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TEACHING NOTE

The Movie Exhibition Industry: 2017

Case Overview

The Movie Exhibition Industry 2017 presents an overview of the domestic motion picture exhibition industry – the local movie theater – from its inception through 2017. From the evidence gathered about the major firms that control the majority of the domestic market share, the outlook for the industry is uncertain. Attendance shows a general declining trend in recent years while box office receipts hit an all-time high in 2017 due to increased ticket prices. The threat of substitutes continues to increase significantly.

We recommend using this case as an introduction to the case analysis process, to highlight changing industry dynamics, and to demonstrate the usefulness of general environmental analysis and Porter's five forces model to understand industry forces that firms are sometimes subjected to with little influence over changing those forces. The first half of the case presents the movie exhibitors situation, while the second half details initiatives undertaken by exhibitors in response to the changing environment.

The first half of the case is devoted to presenting a detailed situational analysis of the external and lack of differentiation among exhibitors. This begins with an overview of the industry value chain. Exhibition is a stage in the motion picture value chain which also includes motion picture studio production and distribution. The case demonstrates how exhibitor power continues to decline due to highly differentiated motion picture content, studios' emphasis on international growth, studios' ability to disintermediate exhibitors, and increased competition for viewing offered by television and home viewing of movies.

The rise of substitutes is central to understanding the exhibition industry. Home viewing of content, including movies and increasingly television shows, through streaming services such as Netflix are substitutes to theater attendance. The main reasons people attend the theater include the big screen, impressive audio, and not having to wait for a movie to be available. The visual and audio experience offered by home theaters is increasingly matching that offered by exhibitors and the wait time for movies on DVD and streaming services continues to decline.

The case presents detailed assessment of exhibitor's three revenue streams: box office receipts, concession sales, and advertising. The movie exhibition business has long taken the form of loss leadership: At best, break even on box office receipts to draw in patrons while profiting from concession sales.

Continued consolidation among domestic exhibitors has increased their bargaining power, yet studios remain more powerful as reflected in stable film rental costs as a percentage of box office receipts. Exhibitors also have no power over which movies are made, they can only hope the studios will produce movies appealing to audiences. A new revenue and profit stream and advertising to theater patrons offers exhibitors attractive profitability, but detracts from the theater experience.

The second half of the case provides an introduction to the strategic initiatives and actions exhibitors are undertaking to attract audiences.

Key Concepts

- Strategic analysis, formulation, and implementation
- External analysis
- Industry structural analysis (5-Forces)
- Industry life cycle
- Value chain (industry-level and firm-level)
- Internal analysis
- Business strategy
- Value proposition
- Revenue streams and profitability
- International strategy
- Strategic actions, initiatives, and alternatives
- Data analysis

Suggested Discussion Questions

1. Why do people go to the movies? What can explain the trend in attendance at movie theaters, and why is this problematic?

2. **How does the rate of technological advancements help or hinder the theaters?**

3. **What determines profitability for exhibitors? Consider revenue components, expenses, and the controllability of these by managers. Are any conditions of revenues, expenses changing?**

4. **What is the trend in profitability? What explains this trend?**

5. **Do trends in the general environment and industry structure affect profits?**

6. **(Advanced) For 1 through 5, which of these are symptoms? Which are causes?**

7. **Are the recent exhibitor initiatives helping to change the profit picture for exhibitors? What types of business-level strategies can you identify for exhibitors?**

8. **(Advanced) What effect will consolidation have on the domestic exhibition industry? The global exhibition industry?**

9. **What are some strategic recommendations for exhibitors to consider?**

10. (Advanced) What are the requirements for implementing your recommendations and what positive outcomes should be expected?

Suggested Answers

1. Why do people go to the movies?

According to the Mintel report presented in the case, the top reasons are the giant screen, the opportunity to get out of the house, not having to wait for the movie to come out on home video, the experience of the theatrical sound system, and the theater as a location for a date. (You can also discuss the movie theater "experience"—a combination of other factors such as nostalgia, popcorn, the environment of the crowd, etc.)

Historically, there have been few entertainment options. From the time films were first introduced (early 1900s) up through the 1940s, the only options were radio, live entertainment, and the family Victrola (record player). In the 1950s, television began to take off, giving people more entertainment options. These options have steadily increased: Think about the availability of movies through DVD purchases, DVD rentals such as Redbox and Blockbuster kiosks, video on demand, streaming, subscription downloads, and rentals like those from Netflix, digital purchases such as on iTunes, HBO, and Stars, streaming services (Netflix, Hulu, etc.) and 100+ television channels with movies on cable and satellite networks. These are just a few alternative ways to watch movies.

The amount of streaming content has increased dramatically in recent years and movies are just one type of content being consumed as a form of entertainment. Netflix and HBO are creating their own content available through their streaming services. The adoption of streaming services is also exerting pressure on value chain components such as studios simultaneously releasing films in theaters and via streaming sites. Add to this other entertainment forms like music (more radio stations, satellite radio, Internet radio, CDs, and MP3s), and the Internet, and you have many ways to spend time. The increased variety of live entertainment (music, theater, arts festivals, music festivals, and so on) available to many towns, not just in the largest cities, is also a growing substitute. Technically, *substitutes* have emerged in a number of forms.

Substitutes are the *causes* of many problems. Of the reasons why people go to the movies, there has been erosion in how these are fulfilled at the movies versus other options.

The Giant Theater Screen is not as unique as it once was. The most discerning viewers can have a large and amazing viewing experience in their home. TVs in homes grow larger:

- 2010 average TV screen = 32"
- 2014 average TV screen = 39"
- Sharp predicts it will be 60" in the near future
- 70+" sets are currently available for homes

TVs in homes higher resolution as broadcast signals were 480 analog, but are now in high definition (HD: 1080) digital; it rivals theaters' 4K systems with optimal viewing distances.

Ultra-high definition (UHD) 4K television sets are the new standard; are the best sellers among 60"+ TV. The next wave of TVs is expected to be 8K which allows massive screens (98" screen is noted in the case) at extremely high quality, but is currently very cost prohibitive. Large screen LCD TV's, Blu-ray HD DVD players and an inexpensive sound systems are all that is required to make a home theater. These can be purchased for than $1,000. Plus, many homeowners have created or want to create a home theater as a major home renovation project.

Supplemental analysis activity: Data in the case highlights the declining retail prices of 32" LCD television sets. It can be useful to demonstrate how rapidly retail prices in electronics are falling. In 2010, *Money Magazine* published data on the price declines from 2005 to 2011 for 32" LCD TVs. Prices fall, on average, about 18% per year. Have students paste the data into Excel and conduct a trend analysis. The forecasted price (power option; R^2 = .98) is slightly above $200 in 2016, nearly the exact retail price (see **Exhibit TN-1**).

This can be used to illustrate the challenge that theaters will have competing on the allure of the "big screen" as home screens continue to get larger and have higher resolution. Applied to the current generation of 4K televisions, the 2017 average retail price was $2,400 for the most current generation of 60" screens. For even greater effect, it can be applied to the next generation of technology; the 8K television. The case highlights the first 8K TV offered for sale: a 98" LG television with a retail price of $55,000. How long until screens with amazing clarity and size are available for the mass audience?

Overall assessment—large home screens are not quite as unique as true big screens, but are impressive and already in peoples' homes.

Follow-up Question: Is it always a big screen in the theater?

The "big screen" is not as big as it used to be—especially in the "-plexes." Exhibitors have different size theaters, the big screens are only in the big theaters and only the major opening weekend films are in those theaters. If you go to the summer blockbuster after it has been in the theaters for three weeks, you'll likely be disappointed with the size of screen.

The Opportunity to Be Out of the House creates more indirect competition to the movie theater. Coffee shops now offer a place where you can just go and hang out, as do new model book stores (Barnes & Noble, etc.). These emerged during the last 10 years.

Not Having to Wait to See a Particular Movie on Home Video The effect of this on exhibitors is mixed. This was really an issue before DVDs, VOD, Redbox, streaming using Netflix, iTunes, HBO, etc. With three network TV stations, no cable, and no other options, if you didn't see it in the theater, you likely never would. However, DVD sales decreased while digital purchases increased by 47% in 2013. However, studios countered by imposing a 28-day delay from DVD sales to rental and streaming availability with some studios considering a 56- day delay. The wait for a movie to be available for purchase was just 15.4 weeks in 2016.

However, if you want opening weekend, it is still an issue. Studios have experimented with simultaneous release to theaters, pay-per-view, and DVD. This is not yet widespread and unlikely in next three to five years. Disney, as the case notes, has indicated they remain committed to the theatrical release model.

But if you miss opening weekend, it is not much of an issue. Movies are in the theaters for fewer weeks. The lag between theatrical and DVD release ("release window") is shortening.

- In 2000, the average release window for DVDs was 24 weeks.
- In 2006, the window averaged 18.7 weeks
- In 2016, the window averaged 15.4 weeks

SUPPLEMENTAL ACTIVITY

Analyze and forecast the DVD release window in future years. **Exhibit 13** in the case presents the weeks until a DVD is released following theatrical release. The time is declining with DVDs being released, on average, one week earlier every two years. First, inquire how students would wait to see a movie versus seeing it in the theater? The answer will likely depend on the movie, but ask for an average. Have students conduct a forecast on the release windows to see what it will be five and 10 years from now (see **Exhibit TN-2**).

An incredible amount of content is available elsewhere, outside of the movie theater.

- Streaming is the fastest growing portion of the windowed theatrical release model. Streaming grew 22% from 2015 to 2016 to $6.2 billion. Note that this is a large market, but provides far less revenue (perhaps $0.50 per viewing) to studios that selling DVDs ($12–$15 to the studio) or theatrical release ($4.67 to the studio).
- Premium video on demand, DVD purchase, electronic downloads, video on demand, rental – daily (Redbox), rental – subscription (Netflix), streaming – Netflix, premium movie channels (HBO, Showtime, etc.), subscription cable, and broadcast networks.
- Price of DVD or streaming declines with the length of time from the theatrical release.
- Not just movies anymore: television, sports, music.
- There are many, many ways to stream content (TVs, Apple TV, Cable and Satellite boxes, video consoles, add on dongles such as Google Chrome, laptops, and tablets).

In summary: It is usually cheaper to wait (own it for what it costs to see it at the box office) until it's widely available. The wait is declining, hurting theaters.

The Experience of Watching the Movies with a Theatrical Sound System Uniqueness of impressive sound is also declining. Size of TVs is still increasing as well as sophistication (4K) bundled with audio systems. Content available in surround sound—same as theater. Inexpensive, but impressive, quality sound. A pretty solid home theater system can be purchased for well under $1,000.

SUPPLEMENTAL ACTIVITY

Have a competition amongst students to assemble a home theater at the lowest cost. Assemble the purchase list for a system with components meeting the following specification: 50" or larger screen, 4K resolution, streaming capability, DVD player (with 4K up-convert), and 5.1 sound system with subwoofer. Research on Amazon.com and Bestbuy.com. This leads to the "How unique is the viewing experience at the local theater compared to what you can get at home? How many of you have this at home already?"

The Theater as a Location Option for a Date is still an advantage of the theater. Anyone want a first date to be a movie and popcorn with his or her date, and mom and dad?

Then there is perhaps the most important aspect of all: **The "Experience."** However, the quality of the theater going experience is widely viewed as in decline. Largest complaints:

- Cell phone interruptions—The bane of modern humanity!
- Broken ticket machines
- Advertisements—Pay $8.65 for a movie and you have to wait through 20 minutes or more of ads and trailers.
- Number of ads has increased, as has advertising revenues. Up 307 percent from $186 million in 2002 to $758 million in 2016. Averaged $17,774 per screen in 2016, about $0.57 per attendee.
- Others: rude moviegoers, lousy movie choices, sound from other theaters, no ushers, etc.

It is unknown if this is truly a decline in service or if it is fond memories.

1. What can explain the trend in attendance at movie theaters, and why is this problematic?

The headlines report a record setting gross revenue—but that fact doesn't tell the whole story. Revenues = # tickets × $ per ticket. Prices have increased (above the rate of inflation in recent years indicating the theaters are able to create additional value added), while ticket sales have not. Attendance is way off the historical high, and has declined in the most recent year:

- 2016: 1.314 billion tickets sold (ranks 8th lowest in 10 years) – 3.8 movies per person
- 2014: 1.25 billion tickets sold – 3.9 movies viewed per person
- 2012: 1.364 billion tickets sold – 3.9 movies viewed per person
- 2007: 1.386 billion tickets sold – 4.5 movies viewed per person
- 1980: 1.022 billion tickets sold – 4.5 movies viewed per person

Over the long term, the trend is downward, both in absolute tickets sold and per capita. In 1946, four billion tickets were sold (= 28 movies viewed per person). Movie attendance is declining domestically. In the case, **Exhibit 2** shows attendance and revenues, **Exhibit 3** shows ticket prices.

Attendance figures are **symptoms** of the problems.

The quick response answer, "because it hurts your profits" is not entirely true. As the next question addresses, the exhibitors do not actually make a great deal on box office revenues, but it hurts sales of concessions (which are profitable) and eventually would hurt advertising revenues (which are based on attendance).

Decreased attendance is best viewed **as a symptom of the problems identified earlier**, *not as the cause*. Exhibitors are being disintermediated—they were once the sole route through which movies reached audiences. Now there are DVDs, cable TV, Redbox, VOD, iTunes, and other media formats. At some point, the industry may lack sufficient scale to remain viable.

What explains this? The preceding factors – TV, viewing options, bad experience, etc. According to Mintel, the reasons for *not* attending the movie theater are attributable to the declining "experience" and:

- The overall cost: ticket price + concessions
- At-home viewing options
- Interruptions such as cell phones in the theater
- Rude patrons
- The overall hassle: driving, parking, crowds, going out, etc.
- Ads prior to the show

Also, there is an emerging trend that is highly problematic for the exhibitors—the population among core movie audience (12–24-year-olds) will grow very little (see case **Exhibit 4**).

- Overall, from 2016 to 2035 the U.S. population will increase 17 percent, 58.4 million people.
- But the 12–17 age group will increase 14 percent—4.6 million more potential viewers and the 18–24 age group 18 percent – just 4.6 million additional viewers. The fastest growing segment of the population is the 60+ year old group, which currently has the lowest per capita viewing.
- Additionally, the 12–17 and 18–24 groups more readily rely on other eyeball entertainment via electronic devices more than previous generations; is the most likely to seek substitutes.
- Overall, the population will add just 1,452 additional viewers per screen (at current # screens). Based on attendance trends within age groups, this equates to 4,956 additional attendees per year per screen. Currently, screens average about 33,000 admissions annually (**Exhibit 9**: 39,579 screens and case page 1 = 1,314,000,000 annual admissions = 33,199 annual admissions per screen). Therefore, population growth will add 15 percent over a 20-year period, approximately 0.75 percent growth per year.

- The largest growth opportunity is amongst those 60 years and older (growing 42 percent; an additional 28.7 million potential viewers). The challenge is that Hollywood typically does not make movies for this audience and is increasingly focusing on international, rather than domestic, growth.

2. How does the rate of technological advancements help or hinder the theaters?

As exhibitors upgrade their equipment for better sound (Dolby 3.1, 5.1, 7.1, Atmos) and picture quality (analog, digital, HD, 3D, 4D, IMAX, 8K), how quickly do these innovations transfer to TVs? What is happening to the window of opportunity for theaters to repay their investment for upgrading their equipment? 4K TVs are already available on the market and screen size is growing rapidly while prices are decreasing.

Follow-Up Question: How does Moore's Law impact this industry?

If additional technological advancements are more quickly adapted for TVs, what are the distinguishing characteristics of theaters?

3. What determines profitability for exhibitors?

Consider revenue components, expenses, and the controllability of these by managers.

Exhibition portion of the business is not very profitable. (See **Exhibits 10 & 12**). Operating margins among exhibitors average about nine percent for smaller, regional theaters and 10.6 percent among AMC (6.6%), Regal (10.6%), and Cinemark (14.5%). Net income is quite low, averaging 5.8 percent: AMC (3.5%), Regal (5.3%), and Cinemark (8.7%). Note that net income is actually improving! During the period 2009–2010, the average net income for Regal, Cinemark, and Carmike was just three percent of revenues. Things could be worse: In 2007, Carmike had a negative margin on operations and experienced negative margin again for 2014. This, perhaps, helps explain why the firm was available to be acquired by AMC.

Overall, the business of exhibitors is best described as loss leadership on movies: the firms make money selling concessions and showing ads to patrons who are drawn in by the movie.

Revenues, expenses, and controllability:

Box Office Receipts One-half to two-thirds of revenues remitted to studios; very little return as almost all goes to the studios. Ticket price increases in recent years do not help increase attendance

- 2007 average: $6.88
- 2012 average: $7.94
- 2014: average: $8.59
- 2016: average: $8.65

Over the long term, ticket prices keep up with the rate of inflation. Over the last 10 years, ticket prices have increased faster than inflation. There is no data in the case to support this, but this appears to be attributable to general ticket prices, but also to charges for premiums, such as 3D, IMAX, and possibly even 4D (see **Exhibit 3** in the case).

Theaters have made significant investments in converting from film-based projection to digital, an investment estimated at $2.562 billion with mixed results. Cost side: Exhibition rental fees have not changed materially, still averaging 54 percent of the box office receipts, suggesting the studios and distributors are capturing the savings from lower distribution costs. The exhibitors, who made the digital investments, are not.

Revenue side: Surcharges for 3D and digital screenings do appear to have increased ticket prices. 3D, once considered the next wave of film, has been losing its appeal (based on the decreasing portion of revenue from opening weekend sales data; **Exhibit 14**). In 2010, 3D for televisions was the "hot" new feature. It remains available for many TVs, but receives little attention. Actual home usage is unknown.

Overall: Little managerial discretion beyond which movies are shown (but all theaters show the same movies; studios decide which movies to create and audiences to serve). If you can increase the experience, you can increase draw.

CONCESSIONS

Concessions average from 25 to 30 percent of revenues. Historically, direct costs are less than 15 percent of selling price, 85 percent gross margin. Concessions are the largest source of exhibitor profit. Profits are influenced by the three factors:

- Attendance at the movie—so the draw of films is still critical; more attendees = more concession sales
- Prices—highly studied, calculated on profit maximization
- Material costs—purchase volume (consolidation helping)

There is not much managerial discretion for concession sales. A common moviegoer complaint is high concession prices: $5.00 for a soda? $9.00 for popcorn? Not much room to increase prices on **existing** items. Prices are set based on profit maximization calculations. If prices are raised, sales and total profits decline. If prices are lowered, volume may increase, but total profit declines.

Theaters have expanded the concession options available in an attempt to increase food sales. Concession sales per attendee are increasing (see **Exhibit TN-3**).

Margins on concession have declined very slightly due to higher food costs. Overall, initiatives to sell higher cost food items appear to be one contributor to increased exhibitor profitability. To illustrate for students, consider an example for a large circuit (see **Exhibit TN-4**).

ADVERTISING

Advertising is just five percent of revenues. There is not much more growth in this revenue category without consequences to attendance. Seek to increase the revenue per ad instead of increasing the number of ads.

Advertising is, however, highly profitable. Any costs? Theaters are *paid* to display ads, but a common audience lament is too many ads. Managerial control—audiences *hate* the advertisements at the theater. Balancing the revenues from ads with audience tolerance is an ongoing struggle for exhibitors.

Several approaches being taken: increase ad quality via better production and make the ads seem more like content; interactive ads that use motion sensing technology to turn ads into games for the audience. These may lessen the detrimental aspects of ads, possibly make them seem like entertainment. Consider materials offered by National Cinemedia Advertising URL: https://www.ncm.com/

Follow-up Question: Why do all the exhibitors look the same?

There is little / no differentiation in the offerings of the major theater exhibitors. The prices within markets differ little, the same movies are shown . . . at the same times, the food and services are nearly identical. A viewer's choice of a theater comes down to: distance from home, convenience of parking, and proximity to restaurants.

Innovations by one theater chain are quickly adopted by others. The chains do serve different geographic markets and do so in different ways.

- AMC, operating under AMC and Loews chains, is the largest domestic exhibitor with 8,293 screens in 819 theaters domestically. AMCs domestic operations result from the combination of AMCs historical presence and the acquisition of the Carmike Chain. AMC historically focused on large, multiplexes in urban settings such as in California, Florida, and Texas with nearly 15 screens per location. AMC leads the industry in the operation of large multiplexes. They differentiate the viewing experience by offering 3D, IMAX, and other premium options. Not surprising, due to these additional and costly urban locations, AMC historically had the highest ticket prices ($9.43 in 2014). Carmike, alternately, through the Cinemark and Century brands, served smaller markets, operating as the sole theater in over 80 percent of its markets. Their average ticket price of $7.02 in 2014 was the lowest of the major chains. Carmike concentrates on small to midsized markets, targeting populations of less than 100,000 that have few alternative entertainment options.

  Most of Carmike's theaters has been rebranded as AMC and AMC Classic locations, but little other changes made. The average ticket price in AMC's combined operations in 2016 averaged $9.59, second behind Regal among the major circuits. AMC's size is not currently yielding increased financial performance. At 6.6%, AMC's operating profit as a percent of revenues is the lowest among the majors, well behind that of Cinemark (14.5%) and Regal (10.6%).

- Regal (Regal, United Artists, and Edwards theaters) focuses on midsized markets using multiplex and megaplexes that average 13 screens per location, with an average ticket price of $9.78. Both Regal and AMC typically face competition from exhibitors as well as other entertainment options.

- Cinemark (Cinemark and Century brands) serves smaller markets, operating as the sole theater in over 80 percent of its markets. Their average ticket price of $7.55 in 2016 was the lowest of the major chains, but is quite profitable. They do so with fewer screens at each location and, as of 2016, continue to achieve the highest profit per admission at $0.91.

  Cinemark has little competition where they are located, so they do not need to upgrade facilities, allowing them to keep costs and ticket prices low, which drive up attendance and bring in more profitable concessions and advertising revenue.

URLs for Circuits

Wanda / AMC

AMC Theaters: https://www.amctheatres.com/

Carmike (subsidiary): https://www.carmike.com/

Wanda Group (Parent): https://www.wanda-group.com/businesses/culture/cinemas/

Odeon, UK (subsidiary): http://www.odeon.co.uk/

Nordic Cinema Group (subsidiary):
http://www.nordiccinemagroup.com/about-nordic-cinema-group/

Regal Entertainment: https://www.regmovies.com/

Cinemark Theater: https://www.cinemark.com/theatre-search

Cineplex Entertainment: https://www.cineplex.com/

4. What is the trend in profitability?

Only a single year of income data is presented in the case (**Exhibit 12**), but it seems reasonably clear that the long-term outlook is a downward trend in profitability unless the initiatives to increase revenues in excess of costs covered in the final section of the case come to fruition. Decreased attendance = decreased concessions and advertising, and increased costs as theaters seek to go digital (which may not help anyway). The environmental factors too are all negative: improving screens at home, improved sound, no interruptions, decreased release windows, more options for viewing content outside of theaters, and so on. Overall, this is not a pretty "picture" for exhibitors.

The one area for potential improvement rests in consolidation which may provide exhibitors with some increased negotiating leverage for film rental rates. Current rates average about 54% in the industry, and are 53.56% among the leading domestic circuits (AMC, 53.2%; Regal, 53.7%; Cinemark, 53.8%; Data from **Exhibit 12**).

Given AMC's scale (15.0% of U.S. screens compared to Regal's 10.3% and Cinemark's 6.2%), the benefits of scale in negotiating film rentals rates may be small. AMC's rental rate is just 0.55 percentage points below the average of Cinemark and Regal. The 0.55% advantage on AMC's box office admissions of $2.049 billion yields a savings of just $11.3 million. This does provide AMC with a slight advantage, so their lower profitability is puzzling. This may increase as the consolidation of Carmike's operations increases, but suggests that the true bargaining power in setting film rental rates remains with the studios due to their differentiated content and their control over it.

If AMC, or any firm, were able to increase their negotiating power to the point of dropping rental rates to 50% (a 6.6% reduction), it would yield savings of $132,000,000 for a major circuit with $2 billion box office revenues.

Follow-up Question: What explains this trend?

The environmental trends are all negative. Exhibitors may reasonably expect continued declines in per capita viewing, and may see increased box office gross, but expect a continuation of relatively flat ticket sales. Key *causes* of this are:

- Low/no growth in their core audience
- Home theater options getting better, growing substitute
- More ways to view movies outside the theater
- More great content beyond movies
- More general entertainment options

Television is not likely to spontaneously self-destruct. Within the current business model there is little opportunity to increase either revenues or profits. Key *causes* of this are:

Box Office Receipts—Studios take nearly 55 percent of every box office dollar. All the power rests with the studios that supply, advertise, and control the motion picture content, and could conceivably go directly to viewers through DVD and electronic distribution. Exhibitors have some additional negotiating power due to consolidation (only for the major circuits), and less power as studios see more revenue from international sales and studios try to replace lost DVD sales (e.g., through video premium on demand; shortened release windows). Some established theaters, and many new entrants, incorporate premium seating with substantially higher ticket prices. These prices deter the teen audience and are aimed at increasing revenue and increasing the experience for older audiences. Exhibitors are also trying to incorporate more alternative content to reduce the bargaining power of the studios and increase revenues at underutilized times, but this is a long-term initiative.

Concessions—Need more attendance, increased per capita spending, or increased prices. The first cause is outside the theaters' control. It is mostly the movie itself; per capita could increase with lower prices or new items. Many theaters are seeking to increase per capita spending by adding higher-priced and gourmet food items, but overall concessions per ticket have not changed dramatically.

Advertising—Walking a tightrope. More ads likely equated with decreased attendance among those with home theaters already. Exhibitors are trying to make them more effective (so they can charge a higher price per ad) and "fun" (so as to increase revenues while (1) not decreasing the appeal of the theater experience or (2) make it an enjoyable aspect that patrons might look forward to).

5. **Do trends in the general environment and industry structure affect profits**?

GENERAL ENVIRONMENTAL ANALYSIS

Demographic—Little increase in the size of the population that is the core audience.

Economic—Historically, economic declines have resulted in increases in theater attendance, but with widespread home viewing options, this may not continue. In 2017, unemployment is very low and the stock market hitting highs. These indicate a positive economy which may negatively affect attendance.

Sociocultural—Movies continue to have a large following, constituting one of the main types of viewable entertainment. However, the availability of movies outside of theaters has increased faster

than increases in going to the movies. Additionally, television offers content which rivals movies. Binge viewing an entire season of a show may be the equivalent of watching four, six or even eight movies or more, keeping potential attendees out of the theater. Teens continue to have a limited number of entertainment options, yet seek time together outside of the home for dating.

Political—Content piracy is a growing issue for movies. Attempts at legislation may deter, but have not eliminated this illegal substitute. This is primarily an issue for seeing the movie as opposed to going to the movies as a social activity.

Technological—Rapid rate of creation and adoption of technologies for viewing movies outside of theaters (computers, home UHD/4K television, HDTV, iPads, DVR, etc.) combined with a rapid increase in the number of distribution formats (streaming, VOD, and even DVDs) and distribution means (physical, web-based, satellite-based). Each increases the ability of viewers to watch movies outside of the theater and allows forward integration of studios (direct studio to viewer, circumventing the exhibitor).

Global—Global market for paying movie viewers is growing rapidly. Seventy percent of motion picture theatrical box office revenues now come from outside the U.S. This puts the attention of studios on global makes as opposed to domestic.

Historically, the only domestic circuit operating outside of the U.S. and Canada was Cinemark. In 2016, they had 1,344 screens in 187 theaters outside of the U.S. That number is little changed in recent years. In 2012, AMC was purchased by Wanda, a Chinese conglomerate, which may signal a shift in global consolidation among exhibitors. Wanda/AMC have continued acquisitions with Carmike domestically as well as Nordic and Odeon in Europe and Hoyts in Australia. AMC's domestic operations (819 theaters; 8,293 screens) is virtually equal in size to non-U.S. operations (862 theaters; 7,087 screens). With studios increasingly relying on revenues from outside the domestic market, consolidation among the circuits may result in greater buying power.

PORTER'S FIVE FORCES MODEL OF INDUSTRY ANALYSIS

From the following analysis, the movie exhibition industry faces many powerful forces that undermine its profitability. The only positive force is the lack of new entrants in the domestic market. However, the international market has many competitors and new entrants searching for ways to reap higher bargaining power over the suppliers (studios). Since many movie studios count on the global sales of movies, larger multinationals that have increased bargaining power may be an effective approach to changing the negative pressures identified in the following analysis. Still, the lack of switching costs, the new readily adopted substitutes from streaming content sites, home theaters, and mobile platforms are sizeable odds that stack against exhibitors even if they amass global bargaining power through consolidation. The picture is not perfectly clear, but the options for the current business model are definitely limited (see **Exhibit TN-5**).

6. (Advanced) For questions 1 through 5, which of these are symptoms? Which are causes?

It is best to mention whether issues are causes or symptoms while discussing each issue (see identified cause(s) and symptom(s) in earlier discussions).

7. Are the recent exhibitor initiatives helping to change the profit picture for exhibitors?

Profitability for movie exhibitors has increased in recent years. Attendance for 2016 was down, ticket prices increased, and profits increased. Motion picture rental rates remain steady. Therefore it is reasonable to conclude that at least some of the exhibitor initiatives are having an effect, perhaps even if pricing along. Attribution as to the cause is not entirely possible. However, in a 2014 market analysis, Mintel reported results of a poll the prices individuals would be willing to pay for specific theater accoutrements including which could aid determination:

- Seating: A sofa ($1.92), luxurious seating ($1.71), footrest ($1.71), and additional legroom ($1.66)
- Food: In-seat ordering ($1.81) and a seat tray for food ($1.68)
- Experience: Adults-only showings ($1.79), an unobstructed view ($1.75), and ideal viewing location in theater ($1.70)
- Immersion: 4D ($1.88)

Which of these specific initiative or initiatives is impacting profitability is not possible. When analyzing these initiatives, it is crucial to pay attention to both sides (revenues and costs) of introducing any initiative. The cost side of many of these initiatives is not reported. Equipment innovations have shown that the ability to recoup these investments have a very short window. Alternative content holds promise but it also needs to draw more attendance on a consistent basis (i.e. a series of concerts or Broadway shows). Immersion experiences are very similar to equipment innovations; however, integrated theater and seats for home theater viewing involves more and different value chains coordinated together – leading one to believe the likelihood of that response would be slower. Enhanced concession initiatives are promising but cost containment is essential (see example illustration in Question 4, Concessions). Similarly, VIP movie viewing holds promise if the costs to renovate and more limited attendance are offset by increased spending per attendee over costs. Reserved seating and dynamic pricing are initiatives that have little to no cost but huge revenue improvement implications. However, dynamic pricing as seen with Uber's surge pricing, can rub people the wrong way. Is it the same movie that everyone else will see next week?

What types of business-level strategies can you identify for exhibitors?

Rural are more cost-leader oriented. Differentiation in technology (digital, 3D, 4D, IMAX, etc.) is short-lived and competitors adapt quickly to respond. Recent attempts by exhibitors to differentiate center around different concession options (full dining), seating changes (VIP, reserved, adult-only, etc.), differing content (Metropolitan Opera), or to luxuriate the entire experience (i.e., iPic, Cinépolis). However, none of these differentiators have been fully adopted across all theater chains. Perhaps none will be fully incorporated into every theater or across every screen, but rather employed by circuits selectively into individual screens and theater locations based upon an analysis of expected return.

8. (Advanced) What effect will consolidation have on the domestic exhibition industry? The global exhibition industry?

Consolidation in an industry is quite common once it reaches maturity. Under a life cycle perspective, maturity is signaled by prolonged periods of slowing growth, typically coupled with homogeneity

amongst products or services as innovations are adopted by all firms in a market. Decline is indicated by reductions in demand. Many industries peak, but never actually decline. The trend in the domestic exhibition industry suggests the industry has matured, perhaps entering into a decline stage.

Consolidation of an industry brings about several benefits including increased bargaining power of combined firms, cost rationalization, and reduction of excess capacity. The bargaining power of the combined firms with suppliers is the primary benefit of consolidation in the exhibition industry. In the box office revenue channel, AMC benefits from film rental cost which is 0.55 percentage points lower than rivals. Caution is warranted, however, as the studios supplying the films are also highly concentrated, have highly differentiated inputs essential to exhibitors, and could potentially disintermediate the exhibitors through VOD and direct release. Other bargaining power benefits include increased power on all concession supplies, but the potential may be limited as these are mostly commodity products. Cost rationalization may be achieved through reduction in the number of parties involved in rental agreements and licensing. AMC, for example, estimated cost savings of $35 million (Lang, B. (2016, March 3, 2016). AMC Acquires Carmike Cinemas for $1.1 Billion, Making It World's Largest Theater Chain. Variety.).

In the exhibition industry excess capacity is limited as studios have limited over investment through the use of "clearances" which restrict the licensing of films in overlapping geographic markets. For example, Regal may have the right within five miles of any of their theaters, eliminating the potential for a start-up theater to enter near their location. Cost rationalization, such as airlines eliminating multiple flights to a city pair with each underutilized, do not really apply.

9. What is the strategic issue facing all competitors in the domestic movie exhibition industry?

ANNOUNCE: "OK, we now have a pretty good inventory of the situation. Are there any major points we have missed? Can we make sense of this? Are these all unique things that are simultaneously occurring or is there a way that we can summarize them into one or a couple of strategic issues?"

The challenge for framing all strategic issues is determining how to do so in a manner that is both specific but does not constrict potential actions. The most comprehensive approach is something along the lines of the following:

> Strategic Issue for Exhibitors: How to create unique value in the movie exhibition business in the age of home theaters (HD, large screens, and widely available content) that produces profits?

Now we start considering profits—that is the *outcome* we are seeking. List this as earlier, and then cross out the word "~~movie~~" leaving just "exhibition business." Compare this to "how do we compete in the ~~horse and buggy~~ *transportation* business? The point being, exhibitors need to redefine their role in the entertainment ecosystem.

Other aspects that students may want to include:

Suggestion for Inclusion	Counterpoint
Limited growth in the size of the core audience (low growth in customer base of 12 to 17 and 18 to 24-year-olds)	Just because the business has relied on this group in the past, must we make the same error in the future? Isn't this audience also already covered in the earlier discussion in a general sense?
"Return to the golden age of theaters"	Can you go back with all the new technology and content availability?
"Make the experience better"	Is the attendance decline due solely to bad experiences within the theater? Or does increased technology and places to view content affect it as well? Order of causality? Which is the cause? Which is the effect?
"Increase revenue"	The business has focused on this for years—remember the box office records—but has it fixed the underlying problem?

ANNOUNCE: "Good start. We are now at the stage that every junior stock analyst can reach. Now to earn our keep as managers, what actions can an exhibitor take to resolve the strategic issue(s)?"

You want to assess: the degree to which these could potentially resolve the issue. What do they resolve well? Where do they fall short? What are the costs? Do we have the ability to implement them? How can it be done?

Note that the following are actions currently being undertaken by the theater chains. Students will likely raise others.

- **Exit: Close the Theaters**—This is likely a premature option. 1.3 billion tickets sold, $13.4 billion (domestic) industry. Let's try to improve it before abandoning ship.
- **Eliminate Other Ways of Viewing Movies**—Studio revenue is tied to the aftermarket of streaming, VOD, DVDs, and other items. They will not go for this. Generally, it is hard to put any genie back into a bottle.
- **Just Charge More for Tickets**—Ticket prices have recently exceeded the rate of inflation. One factor keeping people away from the theater is cost. Simply charging more for the same experience will keep people away from the theater. Exhibitors must lower costs and/or increase the appeal of the theater to attract additional attendees. Doing either does risk lessening the appeal for the current audience.

Just Charge More for Other Items—As blanket propositions, these are bad. Box office prices and concessions are about at a maximum, as are concessions for the income averages of the population. In an environment with viable substitutes, you can't expect to simply increase prices without providing

additional value added without incentivizing customers to consider those substitutes, resulting in losing revenues. There are variants of price increases listed in the following, but these are coupled with increased food quality or a box office revenue management model (lower prices for some showings, higher for others).

REVIVE THE EXPERIENCE: GENERAL

- **Decrease Interruptions**—Theater chains are adding more ushers and better scheduling show times and theaters (think loud movies next to loud movies). Others are working with technology firms to introduce equipment to jam cell phones (this is currently illegal under U.S. federal law).

  Resolves the strategic issue? **Partly**—May reduce bad behavior and interruptions (reduces the reasons people stay away), but doesn't give them a new reason to go to the theater.

- **Focus on 3D**—Students should recognize that 3D was to be the next great thing for exhibitors and studios. At the start of 2015, it appears that 3D movie revenue has already peaked. Even so, theaters generally do not control the content and thus rely on downstream studios for attractive content.

  Resolves the strategic issue? **Unlikely**—Theaters once saw 3D as a technology that could not be countered at home, but 3D television sets quickly became available. Plus, not all movie types translate well to the 3D format. Demand appears to have peaked based on ticket sales.

- **Focus on Immersive Experiences**—Students should recognize that 3D is just one type of immersive experience along with 4D which includes motion seating and off theater effects. At the start of 2017, 4D is becoming more widely available in select screens in select theater locations. It is important for students to recognize that immersive technologies, at least at this point, would not be rolled out into every screen in every theater. Rather, it is likely one screen in theaters in select markets where demand would be sufficient. This is niche, or focused, differentiation.

  Resolves the strategic issue? **Selectively**—Immersive experience overall could be a draw, or seen as a gimmick, for a small, select audience. At a surcharge of $8–$12 per ticket, ask the students how often they would choose this as a viewing technology. Once? Or every time?

SELECT IMMERSIVE EXPERIENCES

- **Smell-O-Vision**—This gimmick really existed. The 1960s innovation involved pumping smells into the auditorium. Think of the swamp smell in a Disney theme park ride. Not expected to return.[1]

  Resolves the strategic issue? **Unlikely**—May create a whole new reason for audiences to stay away. Think sports flicks! Nickelodeon's 4D experience at its resorts involves air hoses and sprays of water in short films (less than 15 minutes) with IMAX screens. Is it likely that mainstream movies will adopt such an involved system? Unlikely to resolve strategic issue due to installation costs and additional time in movie production to set cues for rushing air or sprays of water (envision *The Perfect Storm* shown with these effects).

- **Interactive / motion seating**—Motion seating adds to the experience. This is popular in some international markets and becoming popular in the U.S. It seems like a gimmick audiences might quickly discount as a novelty. What percentage of audiences is susceptible to motion sickness? How much would viewers pay per ticket? How much would it cost to install? To maintain? Again, only certain types of movies are appropriate for this type of experience (action). Some U.S. theaters have adopted this experience. D-Box is the leading provider of motion effect seating (MFX) for commercial and home use: URL: http://www.d-box.com/en/consumer/theater_movies

  Resolves the strategic issue? **Selectively** —May be a select market willing to experience this, but unlikely to be a draw on a regular basis. It is already available for in-home theaters.

- **Enhanced audio**—Dolby's Atmos system offers more sound "zones," including speakers in a theater's ceiling. When incorporated into soundtracks, it could make for far more realistic surround sound. Video URL: https://www.youtube.com/watch?v=oGgwDkwF03s

  Resolves the strategic issue? **Unlikely**—May be a temporary draw for some who really value the sound experience; possibly one viewer segment would pay a small premium for it. If adopted, this would eventually be part of the standard viewing experience, much like surround sound now is. Audio receivers for home theaters are now available which emulate Atmos with 5.2, 7.2, 9.2, and 11.2 home theater systems. Those most likely to value this would seem to be those most likely to have the equipment at home.

- **Expanded Services**—Increased service touchpoints such as babysitting, valet parking, ushers, order-from-your-seat food service, and so on. Generally, attempts to transition the industry back to a service industry. Upside: Some will find real value in these, but will enough moviegoers find these valuable? And do so consistently enough? Some can be met outside the theater—upscale malls offer valet services. Others in the theater—babysitting—need new facilities, staff, a new regulatory environment, and other items in a largely no-load / peak load business.

  Resolves the strategic issue? **Partly**—Some will find value in these services. Reduces the reasons why some people stay away from theaters, but these services really do not seem to give audiences a new reason to go to the theater.

- **Go Upscale**—The VIP approach is being rolled out in both mainstream theaters (AMC, for example) as well as specialty chains (iPic Theaters and Cinépolis, for instance). Think airline first class—still on the plane, but much more comfortable than coach. Two approaches:

  1. **VIP Experience**—Individual theaters within a complex are designated as VIP areas, accessible only with a premium-priced ticket. From plush, assigned seating with waiter service to couch-style atmospheres with usher service, this approach seeks to mimic a private screening room, even offering reserved seating in some locations. At Cinépolis in Jupiter, Florida, for example, patrons can select 21-and-over screens, 3D, and fully reclining luxury leather seating.

     http://www.cinepolisusa.com/locations.aspx

     Your $23.50 ticket includes parking, 3D digital projection, and seating-side ordering. Many larger chains are experimenting with this model with their own locations.

The large circuits are pursing this approach too. AMC Theaters offers "Cinema Suite" (age 21 and older) and "Fork and Screen" (18 and over or accompanied by a parent).

AMC full service experience overview (News report): https://www.youtube.com/watch?v=esph1V4DKt4

AMC in-theater dining menu available at: https://www.amctheatres.com/food-and-drink/dine-in/full-service

AMC premium seats available at: https://www.amctheatres.com/recliner-seating

AMC reserved seating available at: https://www.amctheatres.com/reserved-seating

Tickets: $16.49 in Framingham, Massachusetts (May, 2017) for admission to 3D, reserved seating, in a dine-in theater. Food and drink not included. Price does not include $3 "convenience fee" charge for reserving seats.

2. **The VIP Theater**—Solely upscale location. iPic Theaters is one example. The theater lobby looks more like a high-end hotel than a cinema. Features include memberships, custom seating with optional footrests, complimentary pillow-and-blanket service, in-lobby restaurant and in-theater service, even a by-the-glass winetasting station. Theaters are in upscale locations, including Scottsdale, Arizona, Boca Raton, Florida, and Redmond, Washington. Premium seating: $25.00 ($16 ticket + $9 VIP fee) for a Friday feature in Bolingbrook, Illinois.

   URL: https://www.ipictheaters.com/

   Video Tour or Manhattan, NY opening: https://www.youtube.com/watch?v=wTPuCD4K8KE

   Upside—Re-differentiates the industry (at least for some). Follows the club VIP model (but that's waning). With a restaurant and full bar, it makes the theaters a destination. iPic markets this as "Come for the drinks, stay for the movies."[2] Separates the seating surcharge from the box office admission. May be a way to reduce the rental charge due to studios.

   Downside—What to offer and how to do it in an economically viable way? Reconstructing theaters can be very expensive. Is this about the movie at all? Some in the industry are skeptical of the all-luxury concept. Michael Whalen, president of the firm that operates the Oaks 14 multiplex, says "The idea of an all-premium concept strikes me as a recipe for disaster."[3] Yet, iPic and Cinépolis continue to expand.

   Resolves the strategic issue? This option can resolve the strategic issue for exhibitors that seek differentiation while adding a whole new level of "experience" to the theater experience. Most viable in exhibitors that target upscale markets for adult, professional audiences.

REVIVE THE UNIQUENESS OF THE EXPERIENCE: CONTENT

- **Go Beyond Motion Pictures**—There are no technical reasons that theaters, with digital projection and satellite or Internet content distribution, cannot show non-movie content. Look for more concerts, sporting events, television season openers and finales, corporate and

shareholder meetings, and other "events" to appear at your local theater. The NFL, NBA, and college football are among those who have experimented with broadcasts of sporting events to digital theaters. Content is now readily available through companies such as Cinedigm (http://www.cinedigm.com) and Fathom Events (https://www.fathomevents.com/). Some sports broadcasts have been offered in 3D.

Most exhibitors seek to incorporate alternative content in ways that attract new attendees during off-peak times, particularly Monday through Thursday when only five percent of theater seats are occupied.[4] A theater achieving 20% of box office revenues from non-movie event content would be an industry leader. Some new entrants into the exhibition industry are making filling these seats with viewers of alternative content a central aspect of their business model.

Bud Mayo, CEO of the former Digiplex (acquired by Carmike), described the approach: "What happens with those [alternative content] performances is that a single event will out gross certainly the lowest-grossing movie playing that theater that day, but in practice [it will] have averaged more than 10 times the lowest-grossing movie for the entire day."[5] In marginal dollar terms, alternative content can be a boon on otherwise slow nights. A recent Wednesday showing of Broadway's *West Side Story* at a Digitech theater had an average ticket price of $12.50 and grossed $2,425. In comparison, films that night grossed from a low of $56 to a high of $73. In addition to a larger box office, the show brought in nearly 200 additional viewers who might purchase concessions. Digiplex's goal: Expand alternative content from 2012's eight percent to 20 percent of box office receipts and reach 1,000 screens in the top 75 U.S. markets.[6]

URL: http://www.dcdcdistribution.com/

Cinedigm URL: http://www.cinedigm.com

Fathom Events URL: https://www.fathomevents.com/

Ticket prices typically $12.50–$25 per event.

Upside—Largely untapped revenues. This option may bring in non-peak audiences (Sunday afternoon, Monday night) when only five percent of seats are filled.

Downside—want to watch the Superbowl in a dark theater for four hours? Beer (some theaters licensed for beer sales, others are required to get special one-day permits), social aspects (stuck in theater seat versus moving around; Is talking permitted?) This approach may need VIP-type areas to fully work. How to get audiences in on a *regular basis* Monday through Thursday?

Resolves the strategic issue? —**Possibly.** Has a real possibility to resolve the strategic issue. This may be the only option that reduces dependence on the film studios and may, over the long term, reduce costs.

10. (Advanced) What are the requirements for implementing your recommendations, and what positive outcomes should be expected?

Many of the options listed earlier require additional investments in equipment that need significant capital and must generally use existing space. Caution the students to think of the recommendations as the CEO rather than as a movie attendee. For recommendations that have additional equipment investments required, but have enhanced revenue associated with those investments (i.e., VIP theaters), it is important to have students recognize the scale of investment based on the enhanced revenue options. Take one chain and determine the cost to renovate one screen per multiplex and extrapolate out to the number of multiplexes for that chain. Students should then realize the capital necessary to implement a recommendation, seeing it from the financial position of movie exhibitors and the scale of their operations. General factors: costs, locations, maintenance and upkeep, user reaction (short-term versus long-term willingness to pay).

Recommendations that involve service upgrades, such as increased food offerings and alcoholic beverage services should consider the cost of investment, differences in operating margins compared to existing highly profitable concessions, very high utilization during the peak Friday and Saturday night timeslots versus very low utilization at other times. Permitting, licensing, and space for facilities are also factors.

Recommendations that involve alternative content need to consider equipment, content availability, and how to attract an audience (especially during off-peak times). The recent entry of firms, such as Digital Cinema Distribution Coalition (DCDC) which provides a network for content distribution, and Fathom Events, an intermediary / distributors of alternative content make this a far more viable option than just five years prior.

URL: http://www.dcdcdistribution.com/about-us/

URL: https://www.fathomevents.com/

Additional Resources

Additional materials useful for the instructor are notes under each question.

EXHIBIT TN-1 LCD TV Price Trend

Year	32" LCD Retail Price
2005	$1,566
2006	$873
2007	$729
2008	$580
2009	$511
2010	$374
2011	$319
2012	
2013	
2014	
2015	
2016	
2017	Forecasted price in 2017 using "power" forecast option in Excel should be slightly over $200

Source: The data: CNN Money Magazine reported in 2010 on the falling prices of LCD screens. URL: http://money.cnn.com/2010/11/24/technology/lcd_tv_deals/#

EXHIBIT TN-2 DVD Release Window Trend

Year	Release Window (DVD is available for purchase)	Announcement Window (Announcement of the date on which DVD will be available for purchase)
1997	24.6	16.0
1998	24.7	16.6
1999	24.0	15.7
2000	23.7	15.7
2001	23.1	14.6
2002	22.6	14.4
2003	21.0	12.3
2004	20.0	10.3
2005	19.7	10.0
2006	18.7	9.1
2007	19.9	10.7
2008	19.1	10.0
2009	18.7	10.0
2010	18.9	10.0
2011	17.9	9.9
2012	17.7	9.3
2013	17.3	9.3
2014	16.6	8.4
2015	16.0	8.6
2016	15.4	7.9

Source: National Association of Theater Owners (2015). Average video announcement and video release windows. natoonline.org. http://natoonline.org/wp-content/uploads/2013/07/Major-Studio-Release-Window-Averages-4.3.15.pdf

EXHIBIT TN-3 Concession Sales and Costs by Circuit

Circuit	2012		2016	
	Concessions per attendee (not included in the case)	% of Frequent Moviegoers[1]	# Increase per Existing Screen[2]	% of New Admissions
AMC	$3.55	13.7%	$4.82	13.9%
Carmike	$3.10	13%	Now part of AMC	Now part of AMC
Cinemark	$3.34	13%	$4.19	15.6%
Regal	$3.46	14%	$4.42	12.8%

Source: Data from company SEC filings.

EXHIBIT TN-4 Concession Cost and Profit Scenarios

Example circuit with 2016 Admissions of 100,000,000	
Scenario 1: 2012 Concession Levels and Costs	
Revenue @ 2012 concession levels ($3.35 / admission x 100,000,000 admissions = $335,000,000)	$335,000,000
- Concession costs @ 2012 concession cost average of 13.5% ($335,000,000 x .135 = $45,225,000)	- $45,225,000
= Operating profit on concessions (Revenue – costs = $289,775,000)	= $289,775,000
Scenario 2: 2016 Concession Levels and Costs	
Revenue @ 2016 concession levels ($4.50 / admission = $450,000,000)	$450,000,000
- Concession costs @ 2016 concession cost average of 14.0% ($450,000,000 x .14 = $63,000,000)	- $63,000,000
= Operating profit on concessions (Revenue – costs = $387,000,000)	= $387,000,000
Increase in profit = $97,225,000 ($387,000,000 - $289,775,000)	$97,225,000

Source: Author calculations based on analysis of SEC filings of multiple exhibitors.

EXHIBIT TN-5 Forces Undermining the Profitability of the Movie Exhibition Industry

Factors Leading to...	Threat of New Entrants	Power of Suppliers	Interfirm Rivalry	Power of Buyers	Threat of Substitutes
High threat	Customer switching costs are low	Suppliers cannot legally forward integrate Few suppliers for most conten Content is unique to each supplier Continued reliance on studios and motion pictures	High exit barriers Undifferentiated products	Products are undifferentiated based on source of supplier Buyers have no switching costs Little buyer loyalty Increasing variety of substitutes	Television size growth Streaming technology and adoption of mobile devices Content widely and increasingly available
Moderate threat			Slow industry growth Limited demonstrated commitment for exhibitors to show alternative content		
Low threat	High capital requirements Saturated domestic market Industry consolidation	Incumbents face low switching costs High short-term risk to studios if they eliminate exhibitors	Fewer industry competitors Financial instability	Multiple small buyers Buyers purchase in small quantities Buyers are not likely to backward integrate	Other activity / location options for a teen date?
Low threat	Low; real threat is substitutes	Very high; The leading cause of industry's low profitability	Moderate; High when theaters located in same geographic area	Moderate; increasing	High; continuing to increase

Source: Courtesy of S. Gove.

Endnotes

1 Sources on Smell-O-Vision: T. L. Stanley, "To boost attendance, industry seeks Smell-O-Vision sequel," *Brandweek*, 49, 12 (March 24, 2008) 8. Also see the University of Florida, George A. Smathers Libraries, The Belknap Collection for the Performing Arts, accessed January 5, 2009, http://www.uflib.ufl.edu/SPEC/belknap/exhibit2002/smell.htm.

2 iPic theaters. Accessed February, 2013, https://www.ipictheaters.com/default.aspx.

3 Friedman, J. "Upscale chain aims to be the BMW of movie theaters," *Los Angeles Times*, September 7, 2008.

4 Investor Presentation: Jefferies 2012 Global Technology, Media & Telecom Conference. Cinedigm. Accessed May 2012, http://files.shareholder.com/downloads/AIXD/2302444840x0x567367/4a213e2c-11ae-4cdc-8dd1-970919ac80ac/CIDM%20IR%20deck%20050712%20Short.pdf.