

China Film Industry Report 2012-2013 (in Brief)



I Research Background

In 2010, the State Council of China issued a series of guidance for film and cultural industries, which gave significant support to the development of Chinese film industry at the macro policy level. At the end of the same year, it was announced that the cultural industry would be developed as a pillar industry for the national economy. China's film industry has achieved rapid growth in this condition.

In 2012, the Chinese film industry showed exponential development. Total film box office revenue exceeded 17 billion Yuan. Film production and financing, and cinema investment and construction all rose to a new level, attracting substantial capital to this field. In essence, the Chinese film market has come to a golden age. Also, accompanied by film technology innovation and rapid growth of its viewer-base, the constitution of moviegoers and their viewing preferences and ways to receive information have all undergone significant changes compared with previous years.

In this environment, series of challenges emerges, such as how to seize investment opportunities in the rapidly growing market, how to improve the competitiveness of domestic films and how to understand the tastes of audiences. To help companies in film industry get a comprehensive understanding about the status and features of the Chinese film industry, EntGroup presents the China Film Industry Report 2012-2013 based on in-depth research, analysis and interviews. The report is the fifth such annual report presented by EntGroup since 2009.

II Research Scope

This report will focus on the Chinese film industry in 2012-2013. In this report, the Chinese film industry refers to the mainland China film industry, and does not include the industries in Hong Kong, Macau and Taiwan.

III Methodology

This report adopts both quantitative and qualitative methods, and combines revenue figures of the film market to conduct the research on the Chinese film industry. The statistics used in this report are primarily from figures gathered by the Computer Ticketing Network Centre of National Film Special Fund Office, and announced on China Film News, while the market ranking data was obtained from the China Film Exhibition & Distribution Association, and from data provided by major cinema circuits in the country. The above data were cross-referenced by interviewing major cinema circuits and distribution companies. All the figures and statistics used in this report were obtained from more than one source, and they were repeatedly vetted and analyzed to ensure accuracy and authenticity.

IV The Report

1. Overall Analysis of Trends in China's Film Industry in 2012

1.1 Analysis of China's Film Industry in 2012

1.1.1 National Policy: Fewer restrictions on foreign films puts pressure on Chinese language films

In 2012, a new policy agreement between China and the US allowed for 14 “specialty” films (3D or IMAX) to be imported into China in addition to the 20 revenue-sharing foreign films already allowed. After this new policy agreement, the success of huge blockbusters such as “Titanic” and “The Avengers” brought a great blow to Chinese films at the box office.

In order to withstand this outside pressure, China has implemented policies that support domestic films. In 2012, the Chinese government increased funding to encourage theaters to screen Chinese films. It also implemented a new deal between Taiwan, Hong Kong and the Mainland for the co-production of films, and loosened restrictions on cooperation between Taiwan and Mainland China to further promote cooperation and production. It is hoped that co-productions between Taiwan, Hong Kong and Mainland China will increase interaction between these regions and will encourage the overall integration of Chinese language films.

2010-2012 Important Policies of the Chinese Film Industry		
Time	Policy	Content/Meaning
2010	Guidelines on promoting the prosperity and development of the industry	Identified the film industry as a strategic industry
2011	CPC's decision to deepen the reform of the cultural system, to promote socialist cultural development and prosperity	Re-emphasis on accelerating the development of the cultural sector
2011/3/6	Outline of the 12th Five-Year Plan for National Economic and Social Development	Clearly stated the "prosperity and development of cultural innovation and industry" is a vital component of the country's economic stability; in particular, the need to accelerate the building of cinemas in small to midsize cities in the midwest and to enhance international competitiveness and influence

2011/12/1	SARFT's guidance on promoting the coordinated development of film production, distribution and exhibition	<p>1. Theaters cannot take more than 50% of profit during first-round screenings; 2. Theater rental should not exceed more than 15% of box office revenue; 3. Theaters that sign on with theater chains should, in principal, sign for time durations of no less than three years; if a theater does enter into an agreement with a theater chain whose joint assets are more than 50%, the agreement may be renegotiated in order to be a part of the chain; 4. Operations of preshow ads revert to theaters; production companies will no longer operate ad placements</p>
2012/2/18	Memorandum of Understanding between US and China on WTO Related Problems in the Film Industry	<p>1. China will allow the import of 20 American films and an additional 14 3D or IMAX films; 2. Box office shares to the US will be increased from the original 18% to 25%; 3. Increase the opportunities for private companies to release imported films, and put an end to this monopoly held by SOEs in the past</p>
2012/12/1	Subsidize the creation and production of domestic high-tech films	The government will subsidize domestically produced and distributed 3D, IMAX and high-tech films, based on box office revenue.
	Refund policy for newly developed theaters	Theaters to be divided into three refund categories
	Subsidize the installation of digital projection systems	Theaters with a 45% or more box office gross revenue within the last year may also enjoy special subsidized refunds
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Table 1 - 1 2010-2012 Important Policies of the Chinese Film Industry

1.1.2 Economics: Cross-border M&A to be More Common

As China's economy becomes stronger, mergers and acquisitions are becoming the most effective way for Chinese companies to enter into and compete in the international market. Data show a total of \$11.7 billion USD in foreign investment in 2012, which was a 4.5% decrease over the previous year (excluding banks, securities and insurance figures).

2012 Mergers and Acquisitions in Chinese Film Industry

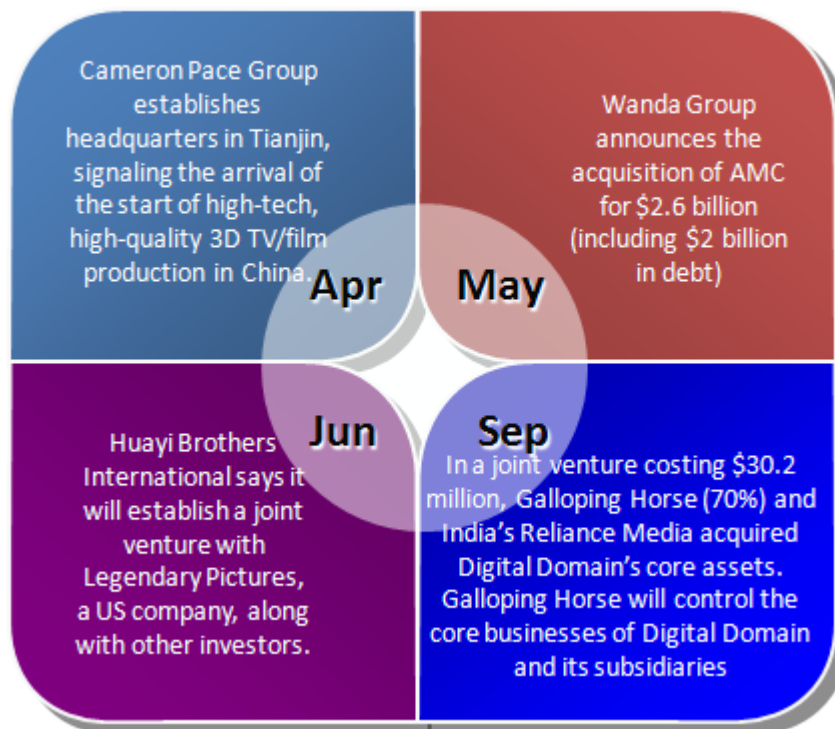


Image 1 - 1 2012 Mergers and Acquisitions in the Chinese Film Industry

As China's film industry continues to grow, it is inevitable that domestic film and television companies will look to expand overseas. By 2012, it had become a common trend for domestic companies to merge with or acquire large foreign companies.

Analysis by EntGroup shows that mergers and acquisitions of foreign companies have expanded from energy and manufacturing to the cultural sector. Acquiring foreign companies in order to expand internationally is a vital strategy for domestic companies. Through mergers and acquisitions, domestic production companies gain access to advanced technology, which compensates for their disadvantage in post-production, and helps domestic films compete with Hollywood productions.

1.2 Analysis of the Scale of the Chinese Film Industry

1.2.1 Overview of the Scale of the Chinese Film Industry

In 2012, revenue generated by the Chinese film industry totaled \$3.3 billion, an increase of 18%. Of this total, box office accounted for \$2.7 billion (a 30.18% increase over the previous year) while non-box office related revenue totaled \$45 million. Overseas sales continued to fall, generating only \$46 million. Projections for 2013 put film industry revenue at \$4.58 billion with hopes that box office generated revenue will reach over \$3.64 billion.

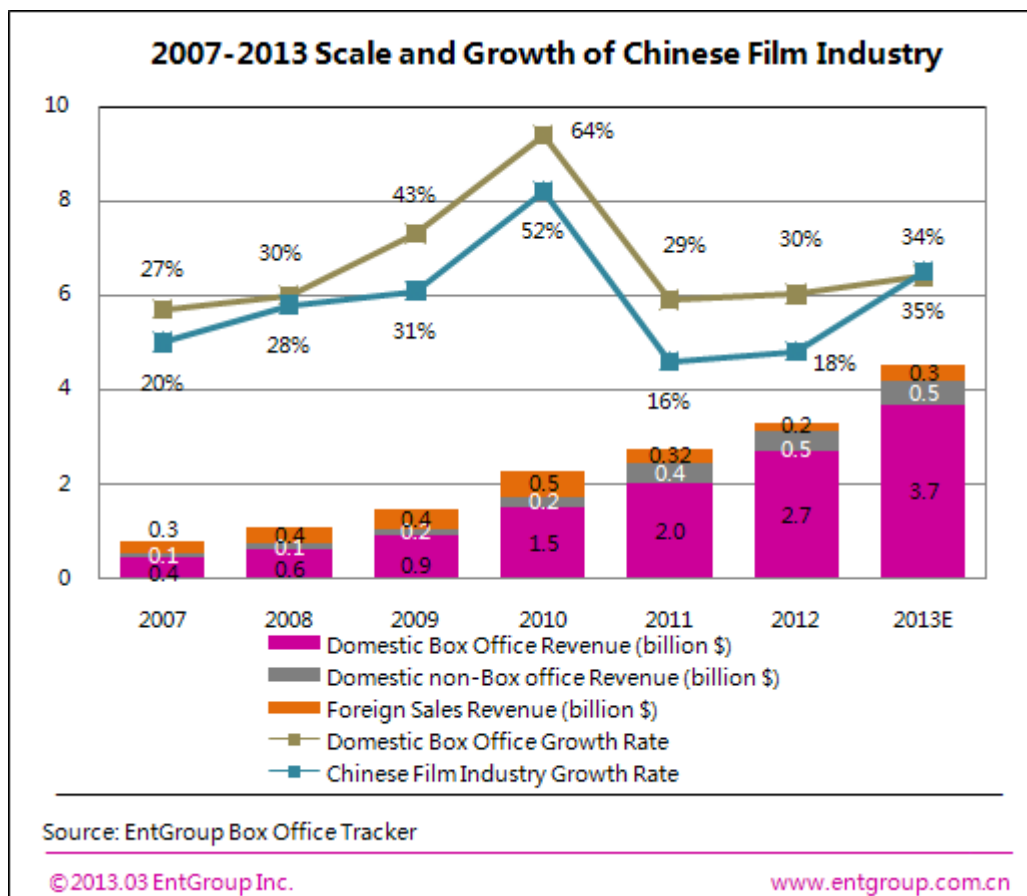


Image 1 - 2 2007-2013 Scale and Growth of Chinese Film Industry

1.2.4 Revenue from Film Advertising

Revenue from preshow ads and embedded ads continued to increase in 2012, with a 22% increase in revenue generated exclusively through preshow ads, while growth for embedded ads was slower at only 3%. Another major avenue used by films to recover investment funding was product placement. Revenue made through this avenue increased by over 85%, which was the same level as that for embedded ads.

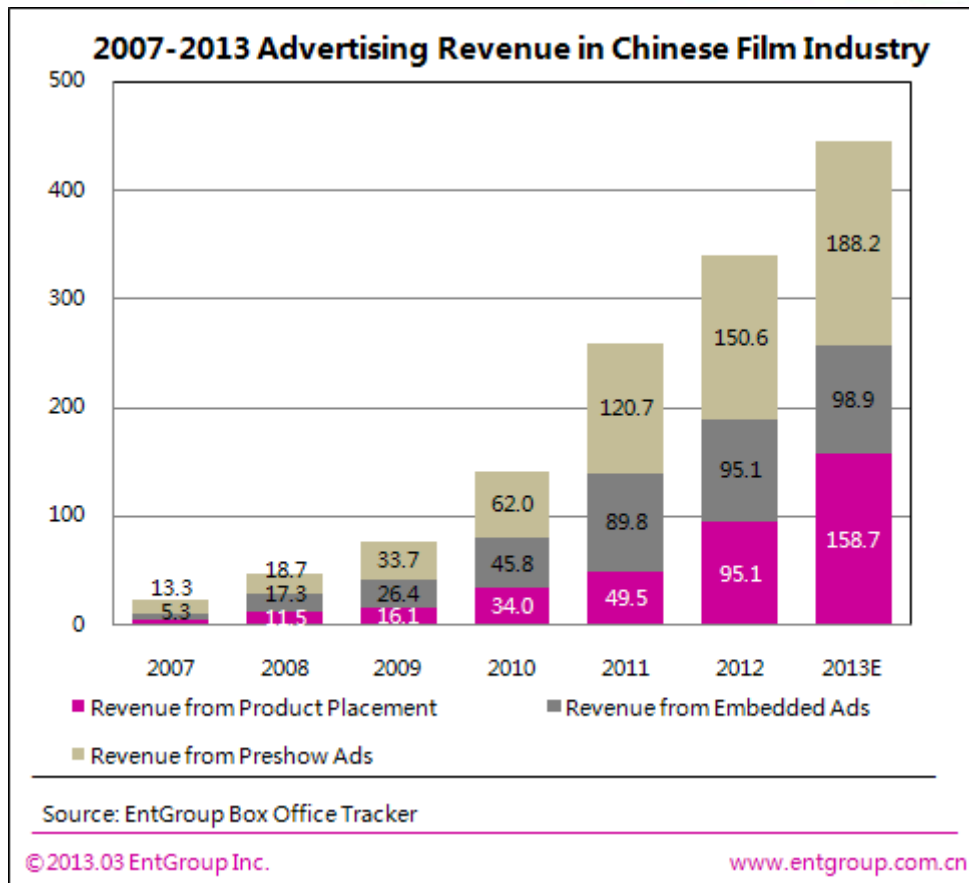


Image 1 - 3 2007-2013 Advertising Revenue in Chinese Film Industry

In 2011, the State Administration of Radio, Film and Television (SARFT) issued guidelines for “promoting coordinated development of film production, distribution and exhibition”, which states that the decision to show ads will be left to the theaters, and production companies will not be involved in embedded ads. These guidelines greatly influenced advertising revenue for 2012.

As business become savvier in terms of entertainment marketing, product placement revenue has risen from 2011 to 2012, approaching the same revenue levels earned from embedded advertisements. There have been a total of 144 examples of product placement in over 30 domestic films. Analysis of data from EBOT EntGroup Box Office Tracker shows that product placements appeared mainly in romantic movies in 2012, and mainly consist of ads for cars, food and beverages, online services, and financial services.

2 Movie Production in China in 2012

2.1 Overview of Movie Production in China in 2012

2.1.1 Analysis of Production Volume in China in 2012: 745 feature films were produced, 30% made it to theatres

In 2012, China produced a total of 893 movies, 745 of which were feature films, and set a new record by doing so. With a growth rate of 33.5%, this broke the trend of slow growth that had been continuing for the past few years. Of all the domestic films, 31% were screened in China throughout the year, which is also a considerable rise over the previous year. This shows that domestic film making has finally made the transition from its “hot money-driven” pattern to a more reasonable strategy last year. The clear rise in the number of films in 2012 shows that film market is on its way to recovery.

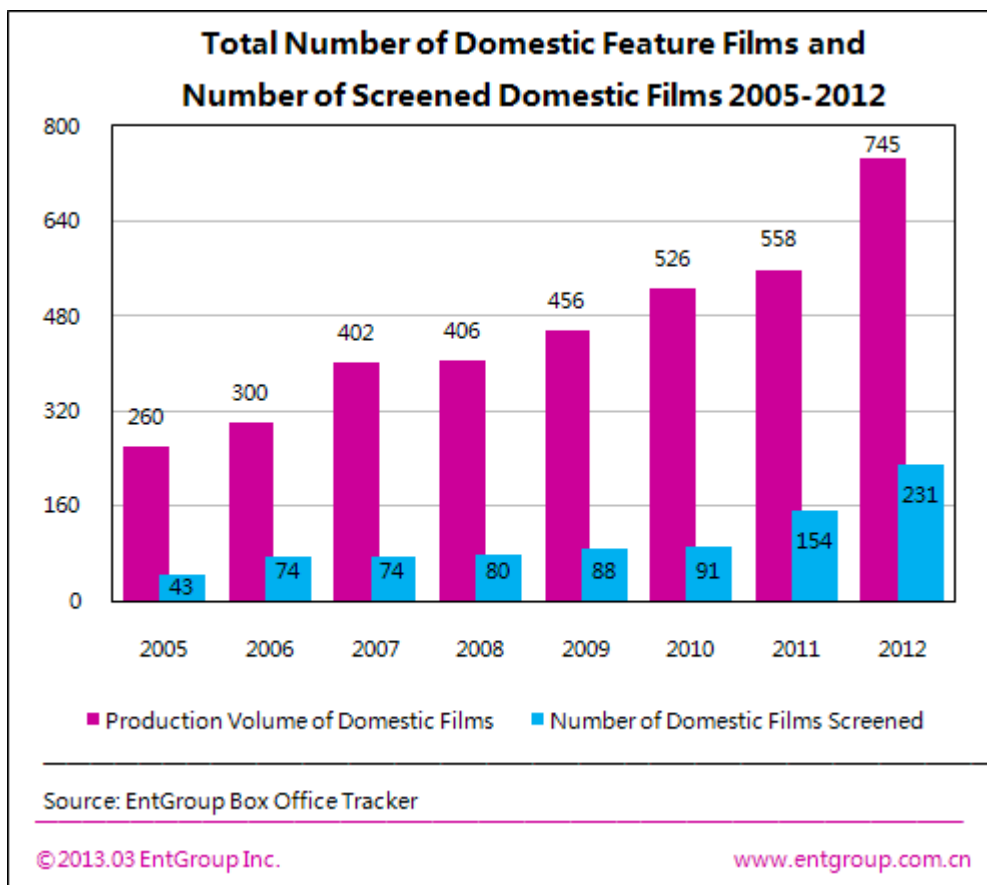


Image 2 - 1 Total Number of Domestic Feature Films and Numbers of Screened Domestic Films 2005-2012

2.1.2 Analysis of Chinese Movies in 2012 by Genre

EntGroup statistics show that of the 315 movies screened in China in 2012, the preference for traditional genres of

romance, action and comedy remained strong among audiences. Of these, domestic films were the most exemplary of this trend. Action films did the best at the box office, while comedies and romances took the top two places among domestic films. Worth mentioning is the unexpected rise of thrillers and animations among domestic films. Thrillers such as “Bixian Panic”, “The Zodiac Mystery” and “Nightmare” enjoyed comparatively good reviews and performed fairly well at the box office. This resulted in a 129% increase for domestic thrillers over last year and a gradual increase in the number of people willing to watch domestically produced thrillers.

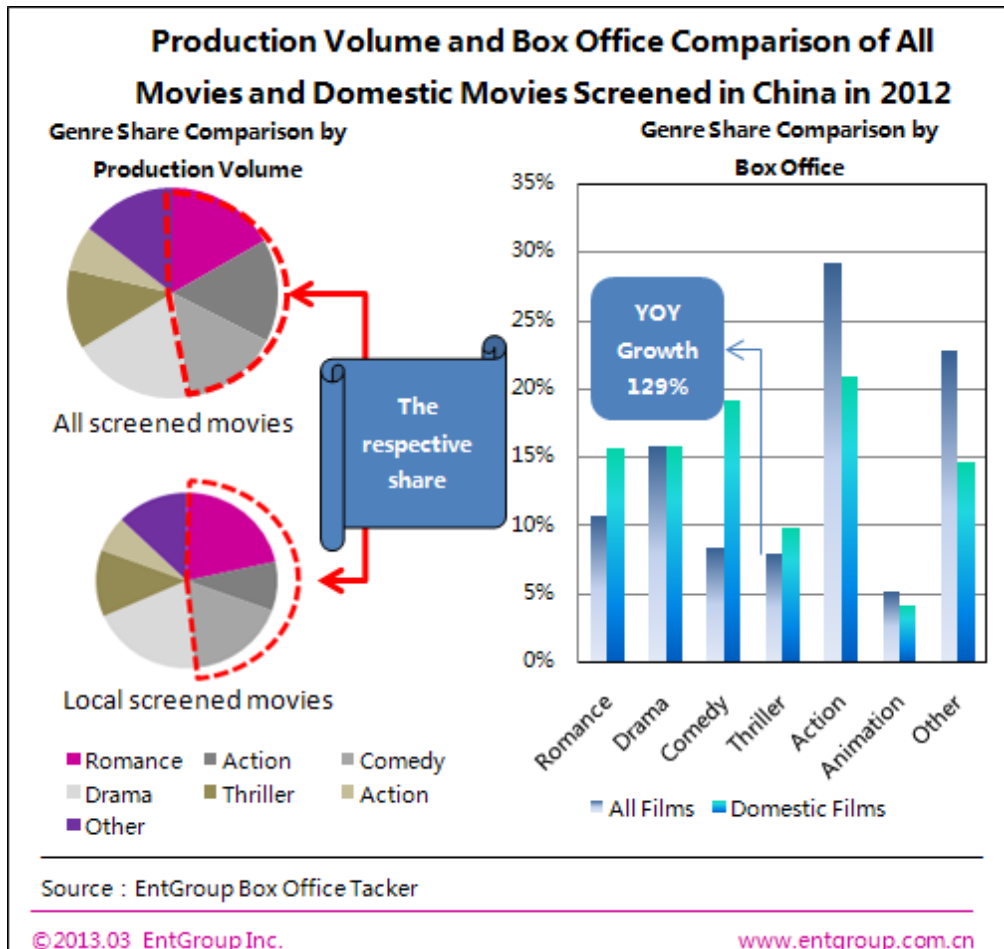


Image 2 - 2 Production Volume and Box Office Comparison of All Movies and Domestic Movies Screened in China in 2012

2.3.4 Overview of Co-Productions in 2012

Data from the EBOT EntGroup Box Office Tracker show that there were 67 co-productions filmed in 2012, with total box office revenues of \$672 million. Currently, co-productions are dominated by partnerships with Hong Kong for 40 of the year's films, taking nine of the places out of the year's top ten best performing films. In addition to Hong Kong, Taiwan's interest in co-productions has also started to pique, with 11 co-production films going into production. The main reason for this is the artistic aspect of Taiwanese films and their ability resonate culturally with Mainland audiences.

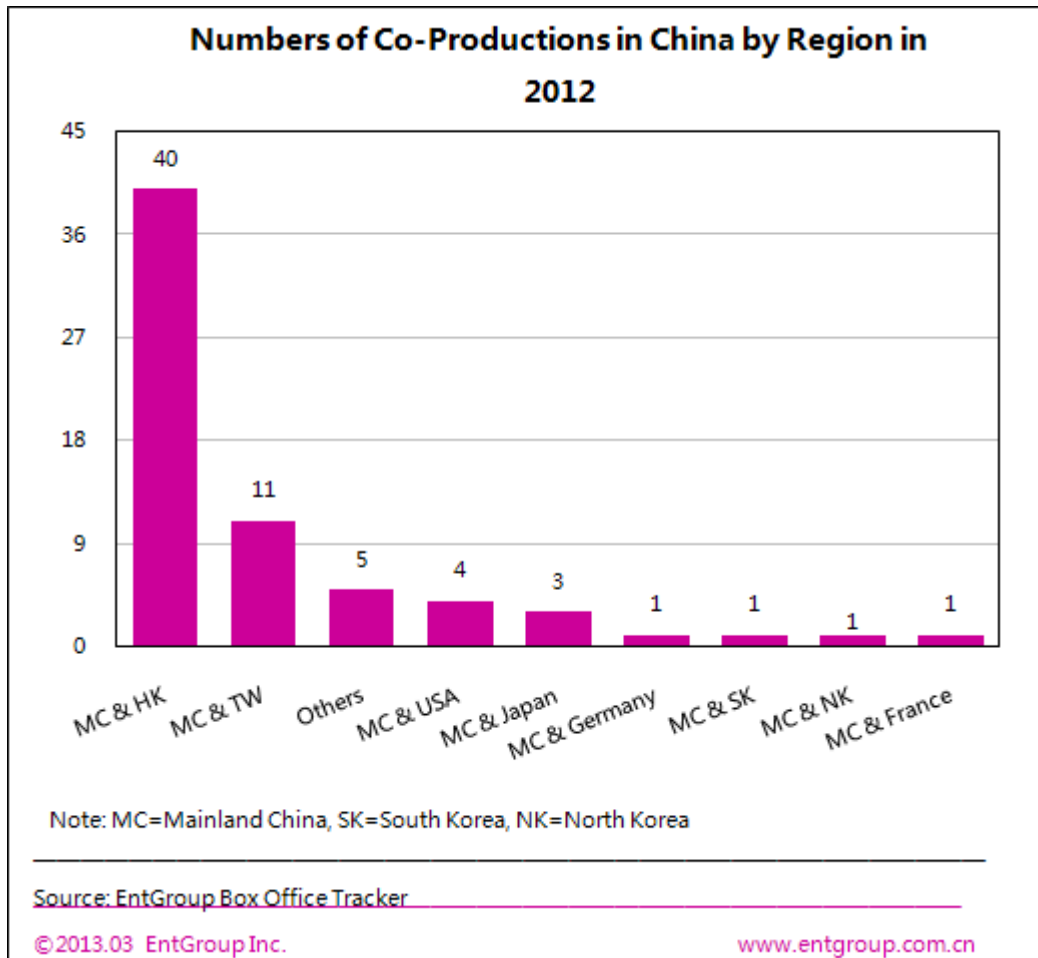


Image 2 - 6 Numbers of Co-Productions in China by Region in 2012

3. Film Distribution in China in 2012

3.1 Overview of Film Distribution in China in 2012

3.1.1 Analysis of Market Shares among Chinese Distributors: private companies more active and four companies split market share for each season

Data from EBOT EntGroup Box Office Tracker show that in 2012, the ten companies with the largest market shares in distribution accounted for 89.2% of the nationwide market, which was a noticeable increase over the 85.0% concentration in the market in 2011.

Among these companies, Le Vision Pictures, Edko Films and Sil-Metropole were newcomers to the Top 10 list, and their performance was especially noteworthy when compared with other newly emerging private distributors.

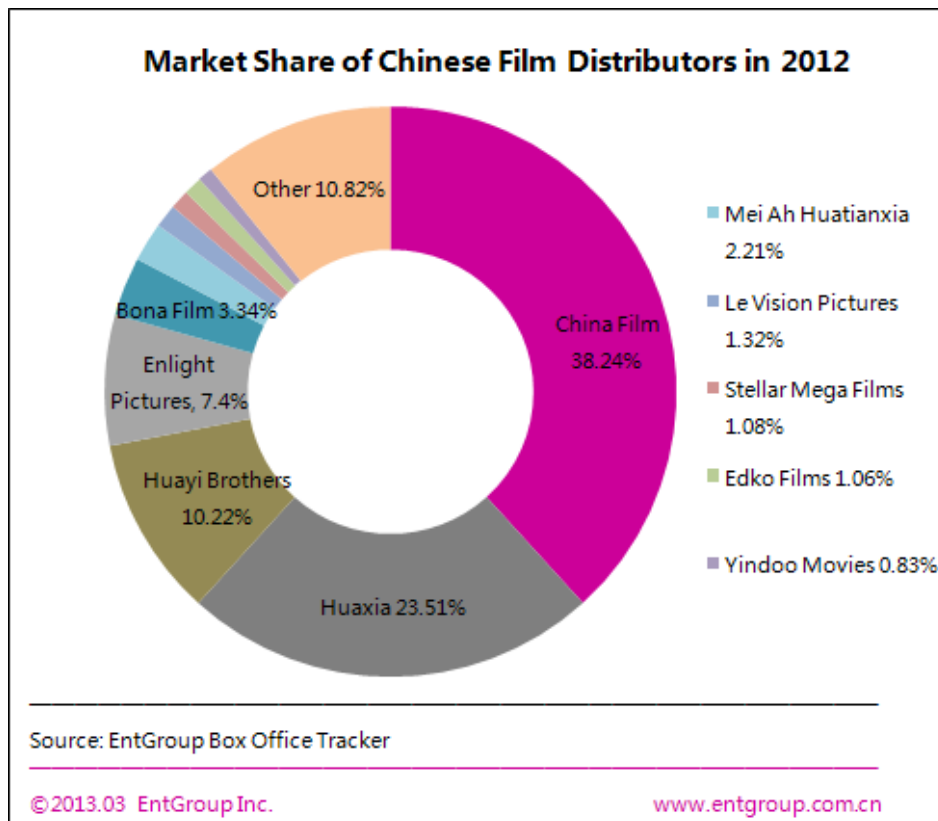


Image 3 - 1 Market Share of Chinese Film Distributors in 2012

4. Analysis of Major Chinese Production and Distribution Companies

4.1 Analysis of State-Owned Companies

Over the past 20 years of reform and development, changes have been made in large state-owned film companies in the areas of property rights, operational mechanisms, corporate structure and institutional innovation, and these changes have essentially completed a strategic restructuring of assets, the market and management. Similar to the structural reforms that have been made within state-owned enterprises, new large-scale state-owned film companies such as the China Film Group, the Shanghai Film Group and especially the Changchun Film Group and Xi'an Movies are also facing policy pressures and systematic shortcomings. In terms of positioning and operational models, they still lag somewhat behind private companies that are growing rapidly.

2002 was a decisive year in the Chinese film industry - the period between 1993 and 2001 was a period of marketization, while the period between 2002 and 2010 was an initial period of development for the Chinese film industry.

The reform of state-owned film companies came just as China was entering the WTO, and the process of marketization that came thereafter drove the development of the film industry. While trade barriers remain in China's film industry, films that are allowed for import every year continue to put pressure on China's domestic film makers. A range of policy guidelines have driven and guided development and changes within state-owned film companies. Meanwhile, the rapid growth of private film companies has also resulted in changes within state-owned film companies.

4.2 Analysis of Listed Private Companies

4.2.1 Huayi Brothers

4.2.1.3 Analysis of Main Business Sectors

Huayi Brothers' main business is divided into six different modules. Excluding film/TV production and artist management revenues, revenue brought in only by theaters, gaming and copyright sales accounted for 11.6% of total revenue in 2012. Huayi Brothers' main source of revenue is still from the production of films and television programs, which is supplemented by cultural products. Movies and related business account for nearly half of Huayi Brothers' total business revenue.

According to Huayi Brothers' financial report for 2012, gross profit from gaming was the highest of all the six major business modules (excluding copyright sales), while gross profit from movies and related business was the lowest. Compared to profit numbers for the same period in 2011, profit from television and theaters both dropped. Revenue from television series and related business remained at the same levels, but gross profit dropped by six percentage points.

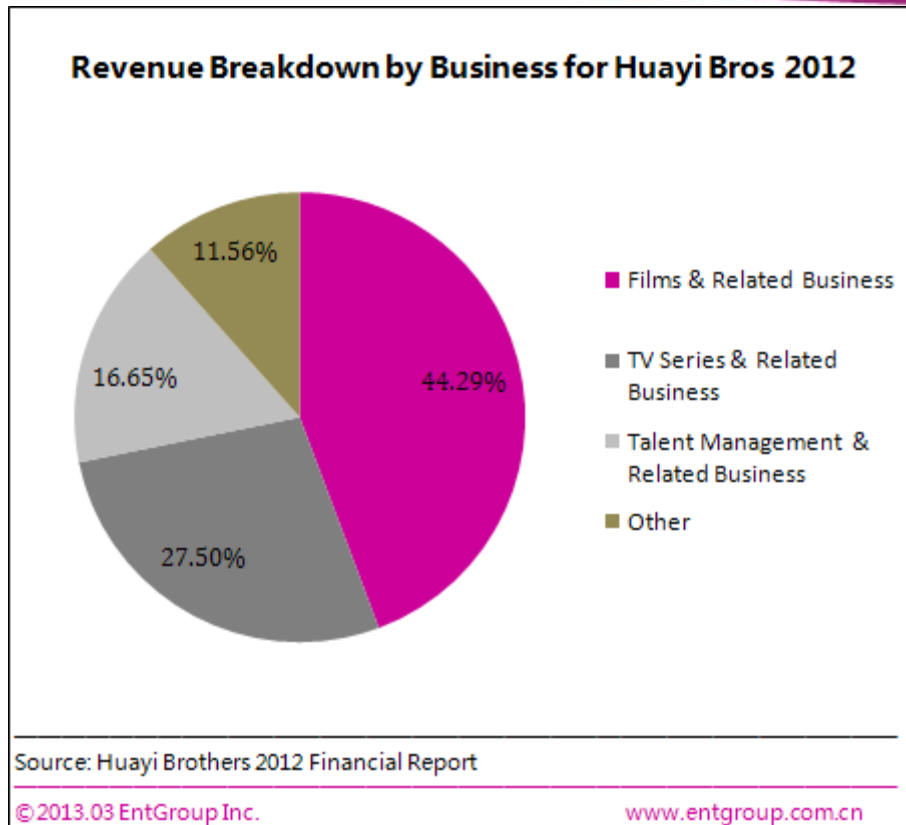


Image 4 - 1 Revenue Break down by Business for Huayi Bros in 2012

Overall, after Huayi Brothers listed in 2009, there was a drop in operational costs in relation to overall revenue, which meant a rise in annual net profit, but this trend has weakened with each proceeding year. The overall trend for profit shows that Huayi Brothers is gradually transitioning from a developing company into a mature company. After listing, there was no expansion of key senior management, but the growth rate continued to rise. The limited scope of management may lead to uncertainty in certain areas of business development and a slowing down of growth. The company's financial report also shows that the future of music and online gaming remains unclear.

5. Chinese Film Exhibition Industry in 2012 - A Study of Movie Theater Chains in China

5.2 Overview of Movie Theater Chain Operations in China in 2012

5.2.1 Market Overview

➤ Theater Chain Statistics

As of the end of 2012, there were 46 movie theater chains operating in cities throughout China, which was an increase of 7 chains from the same period in 2011. The number of theater chains located in the interior of China has been increasing for the past 4 years, with last year's growth rate (2012) being the greatest, at 17.9%. This growth is primarily the initial result of the upsurge in theater investment that has brought great amounts of

capital flowing into theater development that began in 2010. These newly-added theaters also need to establish new theater chains in order to facilitate the consolidation of resources, the strengthening of management capabilities and the improvement of operational efficiency.

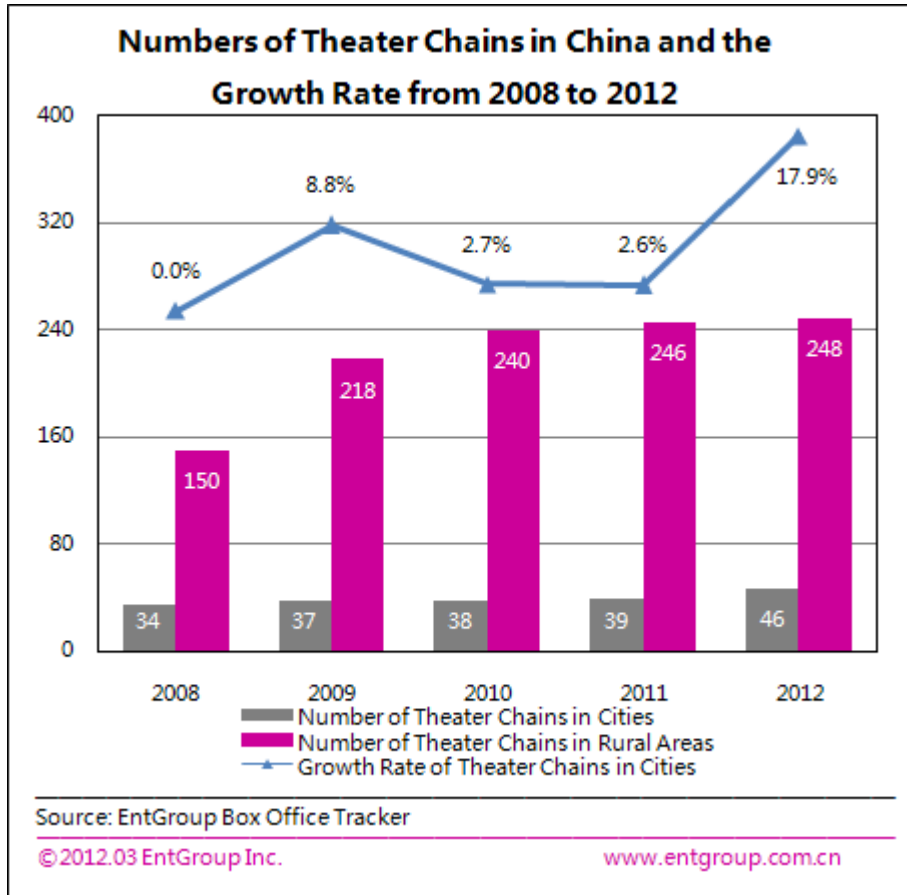


Image 5 - 1 Numbers of Theater Chains in China and the Growth Rate from 2008 to 2012

6. China Film Exhibition Industry in 2012 –A Study of Movie Theaters in China

6.1 Overview of the Development of Movie Theaters in China for 2012

6.1.1 Development of Chinese Movie Theater Numbers and Screen Numbers in 2012

In 2012, the number of movie theaters in China continued to expand at a rapid pace. Theater chain companies across the country built 880 new cinema complexes, bringing the total number of theaters to 3,680. There were 3,832 screens added, an average of 10.5 new screens per day, and this brought the total number of screens to 13,118. With this, the number of screens in China has broken the “10,000 mark.” The average number of screens in the newly added theaters was 4.8, which shows that most of the new theaters added in 2012 were large-scale, comprehensive multi-room theaters. It is estimated that the increase rate in screen numbers and theater numbers

will begin to slow down in 2013 as market investment behavior becomes more rational and the competition between theaters becomes more intense.

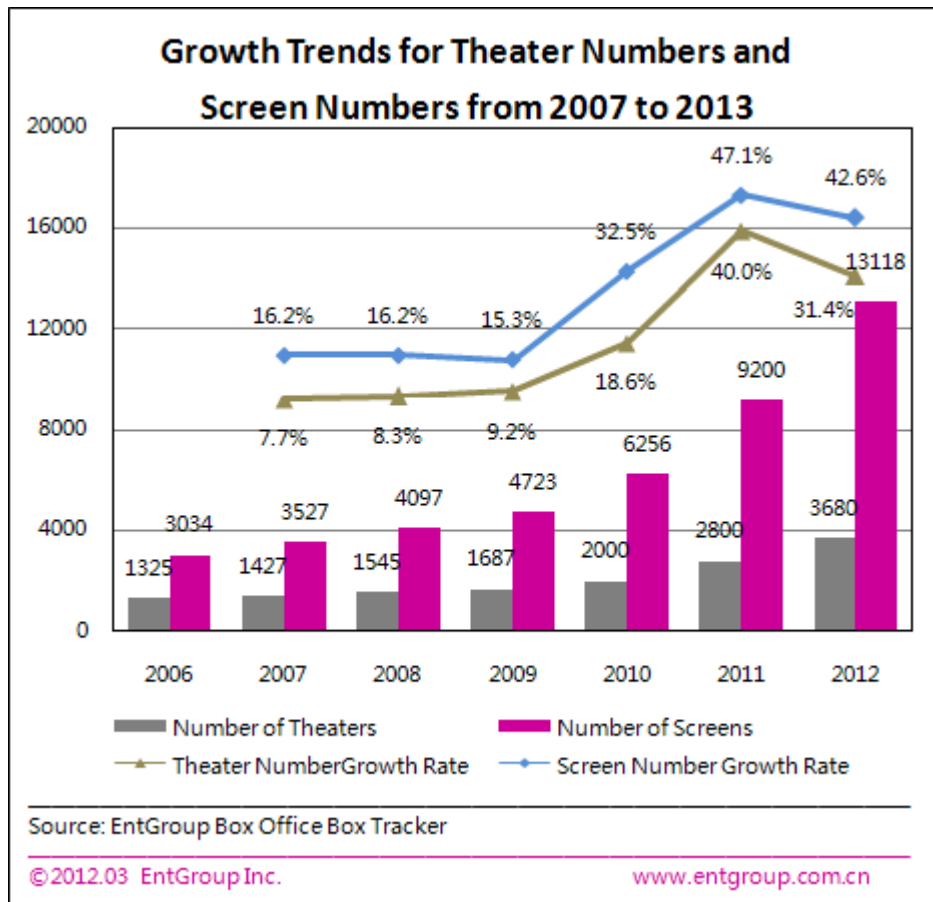


Image 6 - 1 Growth Trends for Theater Numbers and Screen Numbers from 2007 to 2013

6.1.2 Expansion of the Number of Digital Movie Screens in China for 2012

The number of screens equipped with digital movie screens in China for 2012 was 12,225, which accounted for 93.2% of all movie screens. All of the newly added screens in 2012 were equipped with digital movie screens. 2K digital movie screens in China have exceeded 12,000 in number, and the main theater chains now basically only provide for digital viewing. Under the influence of both governmental policy and developing trends in the film market, the dominance of digital movie screens will be further solidified and strengthened.

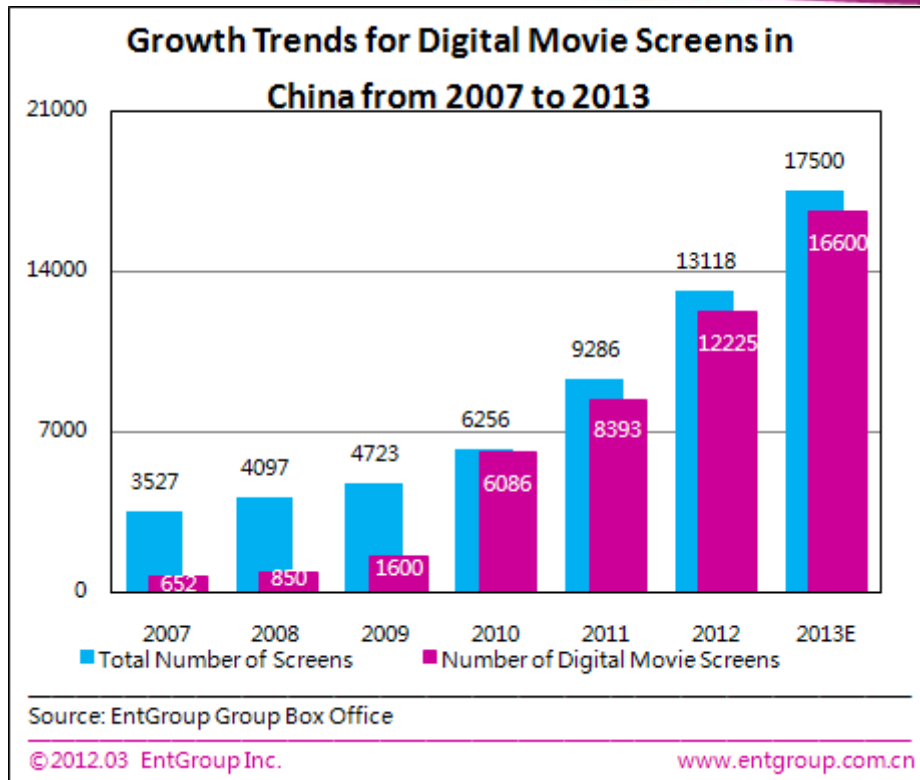


Image 6 - 2 Growth Trends for Digital Movie Screens in China from 2007 to 2013

6.2 Overview of the Movie Theater Market in China in 2012

6.2.1 Different Movie Theater Groupings in China based on Box Office Performance for 2012

According to data provided by the EBOT EntGroup Box Office Tracker, there were 2,988 urban theaters in China with box offices offering statistical information in 2012. These theaters can be categorized at 5 different levels on the basis of their annual box office proceeds. The defined ranges of these five levels are as follows (in Yuan): 50-90 million, 30-40 million, 10-20 million, 5-10 million and less than 5 million. Individual theaters have yet to exceed 100 million in box office earnings. According to EntGroup's analysis, the backbone of the Chinese movie theater market in 2012 were the theaters at the 10-20 million level. It is estimated that the proportion held by theaters in this level will increase in 2013.

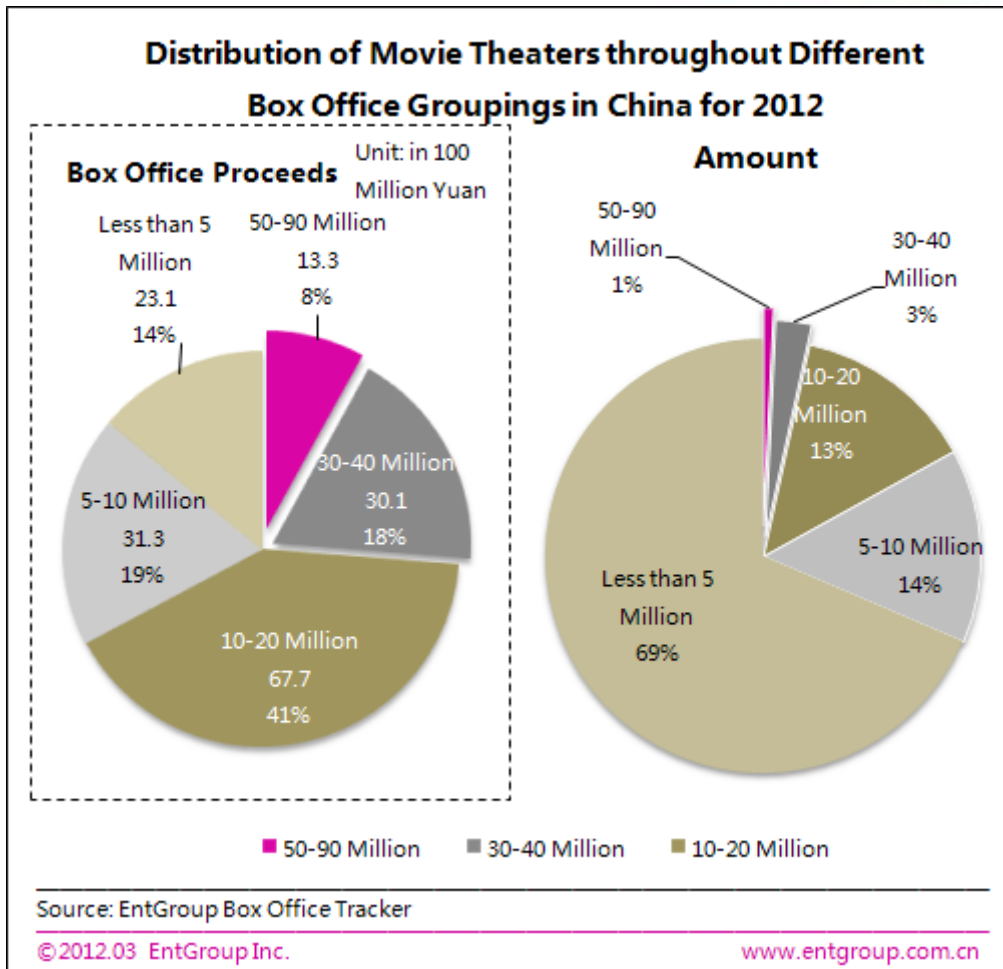


Image 6 - 3 Distribution of Movie Theaters throughout Different Box Office Groupings in China for 2012

7. Timeslot Analysis in China in 2012

7.2 Analysis of the Primary Timeslots in China’s Market for 2012

7.2.1 Summer Timeslot: Income for this timeslot shrank by 200 million, primarily because of a low number of imported films

Box office proceeds for the film market in Mainland China during the summer timeslot of 2012 reached 4.09 billion Yuan. Compared to the 4.28 billion of proceeds during the same timeslot in 2011, box office proceeds for the 2012 summer break shrank by nearly 200 million. According to incomplete statistics, there were a total of 90 films that competed during the summer timeslot of 2012, of which 25 were imported films (including revenue-sharing films, licensed films, Hong Kong and Taiwanese films, as well as specialty films) and 65 were domestic movies (including 19 co-productions). There were 5 domestic films with box office proceeds exceeding 100 million, and there were only 9 films exceeding 50 million. Domestic films made up the great majority of films

screened during the summer timeslot, and these films did not perform especially well. This is the main reason for the reduction in box office proceeds during the summer timeslot.

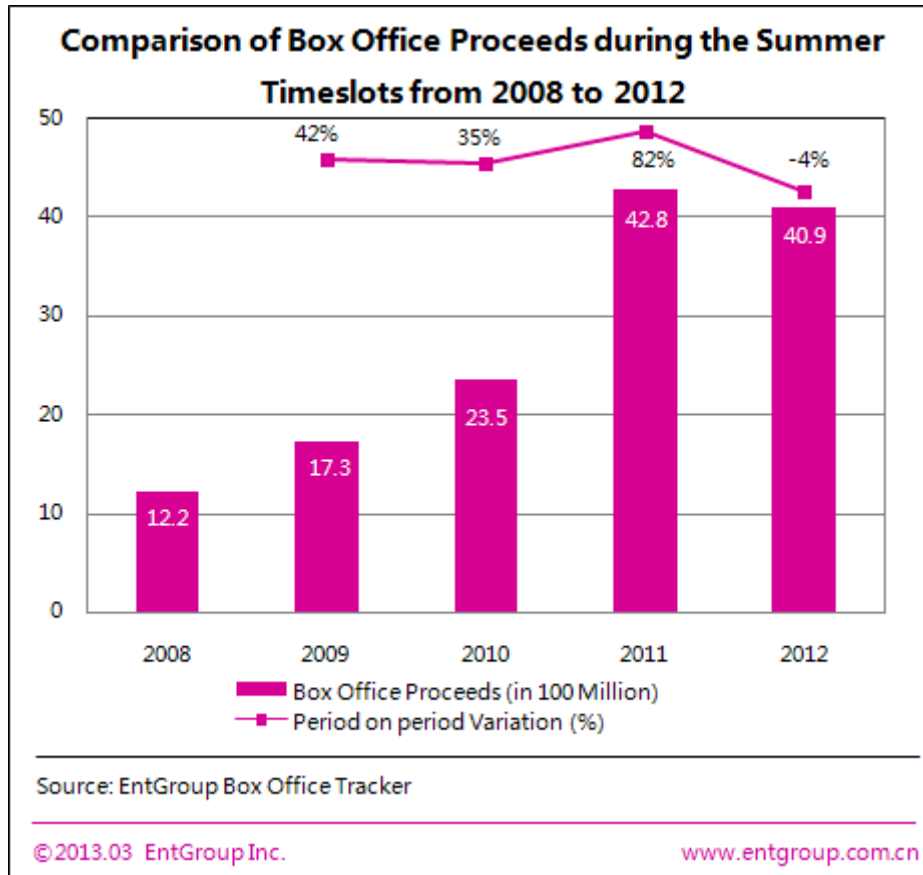


Image 7 - 3 Comparison of Box Office Proceeds during the Summer Timeslots from 2008 to 2012

8. Import of Foreign Films and Export of Chinese Films

8.1 The import of Foreign Films to the Chinese Film Market in 2012

8.1.1 Box Office Performances for Imported Films in 2012

Since 2008, the proportions of total box office proceeds taken by imported films in the Chinese film market have been steadily growing. In 2012, imported films released in Mainland China produced a total of 8.8 billion Yuan in box office proceeds. This was an increase of 2.7 billion Yuan from 2011, and the proportion of the market held by imported films exceeded the 50% mark, arriving at 51.5%. This is the first time in 9 years this share has exceeded that of domestic films.

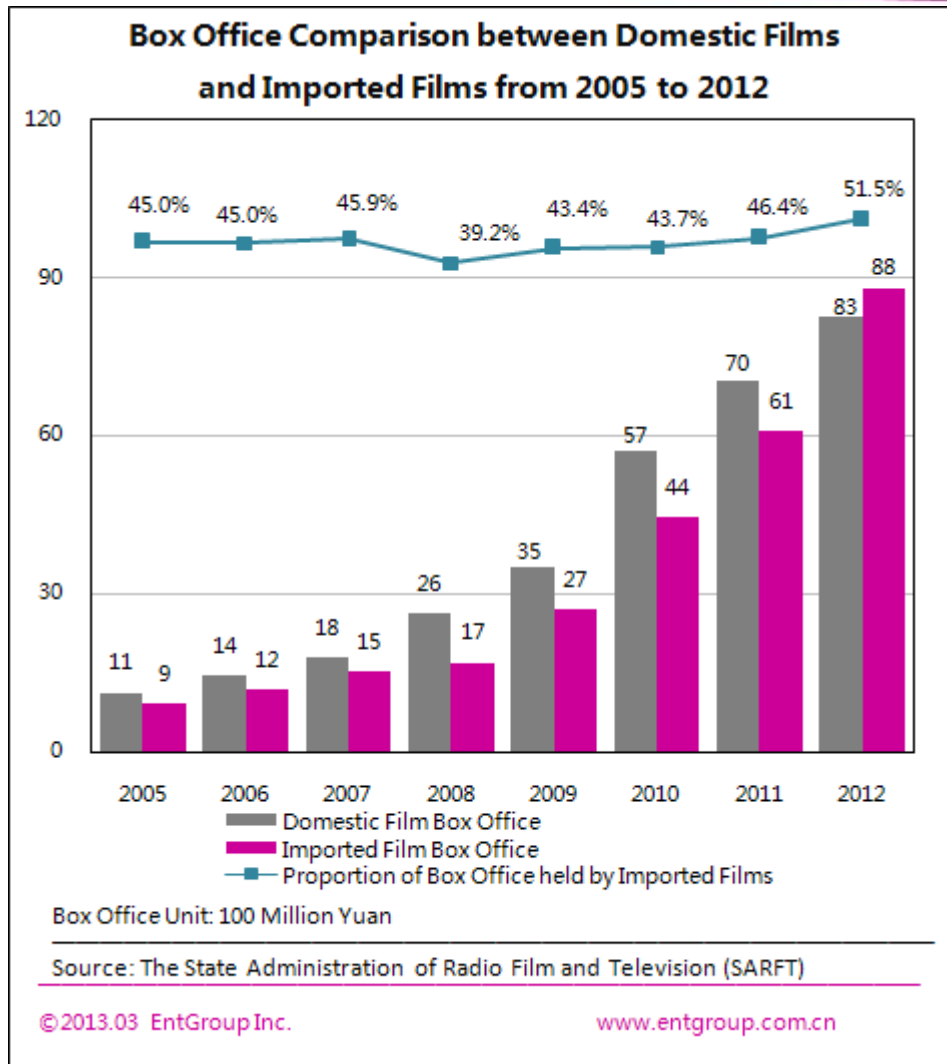


Image 8 - 1 Box Office Comparison between Domestic Films and Imported Films from 2005 to 2012

Data provided by Entgroup shows that, for all the different types of imported films, revenue-sharing blockbusters were able to receive the major shares of box office proceeds. The total box office proceeds taken in by this type of movie accounted for 83.5% of box office proceeds taken in by imported films.

8.2 The Export of Chinese Domestic Films in 2012

8.2.1 The Overview of the Export of Chinese Films in 2012

According to a data report released by the State Administration of Radio Film and Television on January 9th, 2013, China exported 75 films to over 80 countries and regions in 2012. Overseas box office proceeds and sales reached 1.063 billion Yuan, which was a reduction of 47.5% from the previous year.

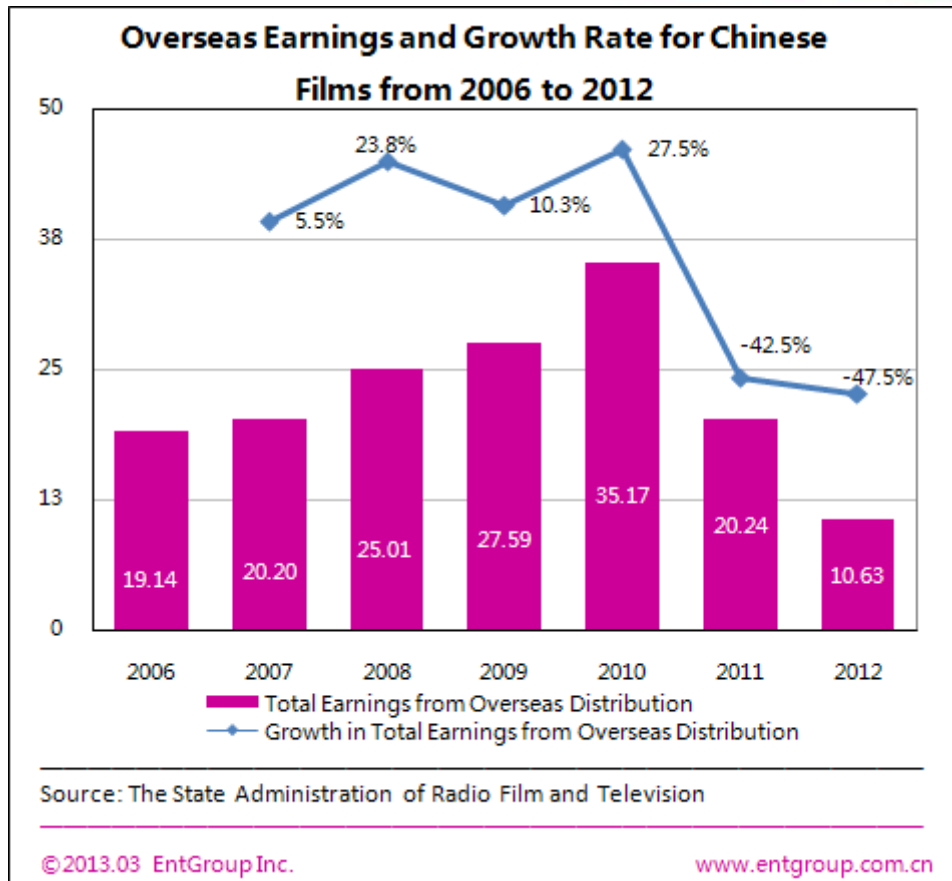


Image 8 - 2 Overseas Earnings and Growth Rate for Chinese Films from 2006 to 2012

In addition to this, according to the statistics provided by China Film Promotion International regarding the overseas box office proceeds for the individual films of each film producing company, the domestic film in 2012 with the highest level of overseas box office proceeds was a film produced by Le Vision Pictures entitled “The Bullet Vanishes” (“Xiaoshi de Zidan”) whose box office proceeds reached 85 million Yuan.

8.3 Trend Analysis for the Import of Foreign Films and the Export of Chinese Domestic Films

8.3.1 Limits on Hollywood’s Share of Imported Films has been further relaxed, and competition with domestic films has intensified

In February of 2012, China and the US reached an agreement and successfully drafted a memorandum of understanding which addressed film related disputes within the WTO. Many new provisions were made at this time, including those allowing for the increase of the amount of American blockbusters allowed into the Chinese import market by 14 films. Looking back on 2012, it can be seen that the new addition of imported 3D/IMAX films has delivered quite a blow to the box offices of domestic films. Domestic films and imported films entered a period of head-to-head competition in the year of 2012.

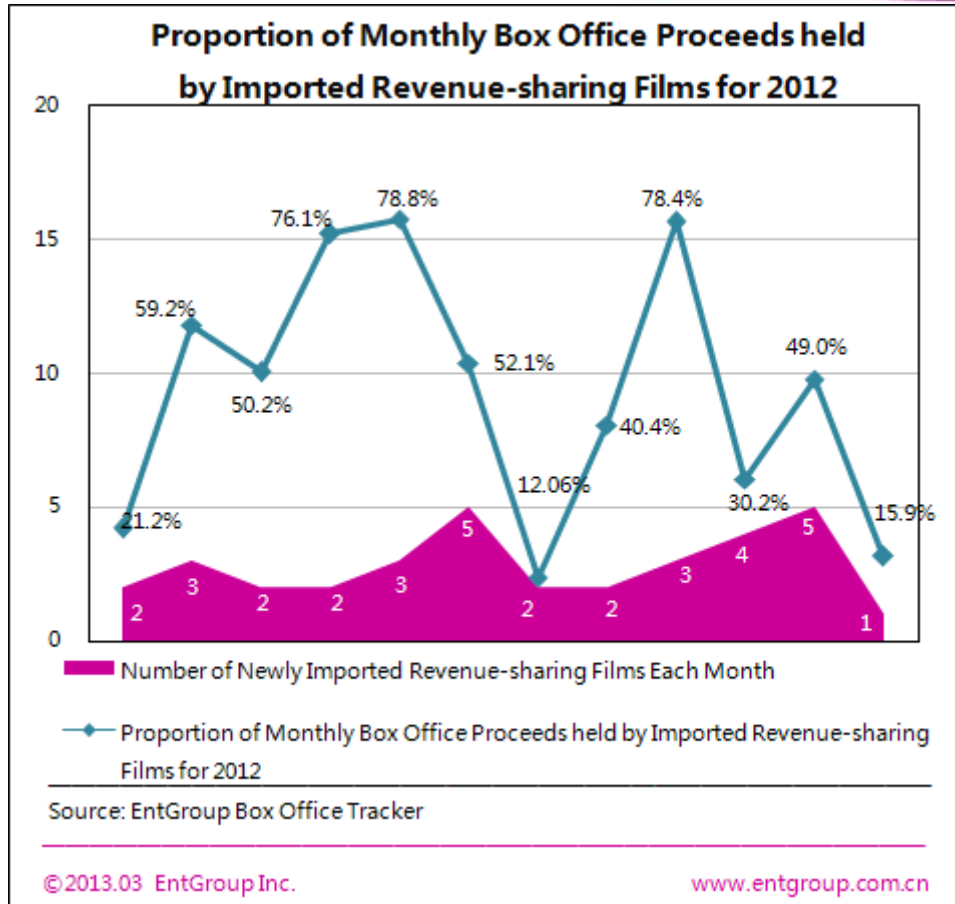


Image 8 - 3 Proportion of monthly Box Office Proceeds held by Imported Revenue-sharing Films for 2012

Looking at the situation at the level of the market, it can be seen that as the quotas for imported Hollywood films continue to increase, the two state-owned companies that originally had a control on the distribution rights for imported revenue-sharing films (China Film Group Corporation and Huaxia) found that it was more difficult to meet the needs of the market with their own operational capacity. This made it possible for a third corporation with distribution rights for imported revenue-sharing films to appear on the scene, which meant that there were to be more competitors entering the market.

Appendix 1:

2012-2013 Chinese Film Industry Report (Pay Version)

Report Type: annual report Length: 150 pages Price: \$ 4000

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Related reports: 2011-2012 Chinese Film Industry Report (Pay Version)

2010-2011 Chinese Film Industry Report (Pay Version)

Published by EntGroup Consulting, the 2012-2013 China Film Industry Report looks deeply into all aspects of China's domestic film industry in a global market. The following is an outline of the content of this report:

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About EntGroup

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EntGroup also operates EntGroup Entertainment Industry Net -- www.entgroup.cn, a portal site on Chinese entertainment industry and economics.

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