

**Reader**



**Two-Part film20 Congress**

**EU-EXPANSION AND THE FILM INDUSTRY**  
**Challenges and Opportunities of EU-Expansion**  
**towards Eastern Europe**

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# Between Hype and EU Enlargement – Problems and Perspectives of the Film Industry in Germany and Austria

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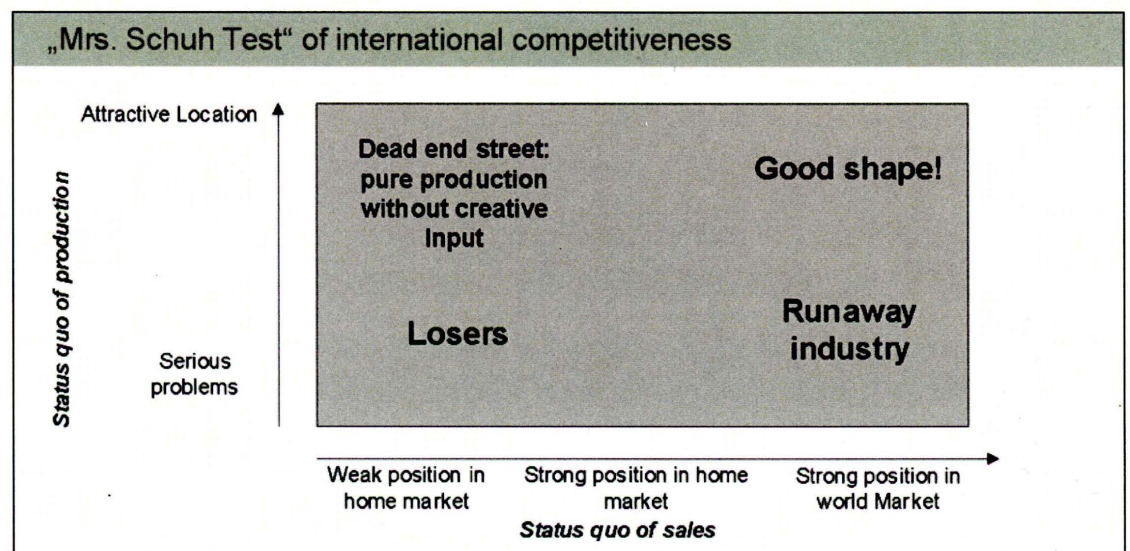
## 1. How fit is the film industry for the EU enlargement?

Are the German and Austrian film industries prepared for the EU enlargement or aren't they? What does that mean, anyway – to prepare for EU enlargement?

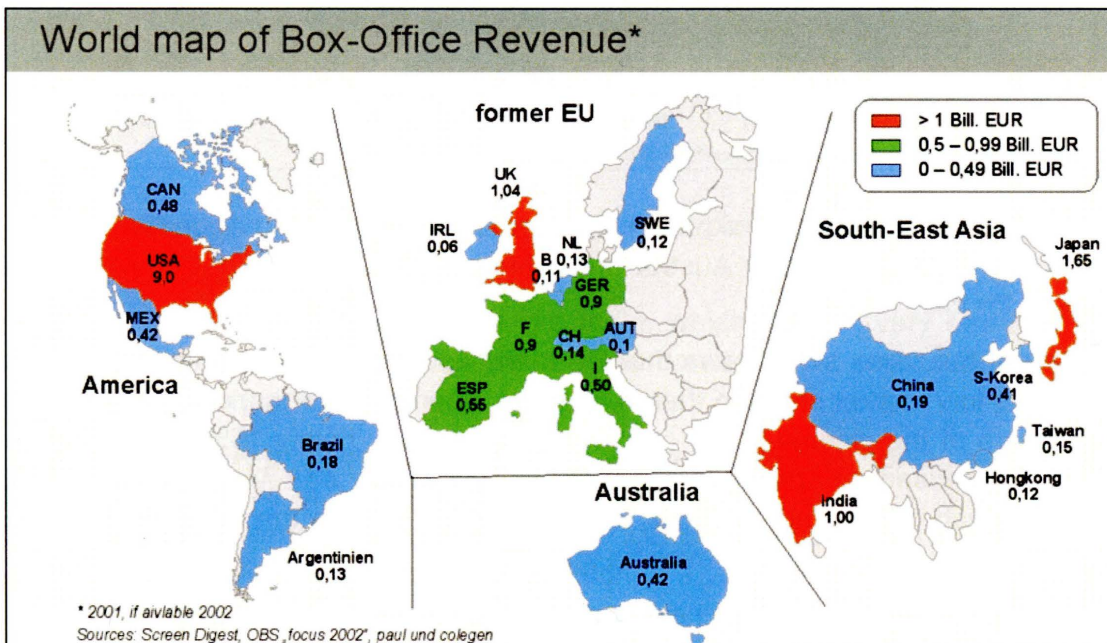
It means to learn from Ms. Schuh. Ms. Schuh is the owner of the hairdressing salon "Salon Silvia" in the Austrian Kautzen near the Czech border and was honoured by the Austrian chamber of commerce for her excellent preparation for EU enlargement. When she is asked what she has done in detail, one hears things like: "As soon as possible I want to employ Czech hairdressers as well. As a service for my Czech customers, but also because I can get qualified staff there that I cannot get here." – "I want to keep my loyal customers, therefore I offer prolonged opening times and a hairdresser's breakfast." – "I have attended Czech language lessons, because I want to gain more customers from over the border. The first ones are already coming." You see, Ms. Schuh does two things: She tries to use the chances that offer themselves on the procuring side as well as on the sales side. This way of thinking is by no means a one-way street. So there are very successful examples of companies from the accession countries that come to Germany and Austria. For one year now the electronics department store "BOF", which is owned by Slovenes, has been situated on Vienna's main shopping street. By the way, BOF means "building of fun" and the hope remains that this fun will be on both sides.

If one takes Ms. Schuh's behaviour as a model, one comes to a kind of "test". Is one's production situation thus that one is an attractive production site?

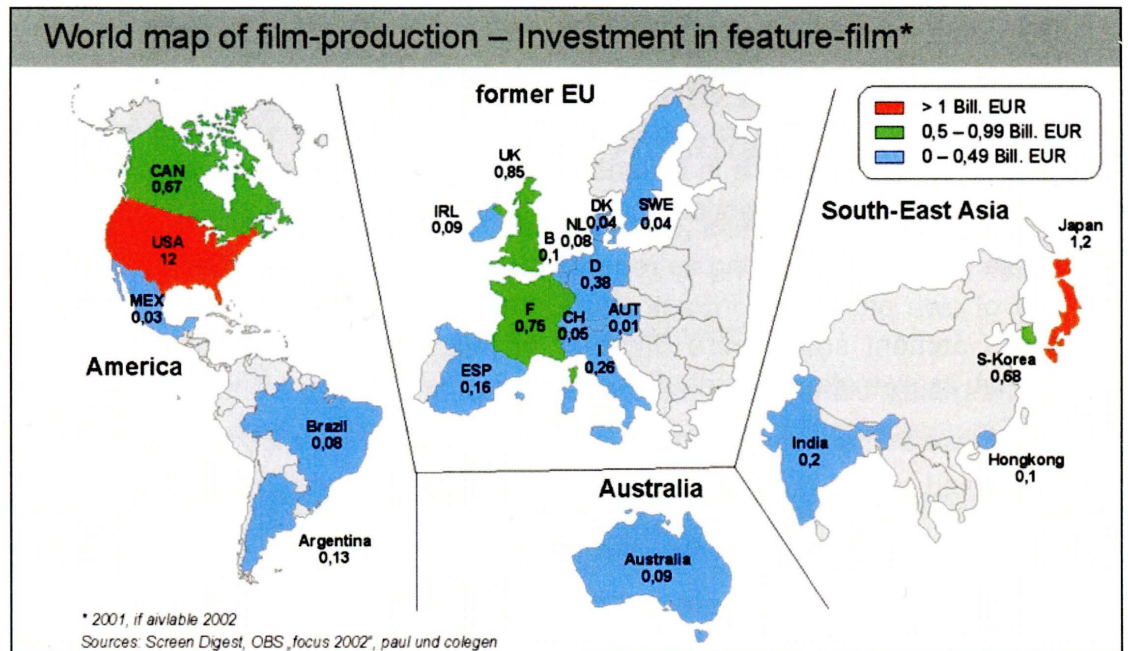
It is important, on the exploitation side, to have the home market as a base and that one tries to gain a strong position on other markets.



- The companies and countries that are weak as regards sales on the home market and at the same time have a weak production position are sure losers.
- Those that are very fit as regards production, but have very little assets as regards exploitation, are in a dead end, so to speak. They develop in the direction of an extended workbench without real creative input.
- Those that are very strong as regards distribution, but have little to offer in the way of own production infrastructure, become "vagabond trade", which produces content somewhere or other in this world in order to distribute it through its own strong distribution channels.
- Only those that are strong in both respects are really fit for EU enlargement.



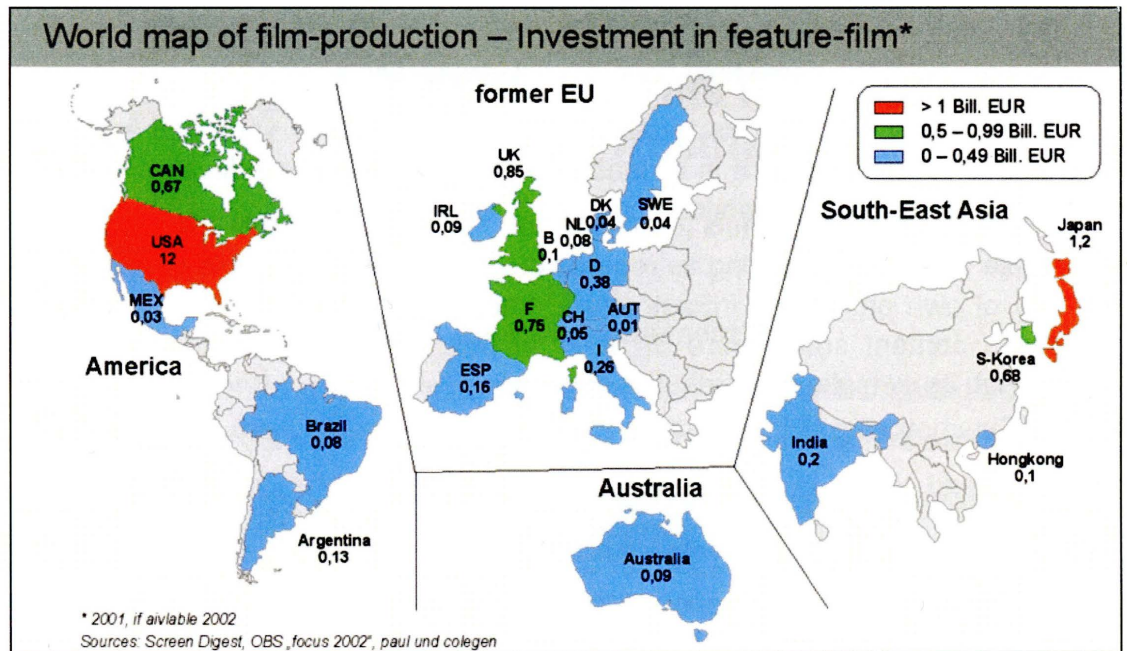
What is Germany's and Austria's position in this respect? One look at the world map of proceeds in the film industry shows that the German-speaking area definitely is of considerable importance here: second on the television market worldwide, fifth on the cinema market with regard to box office takings – definitely an area with a certain importance as a sales market.



How does the other side look, the investments in film, the production budgets? In this respect Germany and Austria fall behind considerably. What could be the reason for this?

A look at the sales side shows that Germany as well as Austria already have a relatively low market share in their respective cinema home markets. In Germany this share of the cinema home market is permanently below 15%, small aberrations are caused by special films, such as *Der Schuh des Manitu* or *Goodbye, Lenin*, which has pulled statistics up this year. In Austria the share of Austrian films on the cinema market is even as low as 4%.

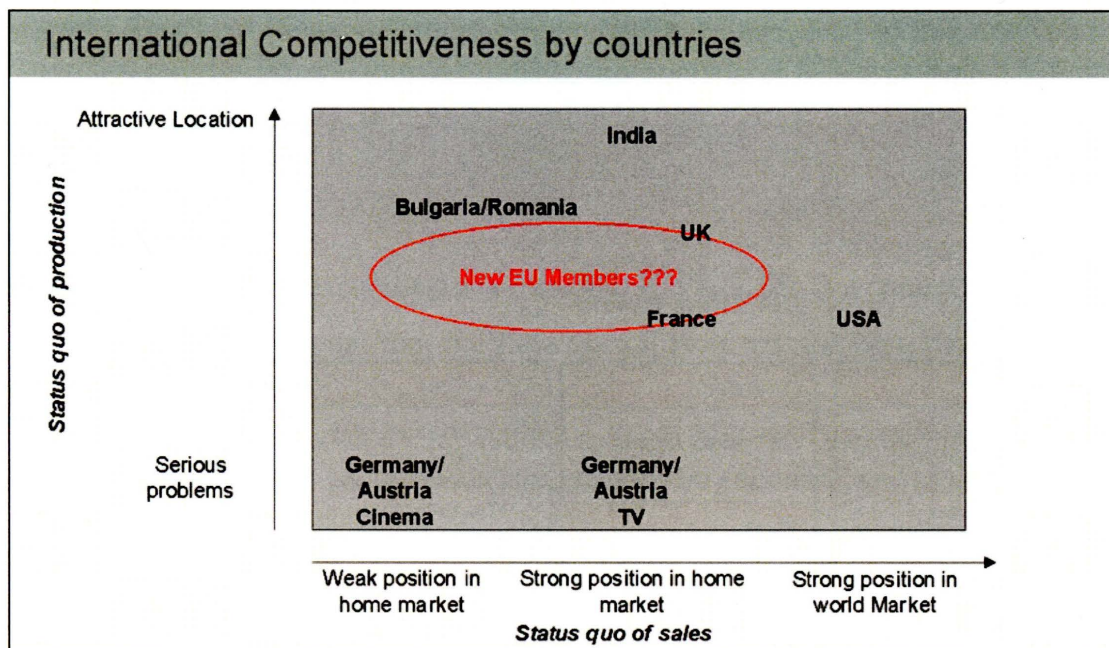
On the production side, the other dimension of fitness, at first there is a quantitative overfill: In Germany there are 453 production companies that say their main work is the production of movies. Of these, 100 companies made just one single movie in 2001 and just three made more than four movies. 330 of these companies produced absolutely nothing in 2001. That means that these companies really did not fulfill their business purpose in 2001. As regards studios and film service companies as well there are unused capacities, as the production situation is not very attractive.



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If one looks at the above developed portfolio again under these basic conditions, one finds

- that there are absolute winners like India, which are not very strong in exploitation outside India, but have a great home market and produce excellently for this market.
- that the USA are outstanding as far as exploitation is concerned, but increasingly have problems regarding production in the USA – due to unions and partially very high costs. Therefore US studios evade production in the USA and strongly develop in the direction of a vagabond trade, trying to combine their excellent sales possibilities with the cheaper production possibilities they find elsewhere in the world.
- that UK and France, who are relatively strong at home as regards exploitation, are also attractive as production sites – especially UK due to very attractive tax incentives.
- that Germany and Austria are in a losing position in the cinema field at the moment, because their position on the home market is relatively weak and they have severe problems in the field of production.
- that Germany and Austria are very strong in the field of television as regards exploitation, but here as well there are severe problems in the field of production.

A first thesis therefore is: the film countries Germany and Austria are not prepared for EU enlargement and they are dwarfs, seen internationally. In this respect they can offer relatively little to the new partners.

## 2. Why does the European film industry need Germany and Austria?

Why, really, is it a problem for the accession countries that Germany and Austria are relatively weak at the moment? Because they are needed, also by the accession countries, because it is a very interesting option for the accession countries

to develop further jointly with Germany and Austria. Because: what would be the strategic alternatives?

Why do the new members of EU need Germany and Austria?			
As an alternative they could cooperate with others ...			
USA-Option	„small sized“ EU-Countries Option	UK Option	French Option
<b>Production</b>	<b>Production</b>	<b>Production</b>	<b>Production</b>
Excellent chances, development depends on the level of cost	Excellent chances	Good chances if low costs can be combined with UK Tax incentives	Excellent chances for Co-Production
<b>Sales</b>	<b>Sales</b>	<b>Sales</b>	<b>Sales</b>
Limited upside because of American Sales Strategy	Good, but market size is very limited	USA-oriented	Good

The first alternative for the accession countries would be to join the USA more strongly. As regards production the chances are excellent here, partially they are already being used because the USA produce a lot there. As regards sales the accession countries would surely have small chances to co-operate with the USA, because the USA have their own interests (because of their own great production volume).

- As far as the smaller EU countries are concerned, there should be excellent chances regarding production co-operations, with regard to sales these markets are of relatively small size.
- The UK option, too, looks relatively one-sided – chances here are in the (co-)production field, as regards sales the UK are oriented rather towards the USA.
- As far as France is concerned, chances are very good, as regards sales as well as production, but France alone would not be enough.

So the great chance for the accession countries is to co-operate with Germany and Austria. For the accession countries this would also be the first step of a cascade for entering the European market. It is a big market and both sides can only profit from it. The film industry in the accession countries needs a strong film industry in Germany and Austria as a locomotive for the world market.

### 3. Why do Germany and Austria have a fitness problem?

What are the problems that at the moment prevent Germany and Austria from acting as a stronger locomotive? Due to economic factors the classical growth factors that in the past made up the system's stability in both countries – high advertising proceeds, high programme investments, growing proceeds from pay TV, imagination with regard to new chances, increasing public interest, or growing turnovers from ancillary rights – failed to apply in the last few years one after the other: due to an advertising crisis, due to the Kirch bankruptcy, which caused

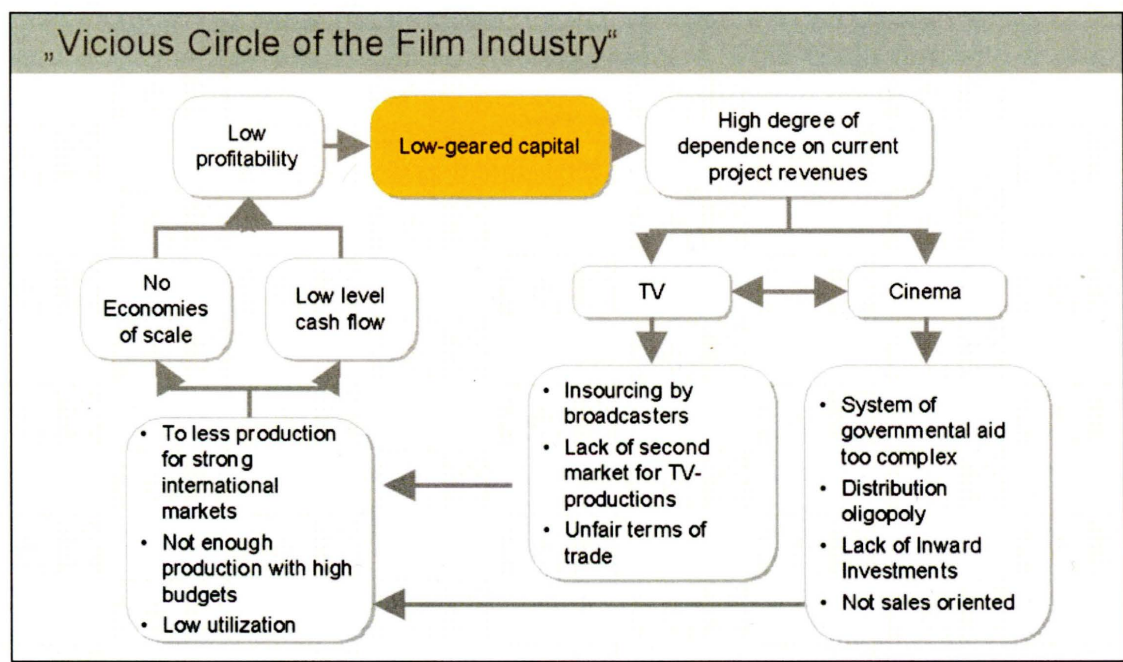
programme investments to decrease quite a lot, due to a lot of free TV, which made the pay TV plans rather fall behind, the bursting of illusions regarding turnover with ancillary rights, due to an exodus to new media, the zapping problem, cutting out advertisements, etc. – altogether due to pessimism instead of new imagination.

If one looks closer, however, one has to say, that even in the years when the media were still doing excellently, international success was not greater:

- Even with the millions from the new market they did not have more success outside the home market.
- The situation, that was influenced by setting up of the German private television system in the '80ies and '90ies, cannot be repeated and signified an exceptional economic situation.

That means that altogether one has to say that the reasons for the lacking competitiveness of the German and Austrian film industry are not really, on an international scale, due to economic factors, as it is said frequently at the moment, but rather structural.

This structural weakness is not due to the taste of the public – German-speaking productions have great success in German and Austrian TV, movies from both countries are rated as excellent by the cinemagoers – but rather to a vicious circle, which will be discussed more in detail in the following:



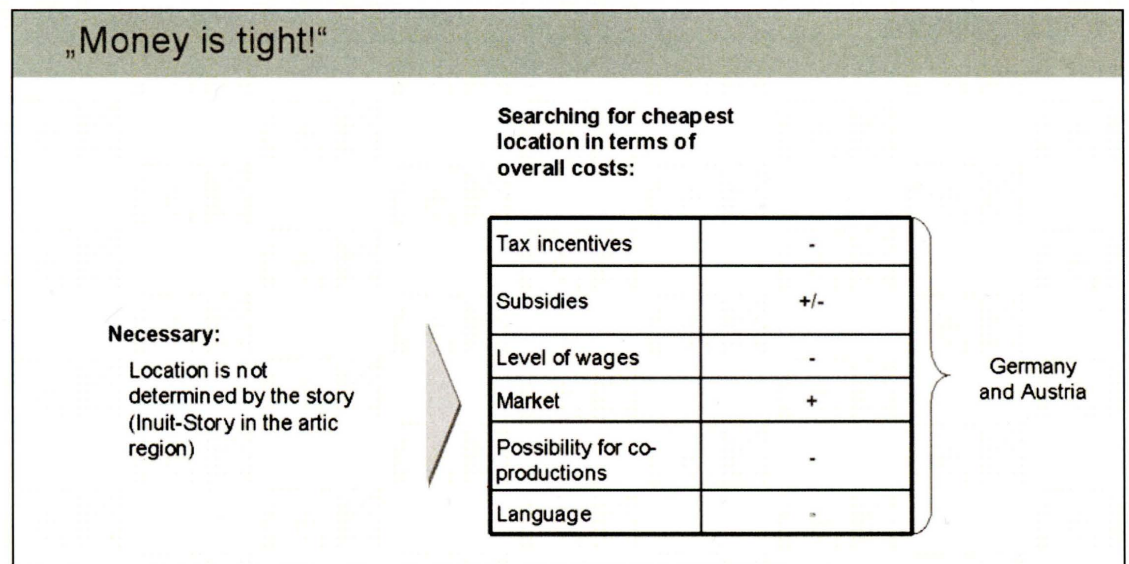
The starting point of this vicious circle is the little amount of company capital that producers in Germany and Austria have. There simply is too little company capital to really move something, to boost distribution, etc. Instead the producers always have to live from hand to mouth, they depend on the regular proceeds and do not have the staying power to situate themselves in a more professional way. However, even this daily business does not make any progress.



As regards cinema it can be seen:

- that in Germany and Austria there is a much too complex promotion system. With regard to Germany one could say: If you want butter, give a litre of milk into the German promotion jungle. There are very different institutions, from promotion from the individual länder to promotion from the federal government – here the system could be much more efficient.
- that the producers are not oriented enough towards distribution, here the producers should show some self-criticism.
- that inward investments, i.e. investments from abroad, is missing.
- that there are problems with the rental situation.

Especially the last two points have to be seen critically. Cinema is very much of a vagabond trade today. Producers go wherever they achieve the best financial conditions. This makes such things as tax incentives important for producers, tax incentives that we don't have in Germany and Austria.

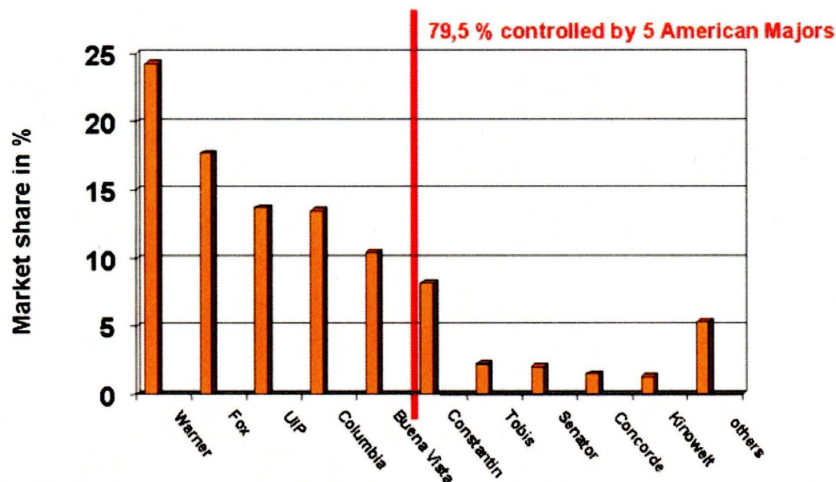


In other countries, such as Great Britain, Luxembourg, Ireland, there is tax promotion of the film industry amounting to between 15 and 25 or 30 per cent of the budget. There is no such thing in Austria and Germany, which renders these countries less attractive per se. Promotion is very complex, as I have said already, the salary level is a real disadvantage, the sales market is a real advantage, the co-production situation is difficult especially in Germany due to a tax law that is a bit odd, and the language is certainly not an advantage either.

The rental situation is another very critical problem as regards cinema. If one has a look at the market shares of movie rental companies in Germany, one notices that almost 80% are in the hand of American majors, which, of course, have only a limited interest in admitting others to this way of distribution.

## Market share of distributors in Germany 2002

Controlled by the American Majors.



Source: Bayern LB Research

That means there is an absolute bottleneck situation here, comparable to the situation in branches of industry such as the food retail trade, where it is difficult for small suppliers to survive against the brands of the big food retail trade groups and place their products on the shelves.

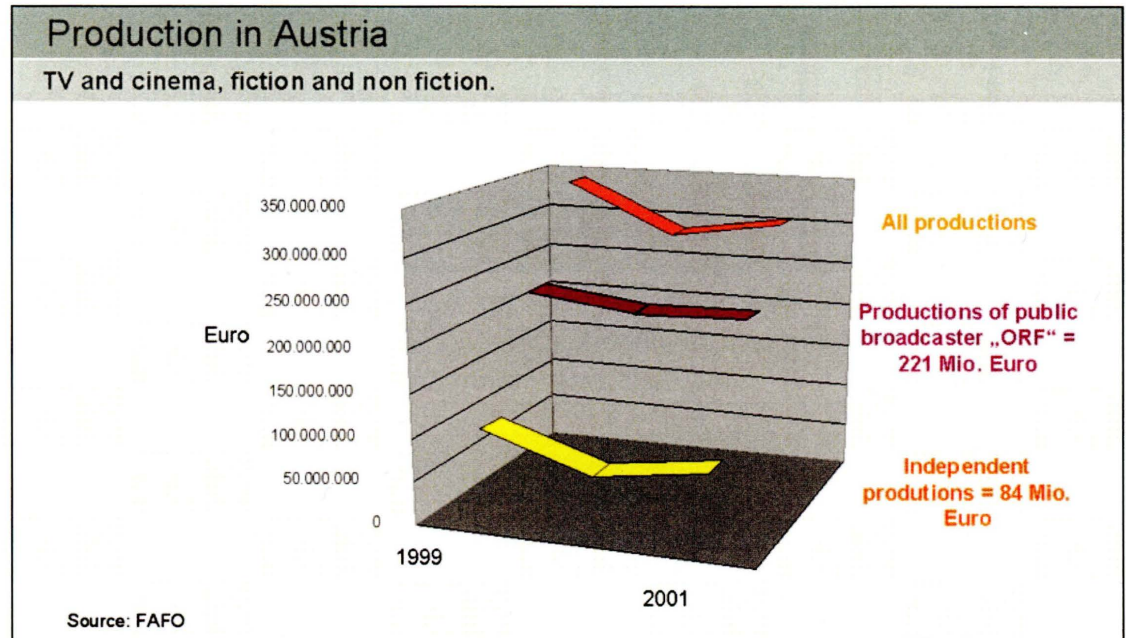
On the TV side on the one hand there is the problem that the television companies increasingly in-source production, i.e. they work with production subsidiaries and do no longer employ independent producers. This could turn into a great quality problem in the long run, because an industry can only be successful, if there is a creative supplying industry. In the automobile industry we would probably still have the cable break, if there had not been such strong suppliers as Bosch, who invented ABS!

The lack of a secondary exploitation market for TV rights makes it very difficult to again make money from these rights and thus achieve sufficient proceeds to cover the production costs and profits to strengthen the company capital. The fact that this is impossible to achieve at the moment can be seen as being caused by the very bad terms of trade.

Particularly in the fictional field these buying arrangements have a negative effect for producers, as there are very many producers offering programmes to very few television companies for a limited number of slots. In the non-fictional field it is a little easier, because there are very few heads and very few topics. The terms of trade are centred on a system called "commissioned production", stemming from a time when the television company still developed concepts that were given to the producer for production only, the producer then receiving a certain budget for invoicing. In this system the producer, who practically was just an extended workbench, handed over all rights to the television company. In the last few years the situation was totally different, because the producers have to develop a lot of topics themselves and then offer them to the television companies in order to be considered. This amounts to considerable preliminary work. Also, the producers have to perform a lot more in production, e.g. casting, etc., which is not covered

by the budget – but now as before all rights have to be handed over to the television companies. A situation in which the producers are downright squeezed.

In addition, the numbers of productions being ordered by the television companies have decreased very much. For example, in Germany TV movies decreased from 330 in the year 2000 to 200 in 2002. In Austria the situation is similar:



All these things lead to an insufficient production for markets that would yield high proceeds. There is too little production with big budgets. Capacity utilization is poor, in this respect economies of sale are missing. There is too little return, poor profitability, and here the vicious circle closes: the little company capital is not increased and possibilities of expansion remain poor.

This vicious circle, and this is the third thesis, is the real structural cause for Germany's and Austria's weakness.

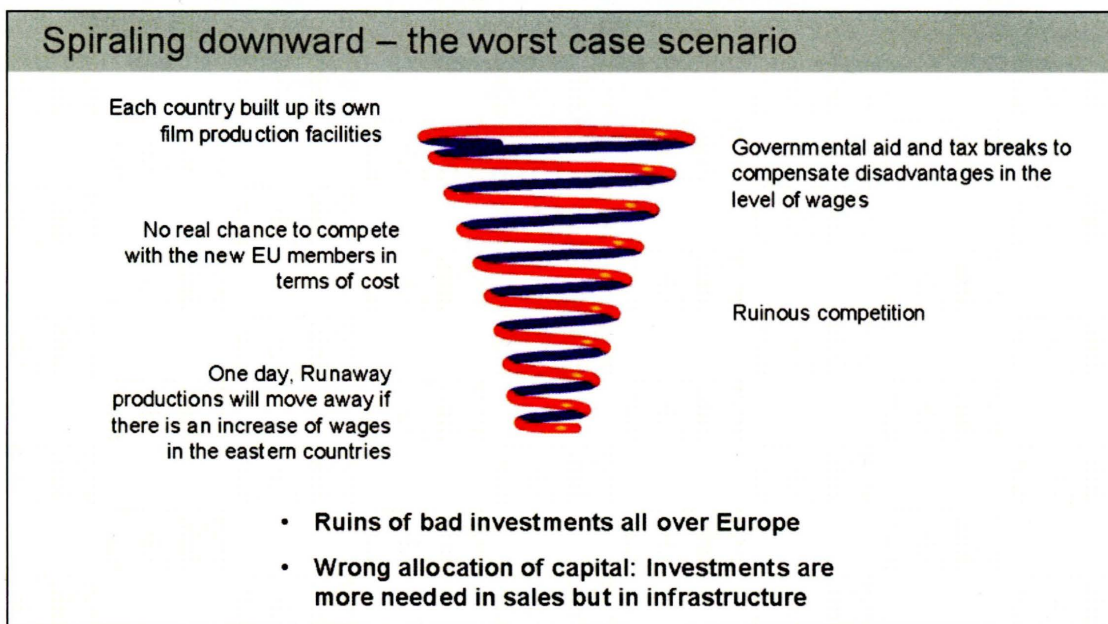
#### 4. What could a training programme for the German-speaking film industry look like?

There is need for action on different levels:

- On the international level it is crucial to strengthen competitiveness, this includes thinking about how tax incentives could play a role in Germany and Austria as well.
- On the national level system faults have to be eliminated, e.g. as regards TV, we have to cut through the jungle of promotion regulations, and the distribution bottleneck has to be eliminated.
- On the individual level of the individual company bigger units have to be formed that work more sensibly with regard to creativity and economy. On the one hand networks of creative production units have to be generated, on the other hand networks of efficiently operating and well utilized technical service companies have to be formed, a newly structured distribution system, and a

network node coordinating these things in a way that the company can act more professionally.

In other words: In Germany and Austria everybody has to make their homework, the producers, the television companies, the rental companies, the distributors, the service companies, and of course the government as well. The one thing that should be avoided in any case during all this optimization in the respective country is a downhill spiral.



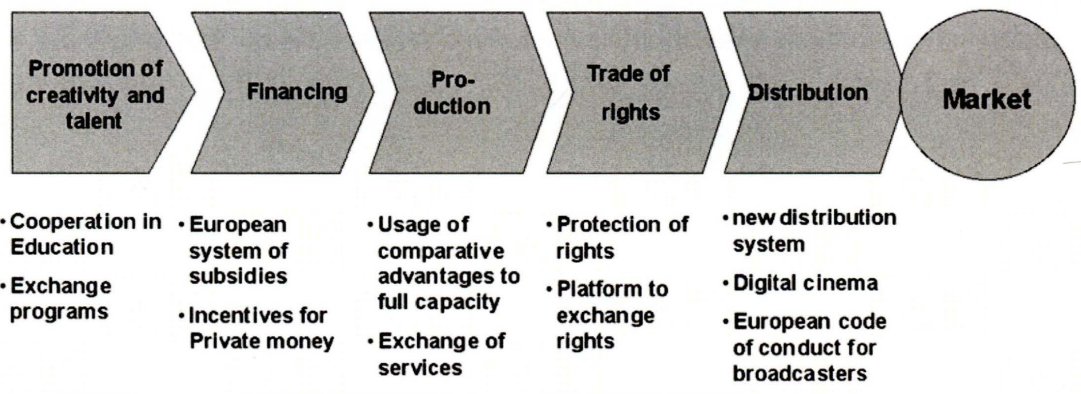
It starts with every country further expanding its film centre, which leads to further considerable over-capacities, which is counteracted by promotion and tax incentives in order to balance these salary cost disadvantages, which in the end just leads to more ruinous competition, with salary cost advantages moving farther east with growing salary levels and investment ruins remaining all over Europe. Built with money that would have flown much better into a common distribution system and the generation of common structures.

Thesis no. 5 is therefore: The imbalance of fear has to stop, in Germany and Austria there must not be a new subvention mentality and the accession countries have to think about what should really be sensibly built up in the terms of infrastructure – everything aiming at mere salary cost advantages is very transitory.

In the end the problems of lacking competitiveness have to be seen on an all-European scale, because in the audio-visual field all Europe has a considerable trade deficit compared with the USA. For this we have to have a look at the entire chain of value added, from promotion of creativity and talents, via financing, via production, rights trade, distribution, up to the market, and to ask at which points useful co-operations could be set up, where there are possibilities of moving more in an all-European way.

## The value chain of film industry

European division of work is necessary...



So what is needed is an initiative "European chains of value added" for the film, which does not ask any longer what can be optimized in the individual countries, but how this could be tackled jointly. Particularly in production there is a wide field of comparative advantages lying fallow and thus a potential for synergetic effects. Also many topics are still waiting for filming, that are fascinating for more than one European country or even for the world market.

The thing most dangerous for the film industry in Europe is a discussion whether there is a European film at all. In fact such a discussion will just hamper development. Of course there will be European films, there will also be national films, that are produced in different European countries, but in the end what is important is that the chains of value added are finally combined. Only this way can a real "film" branch of industry be set up all over Europe which is not noticed just by cultural politics and thus no longer is standing aside compared with less promising branches of industry (e.g. shipyards). In the end the motto for the European film industry can only be: "Just do it!"