SYSTEM FOR CREATING CUSTOMER VALUE FROM DIVERSITY IN THE MOVIE INDUSTRY

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ABSTRACT
Existing theories on competitive strategies tend to focus on systems, such as vertical integrated systems, that maximize a company’s strategic benefits and minimize strategic costs; the theories focus on company efficiency. Although the systems can bring competitive advantage to a company in the deliberately produced goods industry, diversity such as novel benefits or wide assortments, which I call customer value from diversity, is more important than efficiency for companies in the entertainment service industry. Existing theories on competitive strategies, however, tend to focus on a company’s resources or activities that achieve efficiency before considering customer value. This paper views the decreasing size of the movie market in Japan as a result of failure to consider customer value from diversity. A comparative case study between the movie industry with a customer value perspective in the U.S. and the same industry without a customer value perspective in Japan is presented. The production system and the structure of the movie industry in the U.S. created customer value from diversity, generating more revenues than companies in Japan without this perspective. The Japanese companies focused more on their efficiency than on customer value from diversity.

Keyword: vertical integration, market transaction, the movie-theater industry, efficiency, effectiveness

INTRODUCTION
Existing theories on competitive strategies tend to focus on efficient system consisting of the firms in the vertical relationships in the industry. This paper views such inter-corporate vertical relationships as a system, and two types of the systems are presented based on the degree of the forward vertical integration. I follow Porter (1980) in defining forward vertical integration as the degree to which a company owns its downstream buyers.

The choice of whether to adopt the forward vertical integrated system or market transaction system depends on production and transaction costs (Williamson, 1985). It means that research interest has been concerned mainly with the reduction of those costs.

In the currently dominant perspectives in the strategic management and inter-corporate relationship fields, that is firm positioning (Porter, 1980), transaction cost economics (Williamson, 1971), and a resource dependence perspective (Pfeffer &
Salancik, 2003) views, company efficiency has received great attention by researchers. Second, there is another dominant issue, that is effectiveness. Vertical integration is effective in terms of coping with interdependence (Pfeffer & Salancik, 2003). “Effectiveness is the relationship between a responsibility center’s outputs and its objectives. The more these outputs contribute to the objectives, the more effective the unit is (Anthony 1998, p. 131).” One of the focal objectives of competitive strategy is to capture more profits than other companies in the same industry.

Increasing payments from consumers, that equal revenues plays a prime role to the objective, providing customers with customer value, therefore, is crucial. One of the important issue is what kind of customer value companies and systems can create. However, the issue has received relatively little attention in the area of strategic management or inter-corporate relationships. Previous literature has lacked the viewpoint of what kind of customer value the vertical integrated system or market transaction system can create.

LITERATURE REVIEW: EFFICIENCY, EFFECTIVENESS, AND CUSTOMER VALUE

Efficiency and Effectiveness

Efficiency is the ratio of outputs to inputs. If system A requires fewer resources than system B, and both outputs are the same, system A is more efficient than B.

On the other hand, The focus of effectiveness is on an amount of output, which means that pursuing manager’s objectives, such as increasing company’s revenues is important (Anthony, 1998).

Although the systems for efficiency can bring competitive advantage to a company in the produced goods industry, diversity such as wide assortments including novel benefits created by SMEs, which I call customer value from diversity, is more important than efficiency for companies in the entertainment services industry.

Pfeffer & Salancik(2003) argued that reduction of interdependence between the firms in transaction is core issue for mangers, and vertical integrated system can cope with the interdependence, and reduce transaction costs.

On the other hand, a separated system which I call market transaction system has these advantages: first, market transaction enables a company to acquire materials for making products at low cost. Second, quality of a product can increase in the competitive system. The issue concerns customer value.

COMPARATIVE CASE STUDY BETWEEN THE MOVIE INDUSTRY IN THE U.S. AND THE ONE IN JAPAN
In Japan, major movie company has three functions—production, distribution, and administration of cinemas (ref. Figure 1). The system is considered as a vertical integrated system. The integration of the three functions is prohibited by antitrust law in the U.S.

Strictly speaking, The distributor cannot have cinemas, which means that forward vertical integration is prohibited.

Therefore, there is market transaction between the distributors and the cinemas, and an enormous transaction cost, such as negotiation cost for get cinemas to show distributor’s movie.

![Diagram of Vertical Integrated System and Market Transaction System](source: based on (Orbach & Einav, 2007))

However, as figure 2 shows, the movie-theater industry in the U.S. has been more successful than that of Japan.

One of the reason is that the market transaction system can create wide assortments including movies distributed by relatively small firms which received a lot of movie award.
Exhibitors tend to have great power in the U.S. Because managers of cinemas have right to select and show movies in according with customer’s reputation, regardless of the size of the film company. Therefore customer value from diversity can be created from the market transaction system. On the other hand, in theaters in Japan, their own film or a few kinds of films distributed by other major companies is showing, thus, the vertical integrated system tends to generate general customer value, which is not really differentiated.

In Japan, major distributors, as shown figure3, have a big chance to show their movies in a lot of cinemas. However, even if the movie distributed by independent distributors received many movie awards or customer’s reputation, the number of cinemas showing the movies is not likely to increase, because the independent distributors are out of the vertical integrated chain controlled by major movie companies.

**Figure2  Cinema Attendance**

**Source:** Based on (Kinema Junpo, 2008), p.81

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Figure 3: Movie Industry in Japan

<table>
<thead>
<tr>
<th>Rank</th>
<th>Title</th>
<th>Distributor</th>
<th>Box Office (USD MM)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Marvel's The Avengers</td>
<td>Disney</td>
<td>623.4</td>
</tr>
<tr>
<td>2</td>
<td>Dark Knight Rises, The</td>
<td>Warner Bros.</td>
<td>448.1</td>
</tr>
<tr>
<td>3</td>
<td><strong>Hunger Games, The</strong></td>
<td>Lionsgate</td>
<td><strong>408.0</strong></td>
</tr>
<tr>
<td>4</td>
<td>Skyfall</td>
<td>Sony</td>
<td>288.7</td>
</tr>
<tr>
<td>5</td>
<td>Twilight Saga: Breaking Dawn Part 2</td>
<td>Lionsgate</td>
<td>286.4</td>
</tr>
<tr>
<td>6</td>
<td>Amazing Spider-Man, The</td>
<td>Sony</td>
<td>262.0</td>
</tr>
<tr>
<td>7</td>
<td>Brave</td>
<td>Disney</td>
<td>237.3</td>
</tr>
<tr>
<td>8</td>
<td>Hobbit: An Unexpected Journey</td>
<td>Warner Bros.</td>
<td>228.5</td>
</tr>
<tr>
<td>9</td>
<td>Ted</td>
<td>Universal</td>
<td>218.8</td>
</tr>
<tr>
<td>10</td>
<td>Madagascar 3: Europe's Most Wanted</td>
<td>Paramount</td>
<td>216.4</td>
</tr>
</tbody>
</table>

Table 1: Top 10 Films by U.S./Canada Box Office Earned in 2012

Source: Motion Picture Association of America

On the other hand, in the U.S., the movies distributed by independent distributors can get as much revenues as the movie distributed by major film distributors, as shown in Table 1. Although for distributors in the U.S., existence of cinemas is essential and, managers of cinemas have to secure the movies every week. Therefore, the interdependence between distributors and cinemas is high. However, the system that doesn’t eliminate the interdependence brought the movie industry in the U.S. success.

**CONCLUSION**

One of the study’s contributions is that I suggested the existence of the difference in customer value created by the two system—the vertical integrated system and market transaction system. The case study revealed that in the vertical integrated system, a company (which means a cinema in the case) is likely to produce general value which is not sufficiently differentiated from customer value produced by competitors. A company in the market transaction system, on the other hand, tends
to create wide assortments including novel benefits provided by relatively small distributors (SMEs), which I call customer value from diversity.

What type of customer value we can create depends on which system we adopt. Although the viewpoint of efficiency is important, managers cannot afford to focus only on pursuing efficiency especially in the entertainment services industries. Managers also have to consider the kind of customer value. If his company belongs to entertainment services industry, to create customer value from diversity must be at the core of his strategy.

Conclusion from the case study of a single industry is not sufficient for generalization. And, it should be clearer that the difference between the movie industry and the manufacturing industry.

REFERENCES