



THE WAY OF THE BLOCKBUSTER

In entertainment, big bets on likely winners rule.

by CRAIG LAMBERT

In 2006, Chris Anderson, then editor of *Wired* magazine, published *The Long Tail: Why the Future of Business is Selling Less of More*. He argued that the Internet era was changing markets. Take books, the original niche of Amazon.com. As an online vendor, Amazon can stock far more titles than any brick-and-mortar bookstore—so instead of cashing in on 50 bestsellers, Amazon could prosper by selling a few copies each of 100,000 different titles. We are moving away, said Anderson, from a demand curve focused on the “head” of a statistical distribution—where there are many occurrences of one value (“mega-hits”)—and toward the “long tail” of the distribution, where there are many different values, but only a few occurrences of each one.

Hence, he projected, Amazon would tap a goldmine of existing assets, as older “backlist” books continued selling for years. Netflix would cash in on movie studios’ vaults—never mind the current box-office smash. The profusion of cable- and satellite-TV channels would make a thousand niche programs bloom in a million living rooms, not just a couple dozen crowd-pleasers atop the Nielsen ratings. A new, far more diversified era of entertainment was at hand.

Yet, today, movie studios are still making \$200-million new films; book publishers are still paying huge advances for potential bestsellers; and Amazon and Netflix, instead of focusing only on backlists and vaults, are investing millions of dollars in original programming. How can this be?

The answer comes in *Blockbusters: Hit-Making, Risk-Taking, and the Big Business of Entertainment*, the new book by Anita Elberse, Filene

professor of business administration. Elberse (el-BER-see) spent 10 years interviewing and observing film, television, publishing, and sports executives to distill the most profitable strategy for these high-profile, unpredictable marketplaces. She even spent time with star performers like Lady Gaga, Jay-Z, and LeBron James. Her conclusion is the opposite of Anderson’s. The most profitable business strategy, she says, is not the “long tail,” but its converse: blockbusters like *Star Wars*, *Avatar*, *Friends*, the *Harry Potter* series, and sports superstars like Tom Brady.

Strategically, the blockbuster approach involves “making disproportionately big investments in a few products designed to appeal to mass audiences,” Elberse explains. “Smart executives bet heavily on a few likely winners. That’s where the big payoffs come from.” Her book opens its case with a pair of contrasting stories that are almost media-industry parables.

In the film business, many consider the 1975 movie *Jaws* the first big summer blockbuster. But no studio pursued a consistent strategy of shooting for blockbusters until Alan Horn, M.B.A. ’71, became president and CEO of Warner Brothers in 1999. A central figure in *Blockbusters*, Horn began making a handful of big bets on “event movies” each year. “In the movie business, the product is the same price to the consumer regardless of the cost of manufacturing it—whether its production budget is \$15 million or \$150 million,” he told her. “So it may be counterintuitive to spend more

money. But in the end, it is all about getting people to come to the theater. The idea was that movies with greater production value should be more appealing to prospective moviegoers.”

“Production value” means star actors and special effects. Reaching moviegoers also means big advertising and marketing budgets. All these things drive up costs, so a studio can afford only a few “event movies” per year. But Horn’s big bets for Warner Brothers—the *Harry Potter* series, *The Dark Knight*, *The Hangover* and its sequel, *Ocean’s Eleven* and its two sequels, *Sherlock Holmes*—drew huge audiences. By 2011, Warner became the first movie studio to surpass \$1 billion in domestic box-office receipts for 11 consecutive years. “Alan was the first person in the film industry to show that this resource-allocation strategy worked,” says Elberse.

Meanwhile, Jeff Zucker ’86 put a contrasting plan into place as CEO at NBC Universal. In 2007 he led a push to cut the television network’s programming costs: a policy of “managing for margins instead of ratings.” Zucker installed colleague Ben Silverman as co-chair of NBC Entertainment. Silverman began cutting back on expensive dramatic content, instead acquiring rights to more reasonably priced properties; eschewing star actors and prominent TV producers, who commanded hefty fees; and authorizing fewer costly pilots for new series. The result was that by 2010, NBC was no longer the top-rated TV network, but had fallen to fourth place behind ABC, CBS, and Fox, and “was farther behind on all the metrics that mattered,” writes Elberse, “including, by all accounts, the profit margins Zucker and Silverman had sought most.” Zucker was asked to leave his job in 2010. Elberse concludes that his “managing for margins” strategy “had disastrous results.”

The Unique Nature of Show Business

ENTERTAINMENT IS CLEARLY a risky, high-stakes game with both enormous payoffs and calamitous failures that play out in an environment of maddening uncertainty.

Certain characteristics distinguish entertainment from other industries. First, “creative products such as films and television shows are generally relatively expensive to produce, but very cheap to reproduce,” writes Elberse. For makers of Cadillacs or cornflakes, selling more units means *making* more units and hence, even with economies of scale, higher manufacturing costs. In contrast, making the first copy of a movie can cost tens or even hundreds of millions of dollars, but subsequent prints for theatrical release cost only a few thousand dollars apiece—with DVDs drastically less and Netflix distribution cheaper still. Similar economics apply to hardcover, paperback, and e-books. The sharp disjunction between costs of production and *reproduction* means that “hit products are disproportionately profitable.” Elberse writes that “the more copies are sold, the more the production costs can be divided over those copies.” (Pharmaceutical and software businesses show a similar disjunction between costs of production and reproduction, with a similar result: a high value placed on big “hits” like Lipitor and Facebook.)

Second, creative products are what economists call “experience goods.” The vendor is not selling an object or providing a known service, but instead offering an experience. (With live performances, it’s also an evanescent experience: unsold seats at a concert today—like those on an airline flight—are worthless tomorrow.) *Consumer Reports* cannot test a new film in a lab, like a new dishwasher, and evaluate its performance for moviegoers. That makes

it harder for customers to know in advance if the “experience” for sale is one they’d like to have, so critics and word-of-mouth comments from other consumers play major roles in marketing, and subjective judgments rule. There are few, if any, “objective” claims to high quality, and customers disagree on what is good, so their choices reflect tastes, not verifiable differences in quality.

Third, entertainment products—films, books, television—are essentially priced uniformly, as Alan Horn recognized. A movie ticket is \$10, for a hit or a bomb. Book prices vary within a narrow range. The basic commercial approach of attracting customers with lower prices, discounts, sales, and coupons doesn’t apply. The market turns on differences in quality.

Finally, and most important, consumer demand for entertainment products is unpredictable. Entertainment is not a basic need like food or shelter, nor even a secondary need like furniture or transportation. Seeing a movie, hearing a song, or watching a basketball game is completely optional. There are algorithms to forecast how many tubes of Colgate toothpaste will sell next year, but trying to estimate the gross receipts of a hip-hop song or feature film is a crapshoot. In Hollywood, as screenwriter William Goldman famously said, “Nobody knows anything.”

Consider the 1998 film *Beloved*, starring Oprah Winfrey, based on Nobel Prize-winner Toni Morrison’s eponymous 1987 novel and directed by Oscar-winner Jonathan Demme—a team that sounds like a recipe for success. Yet *Beloved* flopped resoundingly: produced for \$80 million, it sold only \$23 million in tickets. After its anemic opening, *The New York Times* quoted Joe Roth, chairman of Walt Disney Studios, which released the film, saying, “All there is, is pain.”

These special characteristics of entertainment make creators and vendors feel their marketplace is much like a minefield—it is hard to know where to step, and a misstep could trigger a catastrophe like *Beloved*. Yet this minefield also conceals enormous treasure chests belowground. Given the essential unpredictability, even irrationality, of the market, entertainment executives rely on several tactics in an attempt to bring its unruly elements under control.

Taming the Media Jungle

A NEW FILM, book, or television show is much like a new-product release: Job One is to get the public to pay attention to something it has never heard of, so the rollout often connects the new release to something people *have* heard of. This explains Hollywood’s weakness for sequels and for movies based on television series, from *Get Smart* to *Sex and the City*. “Copycat” programming offers executives the security blanket of proven winners—thus a hit like Fox Television’s *American Idol* (itself cloned from the British series *Pop Idol*) inevitably spawned a rash of other talent shows, like NBC’s *The Voice*.

In addition, when Horn was running Warner Brothers, “many of the studio’s event films were based on properties that had established their value in other domains,” Elberse writes. *Harry Potter* was a juggernaut in book form before becoming one in the movies. The *Batman* comic-book series gave birth to *The Dark Knight*, and the Marvel comic-book empire of superheroes like *Spider-Man*, *The Hulk*, *Iron Man*, and *Thor* has proved a fountainhead of hit-film characters. From a business perspective, “bankable” movies stars like Julia Roberts, Johnny Depp, or George Clooney func-

tion in much the way Harry Potter and Superman do: providing a known, well-liked persona.

Big names, whether real or fictional, are essentially *brand* names, and branding is one way to bring familiarity and repeatability to the volatility of the marketplace. Brand names can also generate multiple streams of revenue. “Those behemoth movies throw off all kinds of ancillary businesses,” says Lucy Fisher ’71, formerly vice chair of Columbia TriStar Motion Picture Group. She is now co-head of Red Wagon Entertainment, a motion-picture production company in Los Angeles; its most recent blockbuster was the 2013 version of *The Great Gatsby*. “There are amusement-park rides, toys, clothes merchandising, sequels, spinoffs, songs—things that go on past the life of the original film,” Fisher elaborates. “Movies like *Brokeback Mountain* or *Slumdog Millionaire*—which might once have been referred to as ‘wonderful movies’—in the business are now referred to as ‘one-offs.’”

Perhaps no entertainment realm takes greater care in building a brand name than professional sports: fan loyalty reliably builds repeat business. “The NFL is blockbuster content,” Elberse says. “It’s the most sought-after content we have in this country. Four of the five highest-rated television shows [in the United States] *ever* are Super Bowls. NFL fans spend an average of 9.5 hours per week on games and related content. That gives the league enormous power when it comes to negotiating contracts with television networks.”

Elberse has studied American football and basketball and European soccer, and found that selling pro sports has much in common with selling movies, TV shows, or books. Look at the Real Madrid soccer club—the world’s richest, with annual revenues of \$693 million and a valuation of \$3.3 billion. Like Hollywood studios, Real Madrid attracts fan interest by engaging superstars—such as Cristiano Ronaldo, the Portuguese forward the club acquired from Manchester United for a record \$131.6 million in 2009. “We think of ourselves as content producers,” a Real Madrid executive told Elberse, “and we think of our product—the match—as a movie.” As she puts it: “It might not have Tom Cruise in it, but they do have Cristiano Ronaldo starring. Real Madrid is fully aware that they can learn a lot from the way that Hollywood studios manage their business.”

In team sports, “the measure of success is *winning*,” says Bart Waldman ’70, executive vice president for legal and governmental affairs and general counsel for the Seattle Mariners baseball team. “Winning brings fans, television audience, and everything else that makes our business model work. Bringing in a superstar who adds panache and some glitz but doesn’t change the win/loss picture doesn’t move the needle the way winning does. It really depends on whether your team is poised to take advantage of what that superstar brings. In baseball, the marginal value of each victory increases as you approach or surpass 90 wins—the number that typically puts you in the playoff picture. A superstar who adds five wins, taking you from 75 to 80 wins, doesn’t add much value by himself. But the same superstar who takes you from 90 to 95 wins probably puts you in postseason play, adding a ton of value.”

So loyal fans and superstars can help. Another way to hedge big bets is to back them with mighty advertising and marketing campaigns. “You want to use your distribution and marketing power to *make* a hit,” Elberse says. “Advertise a lot to make sure that everyone is aware of it, and leverage your distribution power to make it easy for the public to obtain—get your film on lots of

screens, get your book on a bookstore display table. The blockbuster strategy is trying to take away the uncertainty.” In movies, “if you’ve already spent \$200 million to produce a film, it’s easier to say, ‘Let’s spend another \$100 million to advertise it.’”

Blockbusters offers data to show that advertising event movies is disproportionately cheap compared to smaller-budget films. In 2010, for example, Warner’s top three movies consumed a third of the studio’s production budget, but only 22 percent of its \$700-million advertising budget. “In marketing, we call it ‘breaking through the clutter,’” Elberse says. “It’s about getting the customer to say, ‘If I see only one movie this weekend, or buy only one book, *this* is the one it has to be.’ It becomes a self-fulfilling prophecy.”

The Internet amplifies opportunities for global blockbusters, perhaps especially for products like movies, music, and sports that offer an essentially visual, auditory, and/or nonverbal appeal. Social media like Facebook, YouTube, and Twitter help create international sensations like the South Korean singer-rapper-dancer Psy, whose viral “Gangnam Style” video has attracted a record 1.8 billion views on YouTube since 2012. “With global markets opening up,” Elberse predicts, “we’ll have even bigger superstars.”

No performer has better exploited electronic communications than Lady Gaga. Her spectacular visual presentations, including colored wigs and extraordinary, even outlandish, makeup and attire, clicked in combination with her music to “break through the clutter” in a dazzling way. “Lady Gaga is a star because she was just unattainable—this fashion icon who is unlike any of us,” Elberse explains. “For every occasion, she was dressing up extensively—in the first few years, you never saw Lady Gaga in regular clothes. Many people had no idea what she looked like.”

Even with Internet support, however, superstardom—and entertainment-marketing success—depends on more than a virtual presence. In 2011, eight million different songs sold at least one copy. “But people don’t realize that about one-third of these songs sold *exactly* one copy,” she says. “Few understand how thin the tail is, how concentrated these markets are. There is an enormous amount of content that gets no demand at all.” It’s cheap to post homemade movies, self-published books, and garage recordings, but the global audience is simply not congregating to view, read, and hear these grassroots products.

Superstars and blockbusters now form an essential part of the entertainment complex. Ironically, they may even make possible many of the industry’s less popular, more experimental releases. Take Steven Soderbergh, who has directed Hollywood hits like *Traffic*, *Erin Brockovich*, and *Ocean’s Eleven* and its sequels, as well as smaller vehicles such as *Che*, *Syriana*, and *Sex, Lies, and Videotape*. “We would not know who Steven Soderbergh is without his blockbusters,” Elberse says. “Without them, I don’t think he could get the financing to make his riskier films. And I enjoy all his films, so I’m grateful for that. Of course I understand concerns about the diversity of content, and the fact that certain elements people like are disappearing. But overall I’m not that pessimistic. It’s not a hobby, it’s a business. At the end of the day, the Hollywood studios have to make money to survive another year, to put out more great products.” ▽

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