

China's cultural industry is booming thanks to the rapid rise in China's average national income, and the population's growing demand for cultural and entertainment products. . At the same time the governments in Chinese Mainland, Hong Kong and Taiwan are taking measures to boost the local cultural industry. The Plan for the Promotion of Cultural Industry passed by the State Council in 2009 defined the cultural industry as a national strategic industry. In Hong Kong, the cultural industry has been included among the six most competitive industries by the SAR government. The ambition of the government in Taiwan to transform itself into the center of cultural and creative industry in Asia Pacific region is similarly clearly indicated in the Plan to Develop the Cultural and Creative Industry. These have laid a foundation for further cooperation and development opportunities between the Chinese Mainland, Hong Kong and Taiwan.

Meet the Golden Age of the Entertainment Business

BY / William Chou and Iris Li

I. The cultural industry in the Chinese Mainland, Hong Kong and Taiwan Meet the Golden Age of Entertainment Business.

Deloitte's survey on the segmented cultural markets found that movie and television, computer gaming and advertising industries have been growing fast in all three regions and the cultural industry as a whole is showing an upward trend in the Chinese Mainland (see Figure 1). The cultural markets in both Hong Kong and Taiwan have resumed growth fuelled by the recovering economy. Hong Kong and Taiwan are expected to maintain a steady growth in culture-related consumption as both passed the USD 12,500 per capita GDP threshold some time ago and are defined as high-income economies with a high level of cultural consumption. Their influence is expected to continue radiating to their surrounding markets. Both are targeting to export their cultural products to the Mainland as one of the promising markets in the future.

In this respect, a significant turning point in the transformation of the consumption structure was reached when the per capita GDP in the Chinese Mainland approached USD 6,100 in 2012. Per capita GDP of USD 4,000 or above has been noted in more developed markets as a trigger indicator for a jump in culture-related consumption. A significant shortage in the supply of cultural products in the Chinese Mainland marketplace signals the next ten years will be a booming time for the cultural industry in the Chinese Mainland.

Figure 1 A comparison of YOY growth in 2012 in the segmented cultural markets in the three regions

	Mainland	HK	TW
Publishing	14% growth in 2012	Export volume dropped 11% in 2012 11%	0.2% growth in 2012
Movie	30% box office growth in 2012	12% box office growth in 2012	25% box office growth in 2011
Gaming	22% growth in 2012	N/A	About 4% growth in 2012
Advertising	34% growth in 2011	16% growth in 2011	9% growth in 2011

Source: Deloitte Research

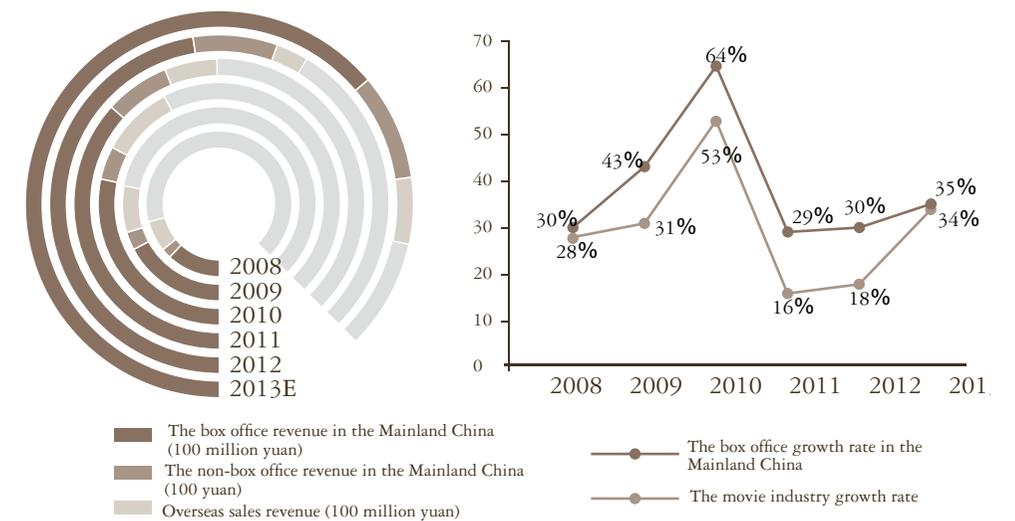
II. The current status of the movie and television industry in the Chinese Mainland

A. While the industry is expected to grow at a compound rate of 30% in the next five years, it still has a long way before it matures.

The Chinese Mainland market posted box office revenue of RMB 17.1 billion yuan (approximately USD 2.7 billion) in 2012, a 30% year on year growth (see Figure 2) which means it has replaced Japan as the second largest in the world. Nevertheless, this is still far behind the USD 10.8 billion box office in the US. According to the forecast by the Entgroup, box office revenue will reach RMB 23 billion yuan and the movie industry will expand its market to RMB 28.2 billion yuan in 2013, and the industry is expected to grow at a compound rate of over 30% in the next five years.

However, the current movie industry in the Chinese Mainland has not yet matured. Box office contribution to the total revenue of a movie is still increasing each year. By comparison, in more developed movie-making markets such as the US, box office, brand cooperation, movie copyright and derivative products each accounts for one third of the total profit. Box office revenue is more "one-off" reflecting but not fully tapping the popularity of the movie with movie goers. Expanded revenue streams including spin-off products such as games, books, audio and video, and theme toy figurines taps are characteristics of the commercial maturity of the movie industry. The fact that 80% of the size of China's movie industry is accounted for by box office receipts indicates that in China this is an industry that is far from maturity.

Figure 2 The size of the movie market and box office revenue in the Chinese Mainland from 2008 to 2013

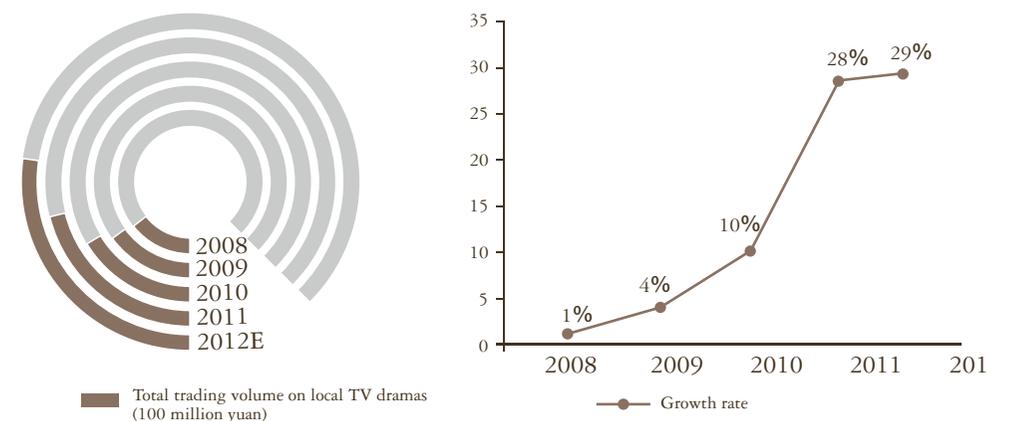


Source: Entgroup

The TV drama industry has been growing exponentially and signaling an imminent trend of M&A

Boosted by the continuous growth in the advertising revenue from TV media and an abrupt rise in new media led by video websites, the market for the trade of TV dramas is still red hot. The total revenue from the trade of TV dramas in the Chinese Mainland market increased from RMB 5.2 billion yuan in 2008 to about RMB 9.8 billion yuan in 2012 (see Figure 3), largely attributable to the increase in the running time of quality TV dramas and the hike in the average price.

Figure 3 Total trading volume on local TV dramas and growth rate



Source: Entgroup

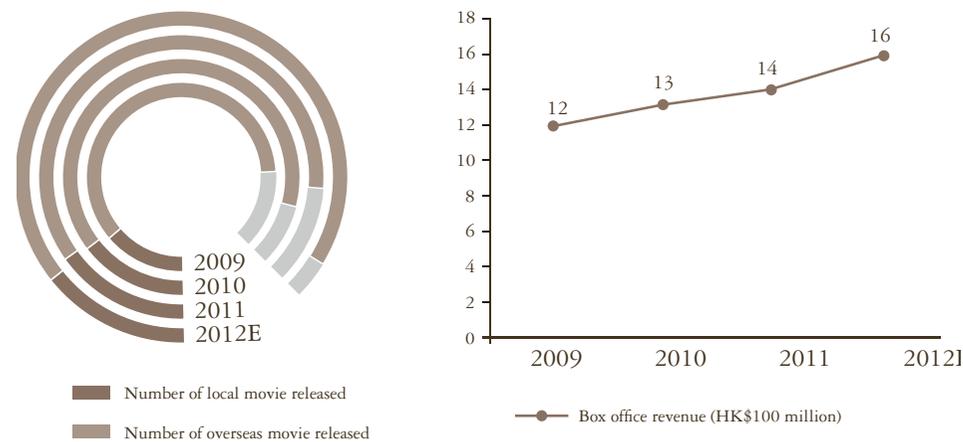
The lower degree of consolidation in the TV drama industry indicates that a large number of mergers and acquisitions will occur in the future. The private TV drama production organizations that currently rank at the top in the Chinese Mainland market include Hairun Movies & TV, Huayi Brothers, Huace Film & TV, New Culture Media Group, HBN etc. Smaller production organizations are at risk of being eliminated from likely future market consolidation by large companies with strong production ability, abundant resources and close ties with the big satellite TV companies. The “restriction on advertising” will accelerate this trend by forcing the satellite TV companies to spend more on purchasing quality TV dramas.

III. The current status of the movie and television market in Hong Kong

A. The steady growth in box office is accompanied by the drop in the share of local movies

Hong Kong is by far the leader in Asia in terms of per capita movie production. The data from MPIA in Hong Kong showed that in 2012 a total of 303 movies hit the screen in Hong Kong generating HK\$ 1.6 billion, an increase of 10% and 12% respectively from 2011 (see Figure 4). However, the number of overseas movies reached 250, a growth of about 14% from that of 2011, while the number of local movies was reduced to 53, representing a YOY drop by 5.4%. Due to the limited size of its local market, Hong Kong's local movies rely heavily on overseas markets, making Hong Kong one of the biggest movie exporters in the world.

Figure 4 The box office and number of movies released in Hong Kong



Source: MPIA Hong Kong, Government Statistics Department

B. Movie exports have been driven by Chinese Mainland and Hong Kong joint productions

With the shrinking of Hong Kong's movie industry and funding pressure, many of Hong Kong's movie directors and producers have resorted to CEPA's policies which aim to open markets between the Chinese Mainland and Hong Kong, and have gone north to seek development opportunities. A total of 37 sets of movies were jointly produced by the Chinese Mainland and Hong Kong, up 60% from the 23 sets in 2008 and accounting for over half of the annual movie production. In 2011, six out of the top ten selling Chinese language films in the Chinese Mainland market were joint productions of the Chinese Mainland and Hong Kong. Movies that have been difficult to recover the cost in Hong Kong have turned a profit in the Chinese Mainland, and the encouraging box office performance of the jointly produced films is attracting more movie production to migrate northward. The deep talent pool and numerous awards won by Hong Kong movie makers in the international movie business arena are appealing to overseas movie dealers. Furthermore, the growing movie market in the Chinese Mainland, fuelled by more frequent cooperation between the Chinese Mainland and Hong Kong, is expected to drive up movie production and the export of local movies in Hong Kong.

C. Fierce competition in the television industry and growing investment in content

Faced by intense competition in the television industry in Hong Kong, the ATV and TVB have undertaken to invest HK\$ 2.4 billion and 6.3 billion respectively to purchase and upgrade digital production and broadcasting equipment in the years of 2010-2015 to meet requirements in the production of HD TV programs. When it comes to the fee-based TV service market, PCCW made a capital investment of HK\$ 162 million in the television and content business in 2011, increasing by 26.6% on a year over year basis. In contrast to Cable TV Hong Kong which announced in its 2011 performance report that its capital investment was reduced from HK\$ 251 million in 2010 to HK\$ 199 million in 2011.

The plan to issue more free television program service licenses in the future by the Hong Kong SAR Government is likely to change the current situation in the television industry. The intensification of competition will require that HK produced movies emphasize both on exportability and marketability to create a commercially-oriented cycle. The returns will be fed-back in the production of TV programs to enhance the ability to locally produce movie and TV programs and increase TV stations' assets in movies and TV programs, building Hong Kong into an export-oriented creative production center with a wealth of movie and television talents.

IV. The current status in the movie and television market in Taiwan

A. The renaissance of local movies

The movie industry in Taiwan has been in sluggish since 2002 with the exception of a few master works. By contrast, Hollywood movies have enjoyed a higher level of acceptance (see Table 1). The sub-prime crisis that began in the US in 2007 has led to the shortage of funding for blockbuster movies in Hollywood that now have eroded appeal to the Taiwanese audience. This has provided an opportunity to the movie industry in Taiwan. Sensing the opportunity, the local government has placed the development of the cultural and creative industry at the top of its development strategy and has taken all possible measures in an effort to build movie making into a flagship industry in Taiwan. With the support of policies, some locally produced movies directed by new and aspiring directors in Taiwan have generated attention grabbing results in terms of box office. The success of the movie Cape No. 7 directed by Wei Desheng in 2008 has rekindled the confidence in the locally produced movies from the Taiwanese audience and has triggered a new round of renaissance in Taiwan.

Table 1 Box office statistics in the region of Taiwan

		Locally produced movies in TW	Chinese Mainland and HK	Movies from other regions
2011	Number	36	38	404
	Box office (NT 100 million)	7.1	3.7	30.1
	%	17.5%	9.1%	73.4%
2010	Number	38	37	367
	Box office (NT 100 million)	2.3	1.6	27.0
	%	7.3%	5.3%	87.4%
2009	Number	28	30	311
	Box office (NT 100 million)	0.6	0.6	26.0
	%	2.3%	2.1%	95.6%
2008	Number	26	29	343
	Box office (NT 100 million)	3.1	1.8	20.4
	%	12.1%	7.0%	80.9%
2007	Number	22	20	354
	Box office (NT 100 million)	2.0	0.6	24.4
	%	7.4%	2.2%	90.4%

Source: Taiwan Movie Network

B. The fragmentation of the television media market is forcing a reduction in production cost

According to the data provided by NCC, Taiwan has the highest number of TV channels in Asia, a total in excess of 250 (including both domestic and overseas), serving over 23 million viewers. The television media market is rather fragmented compared with that of Korea that has 70 channels covering a population of 40 million. More television channels mean a diluted viewership and a smaller one per channel on an average basis, affecting the viewing ratio and advertising revenue. The fixed advertising volume has to be spread across a wider selection of channels, resulting in a lower return and pressure on TV drama production cost reductions. The current circumstances of inadequate funding and support are also challenging the ability to enhance the quality of Taiwan produced television programs and the long-term development of the television industry in Taiwan.

Arguably the biggest concern for the movie and television industry in Taiwan is the development and sustainability of local talent. Fierce competition and the limited revenue of the movie and television industry in Taiwan have drained investment in talent development and restrained the accumulation of relevant experiences in areas such as special effects and martial arts, and restrained the.

C. The magnet effect of the Chinese Mainland market

The over 1 billion viewers and abundant funding in the Chinese Mainland market are a huge magnet to players in the movie and television industry in Taiwan. A large number of production companies have been working on TV dramas outsourced by the Chinese Mainland or on joint productions. The trend now has extended beyond directors, actors and actresses, to moving the entire crew including costumes, make-ups, props and photographers to the Chinese Mainland.

V. A comparison of the development in the movie and television industry in the Chinese Mainland, Hong Kong and Taiwan

It is now over twenty years since the Chinese Mainland, Hong Kong and Taiwan started the cooperation in the production of movies and TV dramas in the early 1990s. A look at the development in the industry in the three marketplaces (see Table 2) shows that the Chinese Mainland boasts a vast market; Hong Kong has amassed tremendous experience in the movie industry and its progress in the special effect productions is leading Asia; whereas Taiwan's TV dramas based on Qiong Yao's bestselling novels and the idol dramas have a widespread influence over the Southeast Asian market. The respective restrictions of Hong Kong and Taiwan markets means that both will need to rely on the export market for continued sustainable growth, which augurs tighter and closer cooperation and interaction across the three marketplaces.

Table 2 A comparison of economy, population and movie box office among the Chinese Mainland, Hong Kong and Taiwan

Statistical Type	Chinese Mainland	HK	TW
Per capita GDP (USD) in 2012	6049	35961	19888
Population	Total population reached about 1.35 billion in Chinese Mainland by the end of 2012	The total population of Hong Kong reached 7.174 million, a growth of less than 1%, by the end of 2012	The total population in Taiwan reached 23 million in 2011
Box office revenue (RMB yuan)	17 billion in 2012, a 30% YOY growth	1.28 billion in 2012, a 12% YOY growth	850 million in 2011, a 33% YOY growth
Revenue split ratio between the producer/distributor and cinemas	Suggested by SARFT: 43% for producer and distributor, 57% for cinemas	40:60 (10% of the 40% received by producers to be allocated to the distributors)	50:50 between cinemas and movie producers, with producer's share dropping by 5% on weekly basis.
Number of movie screens	13118	198	115 movie theaters/592 screens

*: Most of the local movies split revenue at the ratio of 38% - 40% with only a small number of local commercial blockbuster movies receiving a share of over 41%.

Source: Deloitte Research

A. Leverage on Hong Kong’s lead in special effect technology to improve the visual effect of the movies

The box office success of the special effect movie Kung fu in 2004 which generated box office receipts of RMB 170 million in the Chinese Mainland, and the 3D movie Journey to the West: Conquering the Demons at the beginning of 2013 which generated box office receipts of RMB 1.24 billion in the Chinese Mainland was, in addition to an attractive story, attributable to the sci-fi special effects that dramatically enhanced the level of visualization rivalling the special effects of American blockbuster movies, and in marked contrast to similar genre movies produced by the Chinese Mainland and Taiwan.

In addition, new technologies will create new markets. Currently, the rapid development in the video websites in the Chinese Mainland has created a wider space for the movies and TV dramas of the three marketplaces. Aided by the growing coverage of mobile intelligent devices, video websites will undoubtedly enable more movies and TV dramas to penetrate into cities of all administrative levels in the Chinese Mainland.

B. Leverage on the export markets in Hong Kong and Taiwan to broaden the distribution channels for movies and TV dramas

According to the statistics from the TV Drama Division of the SARFT, the TV dramas produced in the Chinese Mainland in 2012 climbed to the top in the world to reach 17,000 episodes. But unlike marketplaces such as US and Korea, the export of China’s TV dramas dropped significantly. In 2011, the export volume of Korean cultural products led by TV dramas amounted to USD 700 million compared with RMB 100 million by the Chinese Mainland. The return on investment in the Chinese Mainland’s TV drama production will grow dramatically if its products can be exported to a wider overseas market. In this respect, both Hong Kong and Taiwan have experience of a booming period in the export of their TV dramas and therefore have a bigger talent pool with experience in the marketing, creativity and operation of TV drama exports. The TV drama industry in the Chinese Mainland will have a broader space to grow if the producers in the Chinese Mainland can broaden their international perspective, learn from the greater experience of Hong Kong and Taiwan in the establishment of export channels, and deepen the trilateral cooperation.

In short, there is vast room for the Chinese Mainland, Hong Kong and Taiwan to carry out cooperation in the movie and TV drama industry in the future. Despite the differences in cultural background and the challenge of a complicated approval process, joint production has become a trend. That said, the must-do's include learning from each other, enhancing the influence of and reducing the investment risk in the movie and TV dramas. These are necessary to ensure that the future development of the movie and TV drama industry in the three marketplaces is heading in the right direction.

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