2016 Top Markets Report Media and Entertainment Country Case Study

China

China's M&E industry is on track to reach $242.2 billion by 2019.[1] China has the second largest economy in the world, powered by state-owned enterprises (67 are listed on the Fortune Global 500). The population of 1.3 billion has more than 600 million Internet users and 500 million mobile Internet users. Wi-Fi is widespread and free, but free speech is curtailed and Internet sites are monitored and blocked for offensive content. China's growing affluent middle class is seeking quality and diversity of entertainment products and services. The government has put its weight behind promoting culture and is building movie theaters at a furious pace, now standing at 23,600 screens (compared to 40,000 in the United States) and more than 3,700 theaters and growing and with an estimated 60 million movie goers, there are excellent M&E growth opportunities in the world's most populous country.

Overall Rank

2

Ranking of the Chinese M&E Sectors 2016

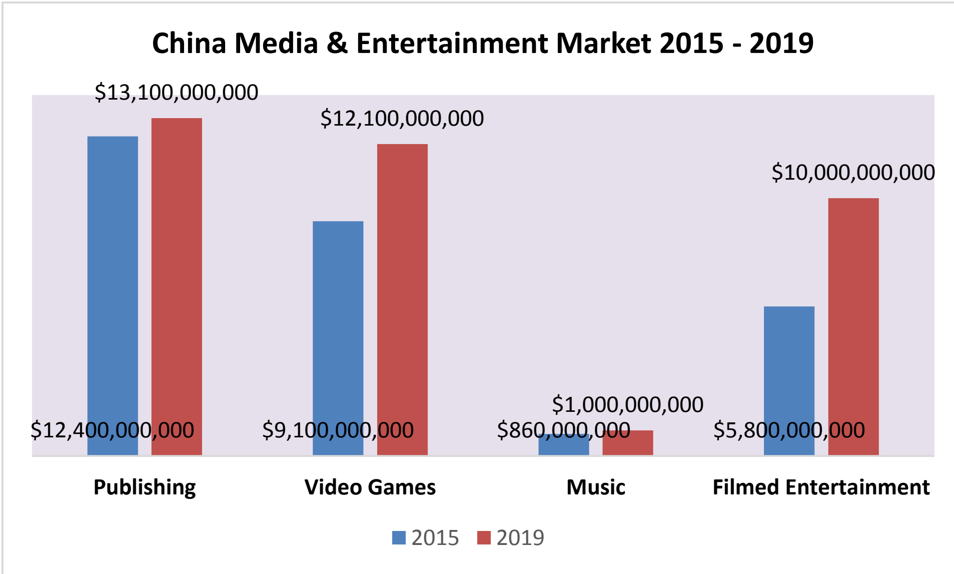
1. **Filmed Entertainment**
2. **Video Games**
3. **Publishing**
4. **Music**

China ranks second on ITA's list of top M&E export markets by sheer size. China offers a powerful, large market place and the government is making sure the entertainment industry is rising to the challenge to match global markets and offerings for its vast consumer base. However, trade barriers such as content restrictions and rules for Chinese ownership limit how U.S. exporters can access and trade in this market, hence it ranks second. U.S. film producers and distributors can enter coproduction agreements or other entrusted production agreements to bring U.S. content to film and TV viewers, both in theaters and online.

The music industry is growing and is equally challenging to enter due to regulatory restrictions and state mandated censorship approval. Demand for Western music, while popular (especially American music), has not developed to the same degree as K-pop (Korean pop music), and Chinese opera and other local content is still very dominant in the Chinese marketplace.

The games sector is also booming, and both digital console and online games are facing robust growth in the next five years, presenting excellent opportunities for U.S. exporters who would like to enter the marketplace with a Chinese partner. With 13 percent of the world's global mobile revenues, a new trend has emerged with games spreading due to the popularity of mobile chat apps.[30] Piracy plagues China, and the government is working to improve copyright and IP protections.

Overview of M&E Market



* Data Sourced from PwC Global Media & Entertainment Outlook 2014-2018

China's M&E market is growing faster than the overall economy as the government has strategically invested in M&E and the growing middle class consumer base can afford to spend on entertainment. The Chinese government has emphasized training in the Chinese M&E industry and has increasingly made capital available to the cultural and entertainment sectors, while cautiously allowing foreigners to invest, such as creating an M&E investment fund in collaboration with Singapore and a media project with U.S. media conglomerate Time Warner.

In addition, both the U.S. and China view this industry focus as a "soft power" tool in a five-year plan to grow the domestic industry and increase China's global influence as well as their image abroad.[i] There is high demand and consumption of mobile games and filmed entertainment, and some experts advise new exporters to start investing in second or third-tier cities that have established international business ties and active ports before venturing to the capital, Beijing, and so-called first-tier cities, like Shanghai, that are more competitive.

Opportunities for U.S. Companies

Filmed Entertainment

China's filmed entertainment sector is expected to grow 14.5 percent by 2019 to reach just under $10 billion, nearly doubling from $5.8 billion in 2015.[ii] This growth is due to China's policies to stimulate the sector, build its domestic movie production and digital theaters, and expand the role of co-productions, as well as addressing their quota system and increasing revenue sharing imports. According to the Los Angeles Times and Artisan Gateway (a leading film and cinema consulting firm in Asia), box office receipts increased 48.3 percent to $6.8 billion by year end of 2015.[iii] This enormous growth is the largest jump in the past five years, and 61 percent of it was generated by Chinese films, as American share of the market has continued to decline.[iv] Chinese screens increased by more than 9,000 in 2015, bringing the total amount of movie theaters to 32,000.[v]

China boasts the second largest theatrical market worldwide after the United States, and box office revenues are on a meteoric rise and are expected to reach $8.8 billion (15.5 percent) by 2019. Filmed entertainment is a main driver for the entertainment sector in China, and the government has invested a tremendous amount in new mega theaters and entertainment complexes, collaboration with U.S. media and entertainment conglomerates, and co-productions with foreign entities and domestic film production.

In 2014, 67 foreign films were released in China; 33 of those were released on a flat-fee basis and 34 on revenue-sharing basis, meeting the full quota of films.[33] The U.S.–China film deal of 2012 allows for

14 additional movie imports of new format films in 3D or animation on a revenue sharing basis. China's overall import quota on a revenue sharing basis now stands at 34 films annually for all countries. Co-production is gaining in popularity, and several major Hollywood studios as well as indie film makers engage in these deals with China. In 2015, foreign films held 45.5 percent market share, in large part due to the success of the U.S. blockbuster *Transformers: Age of Extinction*.

Whether importing or co-producing, foreign firms interested in working with China will have to understand how to address State Administration of Press, Publication, Radio, Film and Television of the People's Republic of China (SAPPRFT), regulations for the industry, including cultural and content restrictions, a quota system for foreign films, and garnering data and earnings from unclear box office reporting. There are two major modes of co-production in China: joint production (collaboration) and assisted production (entrusted production). Joint production, or "co-pro," is considered a domestic film and not subject to the quota and will also be at least 51 percent Chinese-owned. In an entrusted production agreement, the foreign party puts up 100 percent of the capital; the Chinese side produces the film, but it counts as a foreign film under the import quota.

U.S. exporters and licensors also face a marketplace with widespread piracy of creative content and are advised to conduct a cost-benefit assessment prior to entering the market. The Department of Commerce offers IPR resources specific to the Chinese market, which is available on www.stopfakes.com. In addition, the China Film Group (CFG) controls distribution of imported movies, and investors will have to either use a joint partnership or hire U.S. or local experts to help maneuver the bureaucracy. Either way, a Chinese entity must be approved for "film distribution" in order to distribute foreign movies. While CFG has such an approval, other Chinese entities may also be approved.

It is a must to speak Chinese or have a local representative who is fluent in Chinese (Mandarin on the mainland) when doing business in China. U.S. producers and exporters will compete for the online generation in China with the "BATs," namely the three Internet giants in China: Baidu, Alibaba and Tencent, which have all moved into film production.[34]

Dalian Wanda Group, China's largest cinema owner and commercial real estate developer, which acquired the U.S. company AMC in 2012, is building a movie studio to rival Hollywood studios in Qingdao, a major port city in eastern China, with a $160 million fund to attract producers.[35] Qingdao Oriental Movie Metropolis, an enormous film studio development owned by the Dalian Wanda Group, is set to open in April 2017. The complex will include a theme park and entertainment center, a 4,000-room resort-hotel complex, a shopping mall, a 300-berth yacht club, a celebrity wax museum, and a hospital. Wanda Studios Qingdao is going to be one of the largest and most technologically advanced feature-film-production facilities in the world, encompassing 30 sound stages; an enormous, temperature-controlled underwater stage; a green-screen-equipped outdoor stage that is still larger at 56,000 square feet; a permanent facsimile of a New York City street; and much more.

China has the largest cable TV market in the world with 216 million subscribers. Via the media giants Tencent, Baidu, LeTV and Youku Tudou, Through-TV-subscription revenues are projected to reach $462 million in revenues by 2019, up from $314 million in 2015 (13.4 percent).[vi] Electronic home video is expected to reach $480 million (16.6 percent), driven by smartphone and mobile expansion. OTT and streaming will grow at a fast clip of 16.6 percent from $166 million to $291 million during 2015 to 2019, a significant revision downward from the 2013 to 2018 predictions.[vii] Nevertheless, China is the largest IPTV market in the world, yet this sector is also under siege from piracy.

Effective April 1, 2016, SAPPRFT requires foreign films and TV series to register for a "publication license" in order to show content and stream online.[viii] Imported TV series also have to be reviewed by China's censorship authority in their entirety before streaming on the Internet. This has a huge impact on weekly shows. Programs that were not registered by March 31 will be removed from VOD platforms. Finally, a recent 30 percent limit on foreign TV shows and films has been implemented, creating challenges for U.S. industry and raising questions in the context of the 2012 film agreement, which promised to make the process of importing films easier and more transparent.

Music

China's $860 million (2015) music market is dominated by local content and is expected to reach $1 billion in 2019 (5.9 percent). Of this, recorded music will grow 5.3 percent to reach $759 million, led by digital revenues and mobile devices. By 2009, digital had substantially surpassed physical recorded music, and in 2015, the ratio was $625 million digital to $16 million in physical revenues.[ix] This is expected to expand to approximately a ratio of 75:1, or $750 million digital and only $9 million physical recorded music revenues, by 2019.[x]

In contrast to most music markets globally, including any of the top markets in this report, mobile is king at $482 million, dwarfing both streaming services ($95 million in 2015, expected to reach $138 million by 2019) and digital downloads, which will remain steady at $15 million during 2015 to 2019.[xi] The live music market is growing, reached $219 million in 2015 and should expand to $290 million by 2019, presenting performance and touring opportunities for bands that are able to connect with state and festival organizers for a slot for foreign entertainers.

Piracy of creative content is a very significant problem. The USTR reports that 99 percent of music downloads constituted illegal file sharing in its annual Special Report, where China remains on the Priority Watch List of countries with the most rampant piracy rates.[37]

Video Games

China has the third largest video game market in the world after the United States, with Japan coming in second and the UK fourth.[xii] The Chinese games sector posted $9.1 billion in revenues in 2015 and should grow to $12.2 billion by 2019.[xiii] Recently, China ended the ban on the sale of game consoles, such as Xbox and PlayStation, but circumvention devices are proliferating, presenting challenges for new and existing entrants to that market segment. Roughly 345 million Chinese play online games (close to the size of the entire U.S. population), which accounts for the bulk of the industry revenues and has spurred growth in Internet services revenues. Approximately 65 percent of gamers play online games, versus 16 percent on browsers and four percent on PCs. The sector will also generate game-related ad revenues of $399 million by 2019, up from $244 million in 2015.

Publishing

China has the third largest publishing sector for exporters after the United States and Germany.[xiv] However, publishing companies are state-controlled and censored by the Chinese government. While censorship may be seen as a major trade barrier to Western publishers, some authors choose censorship of their works in order to target one of the largest markets in the world.[xv] Total publishing revenue was $12.4 billion in 2015 and is slated to increase slowly but surely to $13.1 billion by 2019.[xvi]

The most important subindustry in China's publishing sector is educational e-books, which, while a small part of the total publishing market, are set to explode in growth at 39.6 percent annually from 2015 to 2019, to reach $57 million – up from $10 million in 2014 and $20 million in 2015.[xvii] However, traditional print textbooks still dominate the publishing market with a whopping $5.5 billion in revenues in 2015 and a slight decline percentage wise to remain at roughly $5.5 billion by 2019.[xviii] The Chinese government is the principle buyer of educational books as the penetration rate of tablets and e-readers in schools are low given the cost for students.[xix]

Consumer and professional e-books comprise the remainder of the publishing market with similar characteristics to the educational subsector. The print book market is significantly larger than the e-book versions, with professional print books in 2015 totaling nearly $2 billion and consumer print books totaling $4.2 billion in 2015. The consumer and professional e-book publishing segments are primed to grow over the 2015 to 2019 period at a rate of 27.6 percent and 11.7 percent respectively, so there are opportunities for U.S. exporters in these two subsectors.[xx] While tablets are not yet prolific, the movement towards e-readers is best demonstrated by the expected decline in consumer print books by 1.4 percent through 2019, from $4.2 billion to $4.0 billion during the same period as popularity in tablets continues to rise.[xxi]

Challenges Facing U.S. M&E Exporters

China remains on the U.S. Special 301 Priority Watch List for IPR due to heavy piracy, especially online, on mobile devices, and from the proliferation of media or set-top box piracy. Rogue manufacturers can access, pre-load and store unauthorized content, including pay TV, movies, music, books and games, and sell them cheaply to users who seek access to premium content without paying subscription or market prices. Consumers can also download content from a multitude of illegal sites, onto set-top boxes or other devices. The set-top boxes are sold all over Asia, including markets where much of the content is not even legally licensed, creating deep losses to rights owners and M&E firms. Pay-TV and signal theft is also on the rise, and illegal camcording of movies in theaters is widespread.

Guidance and Resources for Exporters

The following information is intended to provide guidance and resources for U.S. exporters looking to sell their services in China.

- Typical buyers, licensors and distributors of M&E in China might include state and federal government and select private companies depending on the sector.
- Preferred business strategies to enter/expand in the market might include identifying local partners and co-production companies for distribution and to assist with content and other requirements.
- Common trade barriers to enter/expand in the market might include that most multinational vendors have either a regional or local presence in country. Companies should expect some significant challenges with content restriction and State government overview of M&E sectors.
- U.S. Department of Commerce Country Commercial Guide: http://www.export.gov/ccg/china090765.asp

Industry Trade Associations:

- The Publishers Association of China http://www.pac.org.cn/
- China Audio-video and Digital Publishing Association http://www.chinaav.org/
- American Chamber of Commerce in China: http://www.amchamchina.org/

Government Agencies:

- State Administration of Press, Publication, Radio, Film and Television (SAPPRFT) http://www.sapprft.gov.cn

Trade Shows:

Filmed Entertainment

- Beijing International Film Festival April 16 – 23, 2016 http://www.bjiff.com/enHome/
- Shanghai International Film Festival June 17 – 23, 2016 http://www.siff.net/festival-2016
- Taipei Film Festival June 30 - July 16 2016 http://eng.taipeiff.org.tw/Content.aspx?FwebID=113eab9d-8fae-4e6e-9ed9-06b9dd2f0648
- Qingdao International Film Festival Launching Fall 2017 (Dates TBD)
- Hong Kong Filmart March 13 – 16 2017 http://www.hktdc.com/fair/hkfilmart-en/s/4121-General_Information/Hong-Kong-International-Film---TV-Market--FILMART-/Fair-Details.html

Music

- YinYang Music Festival September 15 – 17, 2016 http://www.yinyangmusicfestival.com/

Publishing

- Beijing International Book Fair, Aug 24 - 28, 2016, Beijing, China: http://bibf.net/EN
- China Shanghai International Children's Book Fair, Nov 18 – 20, 2016, Shanghai, China: http://www.ccbookfair.com/en/

Video Games

- China Joy July 28 – 31, 2016, Shanghai, China: http://en2016.chinajoy.net/

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[i] China Briefing: Market Overview: The Entertainment Industry in China - See more at: http://www.china- briefing.com/news/2015/03/06/market-overview-entertainment-industry-china.html#sthash.7VrfgA9L.dpuf. Business Intelligence from Dezan Shira & Associates, March 6, 2015.

[ii] Pricewaterhouse Coopers, "Global media and entertainment outlook," http://www.pwcmediaoutlook.com/dataexplorer, accessed 1/3/2016.

[iii] Julie, Makinen, *Los Angeles Times*, "Movie ticket sales jump 48% in China, but Hollywood still has reason to worry," http://www.latimes.com/entertainment/envelope/cotown/la-et-1230-ct-china-box-office-20151230-story.html, accessed 01/3/2016.

[iv] Ibid, accessed 1/3/2016.

[v] Ibid, accessed 1/3/2016.
[vi] Pricewaterhouse Coopers, "Global media and entertainment outlook," http://www.pwcmediaoutlook.com/dataexplorer, accessed 1/3/2016.
[vii] Pricewaterhouse Coopers, "Global media and entertainment outlook," http://www.pwcmediaoutlook.com/dataexplorer, accessed 1/3/2016.
[viii] SAPPRFT Publication License for foreign TV & Film effective April 1, 2015
http://www.sarft.gov.cn/articles/2014/09/05/20140904102409770812.html
[ix] Pricewaterhouse Coopers, "Global media and entertainment outlook," http://www.pwcmediaoutlook.com/dataexplorer, accessed 1/3/2016.
[x] Pricewaterhouse Coopers, "Global media and entertainment outlook," http://www.pwcmediaoutlook.com/dataexplorer, accessed 1/3/2016.
[xi] Pricewaterhouse Coopers, "Global media and entertainment outlook," http://www.pwcmediaoutlook.com/dataexplorer, accessed 1/3/2016.
[xii] Pricewaterhouse Coopers, "Global media and entertainment outlook," http://www.pwcmediaoutlook.com/dataexplorer, accessed 1/3/2016.
[xiii] Pricewaterhouse Coopers, "Global media and entertainment outlook," http://www.pwcmediaoutlook.com/dataexplorer, accessed 1/3/2016.
[xiv] Pricewaterhouse Coopers, "Global media and entertainment outlook," http://www.pwcmediaoutlook.com/dataexplorer, accessed 12/31/2015.
[xv] [xv] Pricewaterhouse Coopers, "Global media and entertainment outlook," http://www.pwcmediaoutlook.com/dataexplorer, accessed 12/31/2015.
[xvi] Pricewaterhouse Coopers, "Global media and entertainment outlook," http://www.pwcmediaoutlook.com/dataexplorer, accessed 12/31/2015.
[xvii] Pricewaterhouse Coopers, "Global media and entertainment outlook," http://www.pwcmediaoutlook.com/dataexplorer, accessed 12/31/2015.
[xviii] Pricewaterhouse Coopers, "Global media and entertainment outlook," http://www.pwcmediaoutlook.com/dataexplorer, accessed 1/3/2016.
[xix] Pricewaterhouse Coopers, "Global media and entertainment outlook," http://www.pwcmediaoutlook.com/dataexplorer, accessed 1/3/2016.
[xx] Pricewaterhouse Coopers, "Global media and entertainment outlook," http://www.pwcmediaoutlook.com/dataexplorer, accessed 1/3/2016.
[xxi] Pricewaterhouse Coopers, "Global media and entertainment outlook," http://www.pwcmediaoutlook.com/dataexplorer, accessed 1/3/2016.