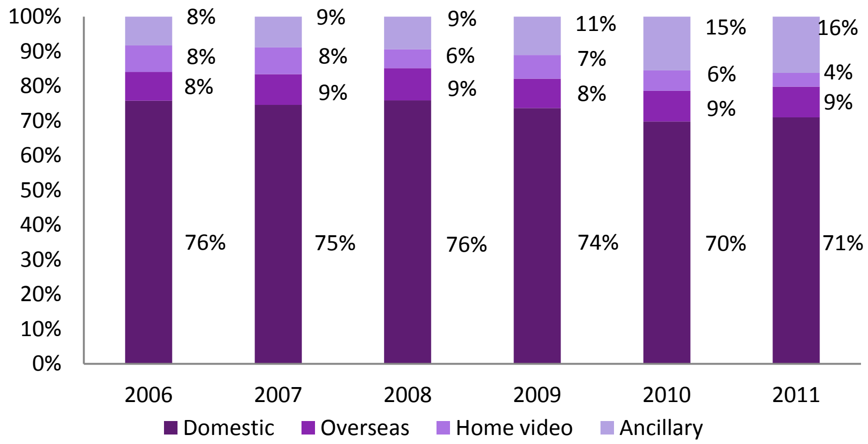
Figure 3
Total revenues of Indian film industry (US$ billion)



Source: India Entertainment and Media Outlook, PwC; IMaCS analysis

Box office collections from the domestic market have the highest contribution to the total revenue. Apart from traditional box office collections, the other contributors to revenue growth today are domestic and overseas home video, as well as ancillary sources including cable and satellite broadcast and digital media. Contribution of ancillary revenue has almost doubled over the past five years.

Figure 4
Revenue contribution



Source: India Entertainment and Media Outlook, PwC; IMaCS analysis

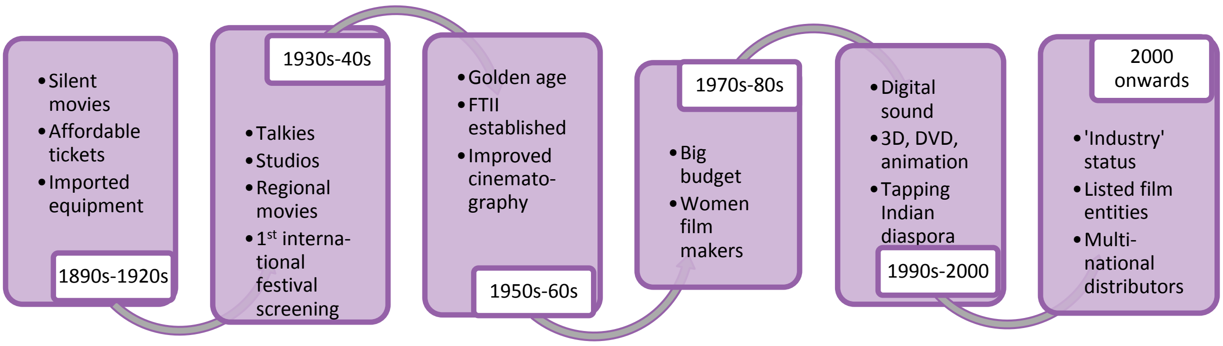
The industry is expected to grow at a rate of 9.1 per cent per annum from US$ 1.9 billion in 2011 to about US$ 3 billion in 2016. The increase in the number of multiplexes and average ticket prices will be the key growth drivers for revenue from the domestic market. However, the growth will also depend on the quality of content and the acceptance of viewers. Revenues from overseas markets are expected to grow further with the increasing demand of Indian films in other countries by the Indian diaspora, i e, non-residential Indians (NRIs) and persons of Indian origin (PIO). Ancillary revenues are also expected to increase.

2. PROGRESSION OF INDIAN FILM INDUSTRY

Beginning with the 1900s, the industry has moved through several stages of evolution in each decade thereafter. Moving pictures were introduced by the French in the late 1800s, when some documentaries were produced in India. The first full-length films were produced in the early 1900s up to the 1920s. These were mostly family managed and driven films – right from the cast to the production to the theatrical releases. This was the era of silent movies, 35 mm films, commercialisation with affordable ticketing and the prominence of Madras as the hub of movie-making. There were no sound-proof studios in those days.

Post 1920s and up to the 1940s, talkies and studios flourished after the release of the first movies with sound in the 1930s. Regional studios and films flourished; advanced sound technologies were introduced; multi-talented casts with the ability to act, sing, compose and produce were in vogue; and play-back singing was introduced.

Figure 5
Important developments in Indian film industry



Source: News reports; IMaCS Research

During the 1950s and 1960s, there was a proliferation of film makers. The south-Indian film industry had a major share of the overall market. New cinematographic techniques were introduced to display visual effects never seen before. Institutions were created such as the Film & Television Institute of India (FTII) for developing technical skills, the Film Finance Corporation for financing films and the Films Division. During this period, parallel cinema also found a space in the midst of mainstream movies. Film stars started gaining commercial importance over studios by the end of this period.

The 1970s and 1980s marked a period when big budget and multi-starrer movies dominated. 'Art films' or parallel cinema did find some audiences too. This period was also significant because of the advent of women producers and directors in the industry. The National Film Development Corporation was formed in 1975.

It was in the 1990s that technology up-gradation really started in the industry. Digital sound was introduced. Special effects were being perfected – 3D effects and electronic media were on the rise. The industry also started catching the attention of international audiences in the form of the Indian diaspora. This further led to an increased interest from the corporate sector in the industry.

Table 1
Studio system versus star system

Studio system • Film producers have adopted a factory-oriented approach for making a film because of the costs and complexities involved. Hollywood had adopted this approach in 1910s and the firms with production facilities were known as "studios". The Indian film industry, influenced by Hollywood since inception, also adopted the 'studio system' of film production in the 1900s. One of the first studios formed in India was *Kohinoor Film Company*, which was founded in 1918. In a few years, many studios were formed and the number of studios had increased to over 20 by the year 1921. • Studios comprised entire teams covering all aspects of filmmaking; including acting, technical expertise for post-production, marketing and distribution. This approach helped studios standardise their film making style, achieve cost efficiencies from economies of scale and develop their own brands in the film industry thorough consistent production. Under this system, all artists and technicians were employees of studios, who were either paid a salary or were contracted for the long-term. • Producers would get finances from film distributors with a guarantee of screening the film in cinemas for a certain period. Loans would be repaid in terms of box-office collections with no further liability of the film producer. Distributors would keep the profits earned from the film with no share for the film producer.
Star system • With the growing popularity of Indian films, the importance of films to viewers transformed into a "hero cult" phenomenon, which made film stars the objects of admiration and imitation. Gradually, fan clubs for film stars emerged and their idolisation reached incredible heights. Although the star system existed even during the silent film era, it gradually grew stronger than the studio system and eventually replaced it in 1960s. • Unlike the norm in the studio system, film actors did not have long term contractual obligations towards film studios in the star system. They operated as freelancers and were commanding professional fees based on the box office performance of each film. Successful actors got paid higher remunerations as compared to monthly salaries in the studio system. However, this increase in professional fees led to higher costs of film production. • Emergence of the star system increased the cost of production and changed the financing pattern of film production. Film distributors only paid 50 per cent of the total film cost, which forced film producers to look for other sources of finances. Promissory note system became the most prevalent source of financing. Producers would write an unconditional order to financers to pay the payee. • Other financiers came into prominence, including conventional money lenders who usually charged interest rates of up to 40 per cent per annum. The high cost of film production and these financing structures made film production a risky profession until the advent of corporate players in the industry.

Post-2000, the corporate sector has changed the way films are made, marketed and distributed globally. Professional service providers have replaced improvisers and developed offerings in areas such as editing, digitisation, archiving, animation and film making. Many production houses are listed on stock exchanges, thereby bringing in corporate governance into the industry.

3. CORPORATISATION OF INDIAN FILM INDUSTRY

In 2001, the Government of India granted "Industry" status to the Indian film industry. The government had established National Film Development Corporation Limited (NFDC) in 1975 to produce and co-produce films. However, institutional funding for the films increased after the grant of "industry" status in 2001, when the Reserve Bank of India (RBI) formulated guidelines for the banks for funding the film industry[1]. This facilitated the much needed institutional financing, which was earlier unavailable.

Under the 'star system', production of films was unorganised, which usually led to production delays and further increased the total cost of production. Securing finances to complete the film was tough, because film producers would usually get finance in parts. Disbursement of the next instalment of money was dependent on saleability of the film to financers. The time taken to secure money for completing the next part of the film usually led to delays in producing films. To avoid such concerns, film producers started looking for institutional funding, which was cheaper and more reliable as compared to other means of finances.

In order to get the funding, the industry had to adapt to new corporate governance requirements such as adherence to standard accounting practices, business plans, targets and time schedules and insurance as mandated by banks and financial institutions. Profitability and commercial success became essential, which required professionalism, efficiency in film making and adoption of market driven practices. It resulted in the entry of corporate entities in all sections of the film industry.

Deregulation of film screens also helped in the corporatisation of the Indian film industry. Earlier, setting up a new screen required many permits and most of the states had stringent procedures to follow. There was also price control on theatre ticketing. After deregulation, the number of film screens increased exponentially and ticket prices started being driven by market economics.

Deregulation of import control increased the industry's access to latest technologies from across the world and promoted digitalisation of film content. Digital films had wider reach as compared to the old analogue system. This led to higher revenue and profitability for films, which encouraged more participation from corporates in the film industry.

With better corporate governance practices, many international studios such as Walt Disney, Warner Bros. and Sony entered into collaborations with local production houses to produce and distribute movies. These collaborations have proved to be win-win situations for the collaborators, because international studios have gained distribution reach and domestic companies have utilised the latter's experience in project management. Also, Indian films can now be released globally, which has increased revenues for the Indian film industry.

Before corporatisation, there was a monopoly of big producers and stars in the industry. With institutional funding available at relatively lower interest rates, new and talented filmmakers can easily produce their films. Corporatisation of the film industry has also encouraged film producers to float new companies on stock markets.

[1]**Refer Annexure I**

Corporatisation also introduced several new measures to reduce uncertainty in revenues earned by a film. Corporates pre-license cable and satellite rights and distribution rights across geographies; which helps them to recover about 40-80 per cent of film production costs even before the film is released. Further, producers have developed new sources of revenue; including the sale of merchandise and partnering with companies to advertise their products in the film. Cost of film production has also been reduced by adopting measures such as revenue sharing with leading film actors.

Marketing of films has also transformed with corporatisation. While only 3-5 per cent of the total film budget was used for marketing a film in the earlier days, it is now as high as 40 per cent. The focus of marketing a film is to maximise the revenue earned by a film in the first week. Increasing use of technology has also helped and corporates have adapted to the latest channels of marketing available, including social media.

Corporate participation in the Indian film industry has increased in production, distribution and ownership of film screens. Revenues of corporates (whose financial numbers are available) involved in film production have increased at a rate of about 16 per cent per annum from US$ 679 million in 2008 to US$ 1.05 billion in 2011. Net revenues of corporates involved in distribution (whose financial numbers are available) have also increased at a rate of about 19 per cent per annum from US$ 3.35 billion in 2008 to US$ 5.58 billion in 2011.

Table 2
Total net revenues of listed companies (US$ billion)

		2008	2009	2010	2011	2012
Film production	No of companies*	85	73	78	82	57
	Net revenue	0.68	0.69	0.90	1.05	0.90
Film distribution	No of companies*	66	72	72	69	45
	Net revenue	3.31	3.99	4.60	5.57	4.44

Source: IMaCS Resources
***Number of companies for which financial results are available**

4. TECHNOLOGY DEVELOPMENTS AND INDUSTRY TRENDS

Corporatisation of the film industry and adoption of technologically advanced equipment and screening have gone hand in hand. In recent years, the Indian film industry has adopted latest technologies to improve visual and cinematic effects, which have resulted in a better viewing experience for consumers. Increasing use of technologies including digitalisation of film content and 3D films has also helped the industry to increase revenues and reduce cost of distribution.

Increasing numbers of 3D films and theatres: Although the first 3D film was released in India in 1984, the number of 3D films in India has increased significantly after the success of the Hollywood movie "Avatar". Since then, the industry is looking proactively to enhance the viewing experience of consumers by using 3D technology and hence increase the viewership. Multiplexes are also willing to invest large amounts for 3D screens to meet the increasing demand for 3D films. According to estimates, about

US$ 20,000 is required to convert a 2D screen into a 3D screen. Average ticket prices for 3D films are higher as compared to 2D films; hence generating more revenues, despite lesser number of tickets being sold. 3D films usually generate about two-three times the revenue as compared to 2D films, which makes the investment well worth it.

Digital screens: With the increasing numbers of 3D films, the number of digital screens has increased, since it is easier to convert a digital screen to a 3D screen. A majority of new multiplexes have digital screens with 3D capabilities. According to estimates, India has over 5,000 digital screens as on date. Digitisation of Indian films will also increase the consumption of movie content by enhancing the viewing experience. Also, users cannot rent or share digital content, thereby curbing the menace of movie piracy. Digitisation has reduced the cost of operations, because content is easier to store and deliver to screens. Digital content can easily be distributed to the screens via satellites.

The Indian film industry has witnessed rapid digitisation of cinema screens over the past few years. This has lowered the acquisition costs for the print of a film to US$ 360 from US$ 1,200 under the old analogue system. Small budget films, which were unable to have a wider release because of high print costs, can now release in large numbers through the digital format; potentially earning higher revenue collections. This has also enabled companies to simultaneously release their movies at the global level. According to industry estimates, around 70 per cent of the screens in India are already digitised. With film producers increasingly making and selling movies in the digital format, there will be no option left with theatre owners but to go digital in the future. Digitisation will also help increase the revenues from cinema advertising, because of the low costs involved in distributing advertisements.

Advent of multiplexes: The advent of multiplexes in India has significantly contributed to the growth of the Indian film industry and helped in its corporatisation. The culture of multiplexes has improved the overall movie-going experience of audiences. Big budget movies, which had to be content with about 500 prints earlier, can now release with 1,500 prints. This has helped them reach a wider audience as well as collect more than 50 per cent of the total revenues in the first week itself.

There are just 10 screens per million in India as against the global average of 54 and 120 in the US. This highlights tremendous opportunity for the Indian film industry, which multiplex owners are gearing up to seize. According to the Multiplex Association of India, Indian had around 1,000 screens in 2012. The number is expected to increase to 1,400 by the end of 2013. New players such as Cinepolis have entered the market and have lined up huge investments for future expansion.

Availability of food and beverages has helped multiplexes to maintain double digit growth for the past 2-3 years. Growth of multiplexes in the coming years will also be significantly driven by growth in the number of malls. Multiplexes are an integral part of malls today and both share a symbiotic relationship with each other. With the retail industry reviving after the slowdown, growth in the number of malls, and thus, multiplexes, is inevitable. This is ideal for both industries as malls get higher footfalls because of multiplexes and multiplexes get the benefit of initial cost reduction because of a revenue sharing mechanism with malls.

Growth of small-budget films: Small-budget films are beginning to create a place for themselves in the Indian film industry. These films are mainly content and performance driven rather than led by 'star' actors who drive big-budget films. They have tight marketing budgets and depend heavily on word of mouth publicity for their success. Some films have recovered their production costs from the sale of TV rights. This has helped good scripts to generate sufficient funding for their future projects. The advent of multiplexes has further helped their cause, as niche viewers are always interested in such films.

The pay-per-view market: The pay-per-view (PPV) market is an emerging source of revenue for the Indian film industry. Growth in PPV market in India has a high correlation with growth in the direct-to-home (DTH) segment. DTH service providers have reduced prices of PPV films and brought them in the price range of US$ 0.5-1.0. With all four metros and many others cities moving towards digitisation, the demand for PPV films is expected to increase. This will lead to increased competition for acquiring movie rights and a new revenue stream for film producers.

Resurgence of regional cinema: While Hindi films continue to dominate the Indian film industry, there has been a resurgence of regional movies over the past five years. This area is mainly dominated by south-Indian films, with films in Marathi, Punjabi, Bhojpuri and Bengali languages also playing their part. Regional films cater to the tastes of local audiences and penetrate deeper into rural areas. Leading production houses in India have realised the potential of regional films and are increasing their presence in important regional markets. Large players like UTV, Reliance Media Works, Eros, etc., have entered the south Indian film market to tap the tremendous potential of these markets.

Studios are also releasing popular films dubbed in different regional languages to reach a wider audience and generate higher revenues. Their strategy has been validated by the tremendous successes of some of the regional movies in the last three years. The box office collections of these movies have also overtaken some popular Hindi films. Emergence of regional cinema has helped production houses restructure their portfolios, moving away from a dominantly Bollywood-dependent model to a more balanced one.

Increasing market for Hollywood films: Viewership of Hollywood movies is on the rise in India. Hollywood production houses have increased their focus on the Indian market because of growing revenues from their releases in India. With greater collaborations and digitisation of cinema, foreign production houses have also been able to release movies globally at same time. Hollywood studios are also making an effort to release movies in different regional languages in India to tap the huge market available.

Growth of visual effects (VFX) industry: The visual effects (VFX) industry is a rapidly growing segment in India. With the increase in domestic demand from high-budget movies and outsourcing of work to India from international clients on the rise, the future of the industry looks very promising. Industry players have been gradually trying to shift from low-end work towards higher-end assignments through collaboration with film and entertainment companies. Domestic players are increasingly setting up offices abroad for better service to the clients. India currently accounts for around 10 per cent of the total animation and VFX outsourcing market. By focusing on key areas such as improving the skill sets of artists and increasing salaries to attract better talent, there is enough room for significant growth in future.

5. CONCLUSION

Corporatisation has transformed Indian film industry and certainly catalysed its growth post-2000. It has facilitated the much needed flow of institutional finance to the industry, which is reliable and is available at lower interest rates compared to other sources of financing. It has also led to the adaptation of better corporate governance practices; including adherence to standard accounting practices, business plans, targets and time schedules. After the entry of corporate sector, the film industry has adopted market-driven practices, which have resulted in greater efficiency in film production and lesser delays. Furthermore, it also prompted international studios to enter into collaborations with Indian production houses to produce and distribute movies.

Corporatisation of the industry has also transformed marketing of films in India, with marketing expenses increasing from 3-5 per cent of total budget to about 40 per cent. With the advent of digitisation, the playing field has levelled somewhat, as even small budget film makers can have far wider releases without a huge cost burden. Several new sources of income generation have come up; such as pre-licencing of cable and satellite rights, sale of merchandise and distribution rights. This has resulted in a decrease in dependence on just ticketing revenues, hence improving the risk profile of producers. Further, it has encouraged new and talented filmmakers to produce films with original ideas. With funding available at lower interest rates, filmmakers have started experimenting on new genres of films and small-budget projects with innovative storylines that cater, in particular, to niche segments of film viewers. International reach of Indian films is another offshoot of corporatisation and a new approach towards marketing strategies. Overall, the industry had become more diverse and competitive.

6. ANNEXURE I: BANK FINANCE FOR FILM INDUSTRY – RBI GUIDELINES

Eligibility

Banks may provide finance to film producers (corporate as well as non-corporate entities) with a good track record in the relative field. Banks may also provide finance to these entities for production of films in participation with the National Film Development Corporation.

Direct finance for film production

Criteria for financing

- Banks may obtain from the producers a detailed budget for each film, clearly indicating the entire cost estimates for the film and the means of financing it. Ordinarily, producers are required to bring in at least 25 per cent of the project cost as promoters' contribution. Producers are also required to tie up advances from the distributors in the usual course as per usual practice (sales advances) to cover 35 to 40 per cent of the budget. Thus, bank advances could be for the balance requirement of 35 per cent to 40 per cent of the project cost. However, in deserving cases, where the banks are quite comfortable with the project as well as with the background of the producers, the financing could be increased to 50 per cent of the project cost on merit basis.
- Banks may provide finance to such projects, where the total cost of production of a film does not exceed Rs 10 crore. The amount sanctioned should be within the overall ceiling of the prudential

exposure norms prescribed by the Reserve Bank from time to time. Banks may also internally prescribe a suitable limit for their overall exposure to the film industry.

- The disbursement of bank loans should ordinarily start only after utilising the promoter's contribution and advance payments from the distributors. There may not, however, be any objection to the bank loan being disbursed side by side along with payments by distributors on a proportionate basis. The arrangement should be firmed up at the commencement of the project. However, in any case, banks may disburse the loan only after the promoter has brought in his contribution to the project.

Period of loan

The period of loan may be fixed based on the financing bank's assessment of the cash generation of the project.

Security

- Banks may obtain the laboratory letter, conveying rights on the negatives in favour of the lenders.
- The music audio/video rights, CD/DVD/internet rights, satellite rights, channel rights, export/international rights, etc. should also be assigned to the banks to serve as main security along with the negative rights in the form of lab letter, through appropriate documentation.
- Banks have first hypothecation charge on all the tangible and movable assets under the project.
- All agreements and intellectual property rights (IPRs) should be assigned in favour of the lenders. Lenders should have the right in negotiation of valuation of all IPRs.
- Collaterals, if necessary, may be obtained at the discretion of banks.

Insurance

The existing insurance products as acceptable to banks may be obtained from film producers.

Follow-up/monitoring

Banks should devise appropriate accounting and information/data submission formats for periodic flow of information from the producers. They should also obtain periodical progress reports, cash flow statements, audit reports and such other reports as are considered necessary. Banks may also consider appointing specialised agencies for monitoring the timely shooting/processing of the film and assessing the reasonableness of the expenditure.

Risk factors

Production completion risk is one of the major risks in any film production. To mitigate this risk, it would be necessary for banks to carefully appraise the projects having due regard to the track record of the producers as also the distributors. If necessary, banks may also engage industry specialists/consultants for evaluation of proposals. Insurance of risks, key personnel, etc. needs to be organised. Pending the development of appropriate risk insurance products, existing products such as equipment insurance, key personnel insurance, etc. could be availed of.

Finance through NFDC/to NFDC

Considering that appraisal of film projects requires special skills (which all banks may not be equipped with, at least in the initial years), banks may, at the request of the National Films Development Corporation (NFDC), also consider extending credit for production of films in participation with NFDC. This would be an additional channel for extending credit to the film industry. The detailed modalities in this regard (including security cover) may be worked out mutually by banks and NFDC.

DISCLAIMER