The effectiveness and impacts of subsidies to film industries

Alan Collins
Jen Snowball
South African Cultural Observatory
First National Conference

Counting Culture
The Cultural and Creative Industries in National and International Context

16 – 17 May 2016
The Boardwalk International Convention Centre, Nelson Mandela Bay

Calling all interested parties in the Cultural and Creative Industries to become part of the conversation between policy makers, researchers and industry players.

To register please visit: www.saco2016.co.za before 21 April 2016.
Outline

• Arguments for and against subsidy
• Distinguishing direct and indirect subsidies
• Why are there so few empirical studies?
• Case Studies:
  – USA
  – Australia
  – Italy
  – South Africa
• Conclusions and future work
Creative Industries and Subsidy

• The case for subsidies
  – Positive externalities (education, culture)
  – Merit goods
  – Infant industry in global market
  – Competition for FDI (jobs, skills, economic impact)

• The case against
  – Inefficiency (negative rates of return & poor quality)
  – Costly to governments
  – Crowding out of private investment
  – Encourages “subsidy wars”
Begella and Becchetti (1999) offer five reasons for state patronage:

- Broaden cultural options
- Redress commercial imperative that favours entertainment over cultural enrichment
- Foster cultural identity and national prestige
- Generate positive externalities for the community and business tied in to the film industry
- To compensate for the low productivity of ‘art’ films
Direct and Indirect Subsidies

• Direct subsidies – Take this cash!
• Indirect subsidies – Rebates on tax due or paid.
• Hybrids.
• Why might direct subsidies be preferred by some firms?
• Why might indirect subsidies be preferred by some firms?
Why are there so few empirical academic studies?

• Perceived commercial confidentiality issues.
• Concern that the actual evidence base may not support (commissioner’s) preferred policy directions so inhibiting the appetite to commission or offer data availability for independent scrutiny.
• Commissioned consultancy studies tend to give the answers those commissioning the studies want (hence boosting chances of repeat custom) (See evidence considered in Tannenwald 2010). Many consultancy studies feature double counting or over-counting which give more ‘attractive’ results.
• Why bother? (i) Project visibility (i.e we’re doing stuff) (ii) Glitz/Glamour utility? (iii) Political Capital formation (iv) procedural utility or spending as an outcome.
• Incidental oversight.
# Comparative Table

<table>
<thead>
<tr>
<th>Country</th>
<th>Subsidy Type</th>
<th>Research Focus</th>
<th>Key Findings</th>
</tr>
</thead>
<tbody>
<tr>
<td>USA</td>
<td>Indirect and Direct</td>
<td>‘Subsidy wars’ among states and Canada mainly</td>
<td>Subsidy wars are unwinnable and subsidies wasteful</td>
</tr>
<tr>
<td>Christopherson and Rightor (2010)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Australia</td>
<td>Indirect and Direct</td>
<td>Performance of Australian firms generally and subsidized films</td>
<td>Subsidy has no impact on financial success</td>
</tr>
<tr>
<td>McKenzie and Walls (2013)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Italy</td>
<td>Direct</td>
<td>Relative performance of unsubsidized and subsidized Italian films</td>
<td>1. Subsidization potentially be commercially helpful. 2. Subsidy is completely commercially ineffectual</td>
</tr>
<tr>
<td>South Africa</td>
<td>Direct</td>
<td>Subsidy effectiveness in terms of ZA DTI criteria</td>
<td>Mixed findings depending on criteria considered.</td>
</tr>
<tr>
<td>Collins and Snowball (2015)</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
USA

• Few studies despite lots of movies

• Very successful commercial Hollywood cinema but also much independent (arthouse) production.

• Focus of work is exclusively on intense competition by individual US States to attract ‘film projects’ by using various incentives (direct, indirect subsidies) and competing against other US states and other countries.
USA

• Beginnings in New Mexico and Louisiana.
• Both states offered generous tax credits equivalent to a % cost of film shoots within their boundaries.
• Other states followed offering more generous tax credits in a classic “race to the bottom” (see Christopherson and Rightor 2010)
• Now practically all states have them. Given the typical number of film projects there must be winners and losers.
• Refundability and Transferability
USA

• There have been a number of independent though non-academic studies of the effectiveness of tax credits in various specific states.

• The upshot is: Costs far outweigh benefits in all cases.

• State of Massachusetts example.
• McKenzie and Walls (2013) study motivated by the failure of Australian films to capture public attention at the Australian box office.

• This is despite Australian films generally being advertised more heavily and released more widely than non-Australian films.

• They also consider what is the effect of Australian government subsidies on a film’s financial success at the box office.
Australia

• Film – level focus but including distributor strategic objectives over the period 1997-2007.

• Sophisticated statistical/econometric methodology but essentially seeks to identify which factors are statistically significant in explaining box office revenue via estimation of a Revenue function. Revenue is the (lhs) dependent variable to be explained by a set of (rhs) independent variables. Economists have a priori expectations based on theory to guide interpretation.

• Robust results to alternative model specifications.
Australia

• Results relating to subsidy (as lhs explanatory variable) across films shown in Australia suggest:
  • Subsidies have **NO** impact on a film’s financial success at the box office.
  • Subsidised films were released on more screens and did have higher levels of advertising expenditure and higher budgets but still no significant impact on both opening week and cumulative revenues.
  • Caveat: These subsidies are based on more than purely commercial reasoning but this dimension does not seem to be formally monitored or assessed.
Italy

- To investigate the robustness of an earlier study (Begella and Becchetti 1999) on data from 1985-1996 that subsidized films did not have a significantly lower performance in terms of cinema admissions and revenues.
- Study outcomes are contradictory.
Italy

- Begella and Becchetti (1999) study use as their measure of performance: end-of-run box office revenue generated in the Italian market
- BUT this measure does not fully reflect the resources embodied in film production (ie including budget costs, subsidy) and hence alternative uses which the resources could be put.
- Arguments also relate to talent
Italy

- Used direct subsidy. So who dished out the cash?
- Specific institutional and political features characterizing the Italian system are important components in this story.
- In an overwhelming number of cases production losses exceeded subsidy.
- Unsubsidised Italian films performed better.
- Apparent separation of ‘cinema’ and ‘audience’
Italy

• Graduated subsidy thresholds depending on various film criteria and past experience in film making.
• For subsidized films: mean rate of return of excluding subsidy: -80.3%
• For subsidized films: mean rate of return including subsidy -65.2% (i.e. overwhelmingly unprofitable).
• For unsubsidized films -:
• mean rate of return is: -28.3%. (i.e. there were a few profitable films but most were not)
• Some changes to the subsidy regime after 2003.
# SA Film & TV Incentive Schemes

<table>
<thead>
<tr>
<th>Foreign Film and Television Production and Post-Production Incentive</th>
<th>SA Film &amp; TV Production and Co-production Incentives</th>
<th>SA Emerging Black Filmmakers Incentive (1/9/2014)</th>
</tr>
</thead>
</table>
## Objectives

- To attract large budget film and TV productions and post-production work that will enhance job creation, skills and international profile of SA film industry.
- To support the local film industry and to create employment in South Africa.
- To nurture and capacitate emerging black filmmakers to take up big productions and contribute to employment opportunities. Focus on local content production.

## Benefits

- 20% of QSAPE (no cap) QSAPE + QSAPPE subsidy of 22.5% to 25% (2.5% to 5% increase to encourage post-production) (R50m cap 1/9/2014)
- 35% of first R6m of QSAPE, and R25% of QSAPE thereafter (no cap).
- 50% of QSAPE of first R6m, 25% thereafter (no cap)

## Eligible Applicants

1) QSAPE of R12m and above, with at least 50% of principal photography in South Africa, with a 4 week minimum.
2) QSAPPE of R1.5m and above, minimum of 2 weeks.
3) Applicant must be a SPV
4) Compliance with B-BBEE (at least level 4)

1) Applicant must be an SPV, the parent company of which must have a majority of South African shareholders, of whom at least one must play an active role in the production.
2) At least 50% of principal photography in SA, 2 week min.
3) Minimum QSAPE of R2.5m (R500,00 for documentaries).
4) Compliance with B-BBEE (at least level 4).

1) QSAPE of R1m and above (R500,00 for documentaries), with at least 80% of principal photography in SA, 2 week min.
2) Applicant must be SPV with at least 75% black SA shareholders who must play active, credited production roles (producer/director).
3) Holding company must have 65% SA black shareholders.
4) At least level 3 B-BBEE status
Research questions

• Have the DTI film & TV incentives been effective in stimulating economic growth, job creation, skills development and transformation?

• Method & Data
  – DTI incentives data (Feb 2009 – June 2012)
  – Unpublished industry reports
  – Interviews with key stakeholders
Does the subsidy work for all films?

<table>
<thead>
<tr>
<th>Subsidy Concentration Index (SCI) %</th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
<th>3 Year Combined</th>
</tr>
</thead>
<tbody>
<tr>
<td>SCI (Top 3 Firms)</td>
<td>51.4</td>
<td>51.6</td>
<td>46.6</td>
<td>43.0</td>
</tr>
<tr>
<td>SCI (Top 5 Firms)</td>
<td>69.9</td>
<td>64.5</td>
<td>52.6</td>
<td>60.0</td>
</tr>
<tr>
<td>SCI (Top 10 firms)</td>
<td>84.4</td>
<td>80.4</td>
<td>68.5</td>
<td>73.4</td>
</tr>
</tbody>
</table>

Source: Authors’ calculations using DTI data
SCI determined by % share (of Top N firms) of total subsidy payments in each time period.
## Incentive payments, Qualifying SA Expenditure (QSAPE) and GDP impact from 2009 – 2011 (in millions of South African Rands)

<table>
<thead>
<tr>
<th>Production Type</th>
<th>Incentive payments: 3 year average (2009 – 2011)</th>
<th>QSAPE: 3 year average</th>
<th>Ratio of subsidy to QSAPE</th>
<th>Ave. increase in real GDP p/a</th>
</tr>
</thead>
<tbody>
<tr>
<td>South African Production</td>
<td>48.12</td>
<td>257.74</td>
<td>1:5.36</td>
<td>605.68</td>
</tr>
<tr>
<td>Co-Production</td>
<td>83.79</td>
<td>333.44</td>
<td>1:3.98</td>
<td>783.59</td>
</tr>
<tr>
<td>Foreign Production</td>
<td>53.63</td>
<td>356.73</td>
<td>1:6.65</td>
<td>838.31</td>
</tr>
<tr>
<td>Total</td>
<td>185.54</td>
<td>947.90</td>
<td>1:5.11</td>
<td>2227.59</td>
</tr>
</tbody>
</table>

All figures reported in 2010 prices
Sectoral multipliers from the South African Industrial Development Corporation used to calculate changes in GDP.
## Job creation of subsidised projects

<table>
<thead>
<tr>
<th></th>
<th>Direct FTE jobs</th>
<th>Indirect FTE jobs</th>
</tr>
</thead>
<tbody>
<tr>
<td>South African</td>
<td>1120</td>
<td>2720</td>
</tr>
<tr>
<td>Co-Production</td>
<td>2417</td>
<td>3518</td>
</tr>
<tr>
<td>Foreign</td>
<td>2163</td>
<td>3764</td>
</tr>
<tr>
<td>Total</td>
<td>5700</td>
<td>10 002</td>
</tr>
</tbody>
</table>

### Transformation?

#### Notes:
Employment duration weightings were applied to convert project jobs for each film/television project into 1 year full time equivalent (FTE) employment.

South African Industrial Development Corporation (2010) employment multiplier for the “Motion picture, radio, television and other entertainment activities” of 4.49.
Evaluation

**Successes**

- Attract large-budget foreign films & co-productions
- 2009 – 2011: Economic impact of subsidised films: R2.2b a year; 15 500 FTE (direct & indirect) jobs
- Skills development through knowledge spillovers

**Challenges**

- Transformation is slow
- Skills & training slow (short-term contracts related to SPVs)
- Lack of demand for SA films
- Smaller producers don’t qualify for subsidy
- Rent-seeking behaviour by agents
## Comparative Table

<table>
<thead>
<tr>
<th>Country</th>
<th>Subsidy Type</th>
<th>Research Focus</th>
<th>Key Findings</th>
</tr>
</thead>
<tbody>
<tr>
<td>USA</td>
<td>Indirect and Direct</td>
<td>‘Subsidy wars’ among states and Canada mainly</td>
<td>Subsidy wars are unwinnable and subsidies wasteful</td>
</tr>
<tr>
<td>Christopherson and Rightor (2010)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Australia</td>
<td>Indirect and direct</td>
<td>Performance of Australian firms generally and subsidized films</td>
<td>Subsidy has no impact on financial success</td>
</tr>
<tr>
<td>McKenzie and Walls (2013)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Italy</td>
<td>Direct</td>
<td>Relative performance of unsubsidized and subsidized Italian films</td>
<td>1. Subsidization potentially be commercially helpful. 2. Subsidy is completely commercially ineffectual</td>
</tr>
<tr>
<td>South Africa</td>
<td>Direct</td>
<td>Subsidy effectiveness in terms of ZA DTI criteria</td>
<td>Mixed findings depending on criteria considered.</td>
</tr>
<tr>
<td>Collins and Snowball (2015)</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>
Way forward/new directions

• Need for frankness that judgements may not be justified on economic grounds but could be justified on other grounds.

• However, given the use of public money those other grounds need to be more transparently monitored and assessed.

• Can artistic, social policy and economic assessments be reconciled?

• One possible approach – PROMETHEE?
**Preference Ranking Organization METHod for the Enrichment of Evaluations (PROMETHEE)**

- Allows a visual evaluation of the relative performance of each film across a number of indicators (policy objectives)
- For example: total employment, spending, employment by type (skill) and demographics.
- Can examine trade-offs between different policy objectives
- Can add in benchmarks and change weightings
- For SA:
  - total employment;
  - transformation (black employment, black skilled employment);
  - spending in SA;
  - skills transfer (international involvement)
Key finding:
There exists potentially considerable policy tension among policy objectives in the contemporary South African context.
Project Scores

Higher employment, but low QSAPE

High QSAPE, but low employment
Concluding Remarks

• Pity that there are few empirical studies of film subsidy effectiveness;
• Difficulty of sourcing data (role for SACO)
• Regular evaluation can lead to potentially useful policy changes/adaptation;
• If subsidies cannot be justified on economic grounds, what are the other evaluation criteria that could be used?
THE END
References


