A political economy of online film exhibition in China

Kan Peng
Hong Kong Baptist University

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Student No: 10466088
Department: Communication School
Degree Type (check one): ☐ PhD. ☑ MPhil.
Date of Graduation: 11 (month) 2013 (year)
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This is to certify that the above student's thesis has been examined by the following panel members and has received full approval for acceptance in partial fulfillment of the requirements for the degree of Master of Philosophy.

Chairman: Prof XIAO Xiaosui
Professor, Department of Communication Studies, HKBU
(Designated by the Dean of School of Communication)

Internal Members: Prof CHEUK Pak Tong
Director, Academy of Film, HKBU

Prof YEH Emilie Y Y
Professor, Academy of Film, HKBU

External Member: Prof LU Sheldon
Professor of Comparative Literature and Graduate Adviser
Department of Comparative Literature
University of California, Davis
U.S.A

Chairman's Signature:  
Dr XIAO Xiaosui  

Principal Supervisor's Signature:  
Prof YEH Emilie Y Y  

Signature:
A Political Economy of Online Film Exhibition in China

PENG Kan

A thesis submitted in partial fulfillment of the requirements
for the degree of
Master of Philosophy

Principal Supervisor: Prof. Emilie YEH

Hong Kong Baptist University
November 2013
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I hereby declare that this thesis represents my own work which has been done after registration for the degree of MPhil at Hong Kong Baptist University, and has not been previously included in a thesis or dissertation submitted to this or any other institution for a degree, diploma or other qualification.

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Abstract

As one of the most revolutionary technologies in human history, the Internet has dramatically transformed the media industry, including the film exhibition industry. In China, new online exhibition networks have continuously been established to exploit the lucrative markets of Internet users' online viewing and sharing habits. The destinies of different types of films in the Chinese market have been greatly changed due to the increasing connections and contradictions between China's Internet and film exhibition industry which are influenced by many political economy factors, such as the conflicting interests among different government departments. Therefore, this paper examines the Internet's impact on film exhibition in China from a political economy perspective.

The thesis first traces the history of two online exhibition networks related to China's film market. One is the online video websites that accumulated their early capital by piracy content, but which were then progressively legalized under the forces of venture capital and government administration. The other is the online piracy network, which has become a problem for film industries worldwide, due to its transnational, decentralized and limitless network. However, this network also functions as a democratic tool to combat with the ideological controls of the government. This thesis argues that these two online exhibition networks are fated to conflict with each other since they operate under two conflicting logics. The former operates in the logic of capital gains, while the latter celebrates the logic of communal sharing and exchange.
Based on the analysis of the dynamic between these two online exhibition networks, this thesis further investigates how, in the context of China’s particular political economy, three different types of film are influenced by the two networks. The first is Chinese commercial films, which are making more and more profits from online video websites, while facing the challenge of online piracy. The second are foreign films, which are expanding their influence and bypassing the entry barriers into the Chinese market through the online video websites and piracy networks. The third are so-called Chinese independent films. As these films cannot be distributed through state-controlled channels, Chinese independent film’s domestic circulation was once quite confined. For independent films, the Internet has become an important exhibition channel that extends their influence to a wider domestic audience and even a bargaining chip with which to negotiate with the state’s rigorous censorship system.
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Several people in the Chinese film industry were interviewed for this study. And my colleagues in Entgroup helped me collecting many useful data. I appreciate their support. Without their knowledge and their kindness of sharing that knowledge with me, this study would have made many errors.

Finally, I wish to extend my gratitude to my family for their love and support.

Any error that may follow is my full and sole responsibility.
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Chapter 1: Introduction

Research background

As one of the most revolutionary technologies in human history, the Internet has dramatically transformed the media industry around the world. In China, hundreds of thousands of Chinese language websites have emerged since the mid-1990s and the number of Internet users has increased dramatically. According to *The 32th Statistical Report on Internet Development in China*, there were 591 million Chinese Internet users by the end of June 2013 (CNNIC, 2013). More and more Chinese people use the Internet as a news source, to learn various skills, to enjoy entertainment, and express their opinions. The Internet is emerging as an ever more dynamic force in China’s political, economic and social transformation (Liu, 2004).

The Internet is also playing an increasingly important role in the development of China’s film industry, especially the film exhibition sector. Before the 1950s, films could only be viewed in theatres. Then the popularizing of television, videos and DVDs expanded the film exhibition business to a much wider scale. Nowadays, the exhibition of films has entered a new era with the Internet providing another channel for audiences to consume, share and review films.

The Internet has transformed the traditional film exhibition business by providing an online marketing platform. Today, all cinema circuits in China have established their own websites to provide screening schedules and promotional information about the films they are showing. Many of them also allow people to buy tickets online. Moreover, there are more and more cinemas using the increasingly popular group purchase website to attract audiences with
lower prices. According to data provided by Entgroup, during the first 11 months of 2012, the turnover from online group purchases of tickets for film screenings was 1.58 billion yuan in China, which accounted for more than one tenth of the total box office revenues during that period.

However, it is not the Internet per se but the booming online video websites that have really transformed the film exhibition business. Since 2005, inspired by the success of Youtube, many Chinese online video websites emerged to capitalize on the rapidly increasing number of Internet users who like to view films online. According to The 31th Statistical Report on Internet Development in China, the number of online video users in China reached 372 million by the end of December 2012, which accounted for 65.1 percent of Internet users (CNNIC, 2013). According to an estimate by Iresearch, the online video market in China will maintain an annual growth rate of more than 35 percent between 2012 and 2016 (Iresearch, 2013). For the operation of online video websites, film is an important part of their business because of its high attractiveness to their target audience. According to the data from Iresearch, Chinese Internet users spent more than 3.7 billion hours in 2012 watching films online. And the most popular films attracted more than 20 million online audiences in just a month (Iresearch, 2013). Therefore, the online video websites have purchased more and more films from the copyright holders and made great efforts to develop their online exhibition business models, such as ad-supported viewing, premium video-on-demand and subscription, to profit from online viewers. And some large video-sharing websites have gone even further and
formed an “online cinema chain” to enhance their bargaining power with the film companies and to develop the online film exhibition market in China.

The Internet is mainly deemed as a benefit source for the film industry in China with the development of online video websites. However, the Internet has also brought big challenges to China’s film industry. The biggest challenge is the ever more serious problem of film piracy, because the online sharing of pirated films has reduced the per-unit marginal costs of reproducing films to virtually zero and the users can share pirated films easily, widely, and quickly (Currah, 2003). Therefore, the online piracy network is much more destructive than the offline piracy network, especially in China, where pirated films can be circulated online just a few days after their theatrical release (Wu, et al., 2011). Most Chinese online video websites gained their foothold by providing piracy films and television programmes when they started, although the government, foreign venture capitalists and the advertisement clients of those websites changed this.

From the above descriptions, it is clear that the Internet has brought substantial changes to film exhibition in China. And there are many interesting issues around these changes that need to be examined. For example, what is the relationship between online exhibition networks and traditional exhibition channels? Why do the main online video websites need to remove pirated films? How are they developing business models under the threat of piracy? How does the development of the online exhibition networks transform the exhibition of different kinds of films in China in distinctive ways? This paper aims to answer these
questions. And as explained in the next part, these questions cannot be easily understood within the isolated technical or economical context, but should be understood within the context of China's political economy.

Literature review

Definition of political economy research on film industry

As an academic perspective which focuses on social relations, particularly power relations, that mutually constitute the production, exhibition, and consumption of resources in a capitalist society, political economy research was originally formulated by the "classical" political economists, such as Adam Smith, who analyzed the Industrial Revolution by drawing on Enlightenment moral philosophies and empirical approaches in the eighteenth century, and Karl Marx who emphasized a radical critique of the evolving capitalist system through historical materialism and class analysis (Holt & Perren, 2009; Mosco, 2009). Then with communication research rapidly developing into a new discipline after World War II, the theoretical concepts and analytic frameworks of political economy research were borrowed by communication scholars to analyze communication systems and media industries around the world, particularly the rapid growth of media companies into transnational businesses, the government's role in the development and administration of media industries, the consequences of the fast evolving information and communication technologies, and the phenomenon of cultural imperialism through the media. Political economy analysis therefore
gradually evolved into one of the major perspectives in communication research (Mosco, 2009).

Due to the differences in economic, political and cultural contexts in different countries, various strands of political economy research on communication can be distinguished by their different focus. But according to Vincent Mosco (2009), Graham Murdoch and Peter Golding (1996), these strands also share some common characteristics in their basic approach. Firstly, the political economy approach is historical. It has constantly focused on understanding social change and the historical transformation of capitalist societies. Secondly, the political economy approach is holistic. It is interested in examining the social whole, or the totality of social relations. Thirdly, the political economy approach is critical. It follows the classical theorists' emphasis on moral philosophy and engages with basic moral questions of justice, equity and the public good. Fourthly, political economy is social praxis. It attempts to transcend the distinction between the thinking and doing, orienting towards social change and practice (Mosco, 2009; Murdock & Golding, 1996).

When scholars intend to study the film industry through the lens of the political economy, they need to follow these four criteria, which distinguish political economy analysis from other approaches. As Janet Wasko (2004, 2005) has indicated, study of the film industry through the lens of the political economy must understand films as commodities produced and distributed within a capitalist industrial structure, which has been constructed in a historical process. Meanwhile, political economical scholars need to focus on the film industry structure
and performance as industrial analysts do. The political economy therefore galvanizes a holistic approach that examines the film industry to be part of the larger communication and media industry and society as a whole. Political economy analysis of the film industry should not only be an elaborate description of the state of the industry, it should also be critical with the ambition to challenge the status quo.

Along with the rapid development of the new media technologies, which have dramatically transformed people's lives, political economy research has become an increasingly important perspective with which to view the media industry since the 1940s. However, political economy analysis of the film industry is still undeveloped. It was not until the 1960s that a political economy perspective was brought to film studies by Thomas Guback and his work on the international film market. And since then, there are still not many works on film that can be regarded as political economy research. As Janet Wasko (2004) has pointed out, film studies have typically showed a bias towards textual analysis and neglected the analysis of cinema as an economic institution. She argues this is, firstly, because film studies typically are based in the humanities, which focus on the artistic and ideological dimension of film works; secondly, for the researchers who hold a political economy orientation, film often represents "only entertainment" and is thus not as worthy of scholarly attention as news distribution or computer and information technologies; and thirdly, access to film texts is relatively easy, whereas finding reliable and relevant data about the film industry on which to base a critical analysis is more difficult, as different data sources may have very different orientations and
thus distort the data they provide (pp. 227-230).

The existing research on China’s film industry from a political economy perspective

Among the studies of China’s film industry, political economy research is also underdeveloped. With the rise of the Fifth Generation of Chinese filmmakers in the mid-1980s, Chinese films became a hot topic in film studies, Asian studies, historical studies and literary studies. According to the list of “book-length studies of Chinese cinema published by the Journal of Chinese Cinema (Williams, 2007; Wang, 2008; Wang, 2009; Wang, 2010), there are already more than 100 English book-length publications on Chinese films from perspectives such as historical research, genre studies, auteur studies, aesthetic criticism, gender studies, and cultural studies. However, few of them employ a political economy perspective. Through checking the publications listed by the Journal of Chinese Cinema and searching the databases of dissertations and journal articles, I found only around 20 academic publications on Chinese films that employ a political economy perspective, and only six of them are books or dissertations, the others are individual articles published in anthologies or

Among these publications, the main focuses are the transformation of China’s film industry since the introduction of market economy (Zhu, 2003; Nakajima, 2007; Zhou, 2007; Zhu & Nakajima, 2010); Chinese government’s policy on censorship and film copyrights (Montgomery, 2004; Gao, 2009; Wang, 2003, 2010); the relationship between China’s film industry and Hollywood (Wang, 2006; Su, 2009) and a political economic study on China Film Group (Yeh & Davis, 2008). While in China, research on film industry has become a hot field along with the marketization reform and open up of Chinese film market. Basically, these research can be classified into four strands. The first is topical research which tightly traces the development of Chinese film industry and provides timely observation. For instance, Yin Hong began to publish his annual summary report on Chinese film industry since 2003 on the journal Film Art, whereas since 2007, the Industry Research Center of China Film
Association also published the annual research report on Chinese film industry every year; the second is from historical perspective, which chronicles the development and reform process of Chinese film industry in a more systematic way (Tang, 2002; Shen, 2005; Yin, 2007; Rao, 2009); The third is application research which offers insights on the operating strategies of film business, especially on the film financing and marketing (Tang & Shao, 2005; Yu, 2006; Xia, 2009; Yu, 2012; Wu, 2012); And the fourth is policy research which aims at influence the official policy on Chinese film industry (Zhang & Yang, 2002; Industry Research Center of China Film Association, 2008, 2009, 2010; Zhu, 2009; He, 2012). Among these researches, political economy theory and analytical framework were frequently applied, but little of them can be actually counted as political economy research, 3 since they generally held a celebrating orientation rather than critical stance towards the development of Chinese film industry. In China, where the academic journal and press are administrated by propaganda departments and the research funds are generally sponsored by the government, it is actually quite difficult for the scholars to hold a critical stance as political economy research requires.

Moreover, the limitation of existing political economy studies on Chinese film is not just reflecting in the amount, but also reflecting in the research scope. According to Vincent Mosco (2009), today’s political economy research on communication has switched “to a focus

3 The publications can be counted as political economy research include: Zhang Zhenqin and Yang Yuanying, eds., WTO and China Film (Beijing: China Film Press, 2002); Yin Hong, Across One Hundred Years: Chinese Film Under the Background of Globalization (Beijing: Tsinghua University Press, 2007); Zhu Hong, The Financial Crisis and China Film (Beijing: Hongqi Press, 2009); He Chun Geng, Research on Chinese Film Industry and Policy Development, (Beijing: Xinhua Press, 2012).
on new media, especially the Internet and the new media forms that it has stimulated" (p. 119).

The media industries are changing as quickly as ever; and there is a strong demand for research that attempts to make sense of the transformations being brought about by the Internet, digitalization, audience fragmentation, and new developments in intellectual property (Holt & Perren, 2009, p. 246). However, so far this concern has not been fully addressed by scholars in Chinese media except Zhao Yuezhi (2008) and Pang Laikwan (2006, 2012). Zhao provides an insightful analysis in her book on how the Chinese partystate change their regime of media control and censorship to get with the advance in new media technologies, while Pang focus on how are the Chinese creative industries challenged by the intellectual property rights offenses brought by the development of new media.

While in the research field of Chinese film, as Darrell Davis and Emilie Yeh (2008) have indicated, the existing political economy studies have yet to venture into media convergence, although the boom in new media has increasingly transformed the traditional business model of the film industry and also the ways audiences consume movies. Thus, through an initial but systematic examination of the impact the Internet, which is the most important of the new media, is having on the film exhibition industry in China, this paper hopes to call for more research in this area.

**The existing research on the Internet’s impact on film exhibition**

To examine the Internet’s impact on the film industry, the first question we should ask is what
are the specific characteristics of the Internet? Basically, the Internet refers to a telephony-based system that links computers and computer networks worldwide to permit exhibition of information to users (Kung, Picard & Towse, 2008, p. 3). Although the history of the Internet can be traced back to 1968 when the overall structure and specifications of the advanced research agency network (ARPANET- the earliest precursor of the Internet) was finalized (Henten & Tadayoni, 2008, pp. 49-50), it was actually not until the emergence of World Wide Web in the 1990s that the Internet began to have a serious impact on the media. By providing browsers for users to access not just text message, but also graphics, photography, video and audio materials, in an easily accessible and sharable environment, the World Wide Web caused revolutionary upheavals in the media industry.

However, the development of the Internet was not an isolated process. It has been argued the Internet is actually "a catch-all phrase for a number of technological developments that relate to economic and social changes" (Kung, Picard & Towse, 2008, p. 3). The Internet is not a fixed and finite thing, it has developed over time by incorporating updated technological developments. It has been further argued that the Internet is best understood as a part of the broader process of digitalization — the increasing use of digital, as opposed to analogue systems of storage and transmission (Hesmondhalgh, 2007, p. 75). Digitalization technology converts different forms of communication — words, images and sounds — into binary code, thus making communication more transportable and manipulable than before, and making different media potentially more interconnectable. The World Wide Web is a revolutionary
platform that integrates different forms of media.

Thanks to the Internet the “broadcasting model” of one-way communication, from a powerful central agency to dispersed and mutually disconnected passive consumers, is giving way at an unprecedented pace to a “broadband model”, in which users are linked in social networks, and productive energy can come from anywhere in the system (Hartley, 2009, p. 234). Rather than traditional broadcast media’s “audience-subjectivity”, the Internet has encouraged “user-subjectivity” in which individuals produce cultural activities by themselves (Marshall, 2006). The Internet has turned individuals into “produsers”, their online activities as much about producing as consuming (Bruns, 2005).

In film studies, there has already been some research examining the Internet’s impact on different sectors of film industry. For the film distribution sector, the focus has been on the Internet’s “disruptive” effect on the traditional film distribution model. In the traditional sense, films are typically distributed in sequential release windows: theatres, videos, pay-per-view television, premium film channels, and finally the cable/network/syndicated television networks. This release windows strategy is crucial to maximize the revenues for films. But as the Internet has increasingly become a viable exhibition channel, it has not only accelerated the process of duplicating and distributing films, more importantly, it is also a cheaper channel for the user than traditional film exhibition channels, especially the buying or renting of videos, pay-per-view television, and premium film channels, which are now heavily challenged by the Internet. Evidence of this challenge is the fate of Blockbuster Inc., once the
dominant movie rental company in the U.S., which filed for bankruptcy protection in September, 2010 (Anderson, 2010). How to cope with the challenge of the Internet is a huge problem for film distributors and exhibitors. As Andrew Currah indicates in his paper on the relationship between Hollywood and the Internet, the decentralized electronic architecture of the Internet seriously contradicts the oligopolistic structure of Hollywood studios, which are oriented around centralized server-client architectures. To deal with the challenge of the Internet, the Hollywood studios are trying to preserve the oligopolistic structure of the film industry by promoting an inefficient and restrictive design for Internet exhibition. The studios confine the Internet to a tiny pay-per-view window, sandwiched between home video and pay-to-view television, so as to protect the current spatial and temporal structure of film release windows (Currah, 2006, pp. 450-451). But this kind of shielding strategy is probably unsustainable in the future as more and more people choose to watch films online.

Besides the Internet’s disruptive effect on the traditional film distribution model, there are some other challenges it brings to film distribution. One of them is the so-called “disintermediation” effect. Some scholars argue that as film production companies or even independent filmmakers can directly deliver their films to consumers via the Internet, the importance of the movie distributor will decrease and the power structure of the film industry will be transformed (Zhu, 2001). Another issue is the problem of piracy, which has become more serious as popularity of online viewing has increased. As Hesmondhalgh (2007) has indicated, making a profit in the film and other cultural industries depends on, among other
factors, the production of artificial scarcity, but the Internet enables all kinds of digital files to be shared at virtually zero marginal cost (Currah, 2007), thus heavily threatening the artificial scarcity and thus profitability of films. The problem of film piracy has become a global issue, because nowadays Internet users can share piracy films easily, widely, and quickly.

In the film exhibition sector, analysis has focused on the Internet’s “dematerialization” effect, which means the digital delivery of films has increasingly displaced physical films, videos and DVDs (Cohen, 2010). Nowadays, films can be sent digitally over the IP network to targeted theatres, can be downloaded through P2P software and various “private” upload sites, or directly watched on video websites such as Hulu, Youtube, and Netflix. Moreover, with the rapid development of wireless networks and more and more portable equipment that can access the Internet, audiences can now watch films almost everywhere at anytime. This “dematerialization” process has eroded the established patterns of film watching, which was based on physical space or time restrictions. The “dematerialization” process has drastically transformed the landscape of the film exhibition industry. For instance, the film manufacturers, processors and duplicators are shrinking as the need for film stock is diminishing (Zhu, 2001). Even the Eastman Kodak Company, the biggest manufacturer of film stock, has been threatened by bankruptcy (Spector & Mattioli, 2011).

Some argue that the Internet provides more opportunities for selective consumption, that, because it is primarily interactive, the Internet allows the consumer to choose from a “buffet” of content, have full control over the movie when they watch it (such as replay, rewind, fast
forward, comment and share with other friends) and enjoy the freedom of time-shifting (view content at their own leisure). Furthermore, more than just consuming films, audiences nowadays can have deeper levels of involvement with films. The Internet provides the audience — its users — with the ability not only to watch a film, but also to alter it for their own purposes. The Internet is therefore creating a remix, sharing, clipping culture of film exhibition and consumption (Boyd, 2007). To some this is activation of films’ democratizing effect, as Benjamin depicts in his *The Work of Art in the Age of Mechanical Reproduction* (Cohen, 2010).

Others, however, hold that online viewing will has a bad impact on society. They argue that watching films in cinemas is a unique and valuable social experience that cannot be replicated by the Internet (Zhu, 2001). Whereas cinemas have been designed for open display of their content, the Internet’s conveyance is through the much more individualized experience of the computer. It is a way that differentiates the individual from what others are doing — it is antisocial in the sense of how it connects to the flows of life around it (Marshall, 2009, p. 84). This unsettled debate should remind us that the Internet’s impact on the film watching experience and people’s social lives is a really interesting topic that deserves more research.

To conclude, the existing research has systematically examined the Internet’s possible impacts on the film industry based on the technological advantages of the Internet. But this research has been mainly focused on a theoretical level, not on an empirical level. Whether the Internet’s revolutionary potential can be realized depends on many other political, economic
and social factors. As Raymond Williams (1974) has indicated, technologies are merely byproducts of wider social processes, technologies should never be seen in isolation but understood in relation to other processes and factors. And, as the situation in different societies are very different, when examining the Internet’s impact on China’s film industry, the specific circumstances of China’s political economy must be particularly stressed under a realistic perspective, as the political economy approach advocates.

The existing research on China’s political economy circumstances and its connections with the film and the Internet industries

China is a unique country on the global stage. As Colin Sparks pointed out, the Chinese case is not just different from capitalist countries, but also different from former communist countries such as Russia and Poland. Its media industry “demonstrates that one can have rapid marketization, including the floating of important parts of the media system on the stock market, without having any relaxation of authoritarian control” (Sparks, 2008, p. 17).

The economic system and the political system in China are developing in very different and often contradictory directions. At the economic level, China’s party-state has implemented progressive market reforms, which have in many ways turned China’s self-proclaimed socialist state into “an ideal capitalist state” with “freedom for capital and the state doing the dirty job of controlling the workers” and “everything subordinated to the ruthless drive to develop and become the new superpower” (Zizek, 2002, pp. 146-147). But on the political
level, reform is very conservative. As Zhao Yuezhi argues in her book *Communication in China: Political Economy, Power, and Conflict*, the Chinese party-state continues to “resist adopting Western-style constitutional democracy to ‘match’ an economic foundation that is already capitalistic, and to give up its communist ideological pretensions” (Zhao, 2008, p. 340), on the contrary, there are continuous re-articulations of socialist ideals at both the state and societal level (Zhao, 2008, p. 343). China’s political conservatism and economical liberalism are essentially incompatible with each other.

How are China’s political economy circumstances impacting on film and the Internet industries? There are already some researches on this topic. From these researches, several things can be learned to guide the analysis of the Internet’s impact on China’s film industry.

Firstly, market forces are not the main drivers for the development of either the Internet or the film industry in China. They are both manipulated by the one-party dictatorship of the Chinese government, which has different priorities in different eras. As Lin Chun argued, China’s post-Mao opening-up and reform process can be divided into three phases. The first phase, from 1978 to 1989, was a period of socialist self-adjustment with the objective of realizing rather than reversing the socialist cause. The second phase from 1989 to 2003 was a near - “revolutionary” transformation aimed at repealing the Chinese revolution and socialist alternative. But after 2003, reform was towards “a harmonious society” through the party-state’s policies of bettering the plight of peasants and migrant workers, improving environment protection and social equity, and increasing the public investment in the cultural
It should be noticed that the development of the Internet and film industry in China is according to the country's overall development. For example, the reform of China's film industry during the 1980s was just some slight modifications, mainly focused on the distribution-exhibition sector, it was not until 1993, with the general trend of in-depth state-run enterprise reform, ownership reform and marketization, that more fundamental reform of the film industry was initiated (Zhu, 2003). Then after 2003, with the state's ambition to improve the rural cultural infrastructure and strengthen social control in rural areas, the "rural digital film project" (农村数字电影工程) was launched. The Chinese government allotted a set of film screening devices for every 23 villages; paid for 12 movies a year for each administrative village with financial subsidies of 100-200 yuan for each movie, thus establishing a film market in the rural areas which is heavily reliant on the official subsidies (Tong, 2010, p. 9). This should remind us that the Chinese government's role must be included when examining the Internet's impact on China's film industry.

Secondly, in the Chinese party-state's intervention in the Internet and film industries it has always kept two goals in mind: making the industry competitive in globalized markets while also maintaining the state's grip on ideology (Zhu, 2003, p. 17). On the one hand, the Chinese party-state enthusiastically hopes to develop the Internet, film and other cultural industries, because it is trying to erect the cultural industry as a new engine for the development of the national economy and for adjusting the economic structure from an economy dependent on
investment and exports to an economy dependent on domestic consumption. The 12th Five-Year Plan (2011-15) of the Chinese Communist Party (CCP) has made it clear that the cultural industry should account for at least 5 percent of the total GDP by 2015, whereas it currently accounts for less than 2.5 percent (Li, 2011). Therefore, the Chinese state has carried out many measures to promote the marketization of cultural industries. For example, more and more policies have been issued and implemented by Chinese government to improve the copyright protection of films and other cultural products in recent years, and the Chinese government has poured resources into developing the Internet economy as a means of spring-boarding it, so it has a stronger and more independent role within the transnational political economy (Schiller, 2008, p. 113).

But on the other hand, the censorship apparatus imposed on film, the Internet and other media industries in China is among the most stringent in the world. All the films produced or shown in China are required to go through a strict censorship procedure. Chinese filmmakers need to submit script outlines before filmmaking and submit rough cuts after film production to State Film Administrative Bureau for approval. Filmmakers have to obey the official’s modification requirements, or they will not obtain permission to release their films. Online technology known as “the Great Firewall” blocks websites via an array of sensitive key words decided on by the government, while tens of thousands of official monitors continuously sweep blogs, chat forums, and even emails to ensure nothing challenges the country’s self-styled “harmonious society” (James, 2009).
Consequently, the Chinese party-state’s economic goals and ideological goals frequently contradict each other, and thus limit the pace of development of the film, Internet, and other media industries. Actually, the party-state’s rigorous censorship apparatus is one of the main impediments to China’s film industry evolving into a competitive participant in the world film market. The most terrible part of Chinese film censorship is that it has no clear criteria. Except for some general guidelines, such as no direct criticism of the party or state is permissible, the state refuses to spell out in any detail what is acceptable and unacceptable in terms of subject matter (Pickowicz, 2006, p. 6). This means Chinese filmmakers are forced into a “self censorship” predicament that stifles their creative inspiration and drives them to safe topics, consequently diminishing the cultural relevance and advantage of local films, and making it difficult for filmmakers to adapt to the increasingly competitive commercial environment (Gao, 2009). But there is little evidence to suggest that the Chinese government will loosen its censorship controls or establish clear censorship criteria in the foreseeable future.

Furthermore, the contradiction is also embodied in the Chinese party-state’s attitude towards foreign investment in China’s media industries. For example, in the cooperation between China’s film industry and Hollywood, the Chinese government hopes to make use of Hollywood for the development of China’s film industry by attracting investment to upgrade China’s film industrial structure and exhibition infrastructure, by learning from Hollywood’s advanced filmmaking techniques to improve Chinese films’ production values, and by
promoting Chinese films through Hollywood’s global exhibition networks. But at the same time, the Chinese government is afraid of Hollywood films’ potential for “cultural imperialism”, many high-level officials contend that the American way of life and American hegemony embodied in Hollywood films are harmful to China’s national and traditional culture, therefore they think it is necessary the state take protectionist measures to avoid the domination of Hollywood films in China. This contention has led to the screening quotas for Hollywood films and the upper limit for Hollywood’s investment in China (Su, 2009). Moreover, within the Chinese party-state’s attitude towards the Internet industry, we can also find this kind of contradiction. On the one hand, China’s film regulators are pleased to see the development of the Internet industry, since it is in accordance with the State’s ambition to develop the country’s cultural industries. But, on the other hand, the regulators are worried by the Internet, because it challenges their ideological control.

When the contradictions between economic goals and ideological goals reach a point where they need to resolved, the economic goals are sacrificed for the ideological goals. For example, in recent years, various government efforts to reassert more domestic control on the media were initiated in China, and the further marketization and privatization of the party-state media sector were slowed, because the Chinese government felt its control on ideology was increasingly challenged by the foreign capital and private capital invested in the country’s media industries. In March 2010, after enduring censorship and selective blocking from the Chinese government for a long time, Google, one of the largest Internet companies
in the world, eventually decided to close its office in Beijing (Waters & Hille, 2011).

Although the Chinese government understood that shutting down Google was harmful to China’s image and its appeal to foreign investment, it didn’t make any concessions on the censorship issue, because it feared uncontrolled information circulated through Google would harm the domestic hegemony of the party-government.

Another thing that can be learned from the existing researches is the party-state’s intervention in China’s media industries is not static. The changes in policy are generated not just by the contradictions between the Chinese party-state’s economic goals and ideological goals, but also by the internal conflict within the party-state departments and the external pressure from foreign countries. For instance, in recent years, the state has changed ideological control strategies toward independent films, especially so-called underground films. As films made or distributed without the government’s approval, underground films were banned by the government and were forced to survive through the International film festivals and foreign markets. The interesting thing is that after some of these underground films received awards and acclaims at international film festivals, the filmmakers could use their success to negotiate with the state’s censorship system for their later works. Nowadays, the Chinese state is not inclined to enforce the ban toward underground filmmakers and films in a rigorous way, unless they directly criticize the party or state. As Pickowicz has explained, this is because the cultural liberals in the CCP see underground filmmaking as a useful pressure release mechanism, and allowing underground film production in China, along with turning a blind
eye to the overseas screening of these films, can make China look good (Pickowicz, 2006, pp. 7-8). Furthermore, the Chinese party-state can improve its image even more by offering aboveground opportunities to the underground filmmakers. For example, in November 2003, the State Film Administrative Bureau invited a number of underground filmmakers to an internal seminar, and then changed its policy towards underground films from prohibition to guidance and administration (Zhou, 2007, p. 186). From the above discussions and examples, we can see that the state’s censorship in China is not a static system but increasingly “more a matter of negotiation than negation” (Zhu, 2008, p. 36). This kind of “negotiation” is also happening within the other interventions imposed by the Chinese party-state on the media industries. For instance, although the Chinese government intends to shield the domestic film industry from Hollywood’s invasion, it has to progressively open up the market under the stick-and-carrot diplomacy tactics of the U.S. government. The Chinese media industry is not an isolated island in the world, it is developing to compete in the global market with the Chinese government’s ambition of enhancing China’s soft power in the world, but it is faced with the rigorous challenges from foreign competitors. Therefore, when conducting political economy research into China’s media industries, the specific political economy circumstances in China should not just be considered from a domestic perspective, they should also be deemed as an integral part of the global communication system (Zhao, 2003, p. 61).

The structure of this thesis

To conduct research on the Internet’s impact on the film exhibition sector in China is
dangerous, because the Internet has not yet reached technical, social and economic maturity, and the landscape of Chinese film industry is also very fast changing. Therefore, there are many imponderable factors that make such research difficult. The research conclusions therefore will probably be tentative. Another danger is that this kind of “impact” research risks being just a “descriptive” project, which is only a summarization of “what is happening”, without any theoretical or practicable outcomes.

To diminish these two dangers in this research, I decided to investigate several specific phenomena that are representative of the increasing connections and contradictions between China’s Internet and film exhibition industry, rather than simply describe the Internet’s possible impact on China’s film industry in a general sense.

Besides this introduction, the thesis is divided into four chapters. Chapter 2 analyzes the four structural characteristics of China’s film exhibition market, and also explores the political economy factors behind these characteristics. These factors and characteristics are unavoidable when considering the Internet’s impact on China’s film exhibition.

Chapter 3 traces the history of two competing exhibition networks related to China’s film market. One is the online video websites, which accumulated their primitive capital with piracy content, but then progressively legalized under the forces of venture capital and government administration. Another is the online piracy network, which has become a global problem for film industry through its transnational, decentralized and limitless network. However, this network is also sometimes used as a democratic tool to combat the controls of
the party-state.

Chapter 4 analyzes the two competing online exhibition networks' impact on the exhibition of three different kinds of films in China. The first kind is Chinese commercial films, which are making more and more profits from online video websites, while also facing the challenge of online piracy. The second is foreign films, which are expanding their influence in China through the online video websites and piracy networks that use volunteers to provide Chinese subtitles. The third is the so-called Chinese independent films, whose domestic circulation was once quite confined due to the state's control of distribution channels. However, nowadays, Internet exhibition is providing a resistance strategy with which Chinese independent film can combat the state's unreasonable censorship system.

The last chapter concludes this paper by proposing a new theoretical framework to explain the impact of the Internet on film exhibition in China. This framework understands the competing relationship between commercial online video websites and online piracy networks as a consequence of conflicts between the logic of the market and the logic of collective sharing.

**Methodology**

As the political economists Eileen Meehan, Vincent Mosco and Janet Wasko (1993) have indicated, "Unlike positivist paradigms, political economy tends to treat its methods and criteria implicitly; practitioners are expected to follow criteria implicit in the paradigm and then to select the method best suited to the problem" (p. 354). Therefore, political economists usually synthesize the research methods from other disciplines. This is also the case for this
thesis, where multiple methodological procedures have been used to examine the Internet’s impact on China’s film industry.

In this methodology part of the paper, the combination of methods used to answer the questions raised earlier is presented. The data collecting and analyzing parts are particularly highlighted, because whatever the method, the process of finding and analyzing industry data should be the central part of conducting political economy research on the media.

In this research project, there were three main phases. The first phase was a primary inquiry of the research objects by participatory observation and literature review. This was done before the thesis prospectus was constructed. As a Chinese Internet user and film researcher for more than nine years, I have witnessed for myself the growing connection between the Internet and the film industry in China. The Internet has changed how I access films, for instance. Since I can find most of the films I want on the Internet I don’t collect DVDs anymore, and my visits to the cinema have also decreased. Furthermore, nowadays I get information on films mainly via the Internet; I post my film reviews online and interact with other film fans through social networking sites. These experiences have provided me with firsthand knowledge of the phenomenon I am writing about. But of course, personal experience and impressions have subjective bias and limitations, thus in the research preparation phase, I also conducted an extensive review of the existing research literature relevant to my topic. These literature helped me to understand the Internet’s potential impact on film exhibition in China from a theoretical perspective and guided me to my research
questions and determined what kinds of data I needed to answer these questions.

The second phase focused on collecting data around the research questions. Sufficient and reliable industry data is the foundation for conducting a good political economy study of the media industry, but the necessary data are not always attainable. For example, personal interviews with industry practitioners are deemed one of the most authentic and reliable data sources, but many film industry practitioners are unwilling to do non-promotional interviews, especially about issues related to their commercial interests. Another example is the consulting institutions, which have lots of industry data but who charge to see it. Furthermore, it seems all sources are providing data "strained through a point of view, vested interest, or argumentative stance" (Meehan, Mosco & Wasko, 1993, p. 356). Different data sources may have very different orientations and thus distort the data they provide. For example, trade publications tend to focus on celebratory coverage of the industry's triumphs, while the political agendas implied in government documents tend to direct the choice and results of the evidence presented. Thus, political economists must utilize multiple data sources and systematically evaluate the data from different sources in a comparative way to enhance the validity and reliability of the research. As Erlandson et al. have argued, "The best way to elicit the various and divergent constructions of reality that exist within the context of a study is collecting information about different events and relationships from different points of view" (Erlandson et al., 1993, p. 31). Thus for this research, I collected data on China's Internet and film industry from the following sources:
Government documents: In China, government documents should be one of the main data sources for research on the media industry, because, only government and government-supported institutions have the power and resources to survey the media industry nationwide. Although the government documents always have political agendas, they can still provide us with useful information about the overall situation of the media industry. Thus in this research, government documents, such as *The Statistical Report on China's Internet Development*, which is regularly released by the China Internet Network Information Center (CNNIC), and *The Research Report on the Chinese Film Industry*, released each year by the Industry Research Center of China Film Association, have been utilized.

Trade Journals: Chinese Internet and film industry trade journals, such as *China Internet Weekly*, *China Film*, and *China Film Market*, were also used as data sources in this research, because they provide extremely useful documentation of the latest industry developments, although this information is presented in a fragmentary way and needs to be weaved through an extensive archival research process.

Consultancy companies: Several Chinese consultancy companies, such as the Beijing-based Iresearch and Entgroup and Shanghai based Artisan Gateway, that focus on the Internet, film and other media industries, have been established in recent years. These consultancies frequently publish research reports on the Internet and film industries. These reports are informative, but to view them requires paying hefty fees. To obtain data from these companies, I took a part-time job at Entgroup, this gave me access to the reports that are used in this
In-depth interview: Nowadays, the development of online social networks, such as microblogs, is providing a new channel for researchers to connect directly with industry practitioners and thus in-depth interviews can be used as a firsthand data source. In this research, some in-depth interviews were conducted with insiders in the Chinese Internet and film industries, such as the managers of the online video websites and the executives of film exhibition and marketing companies. These interviews aim to explore information that is not disclosed by other sources but is necessary to answer the research questions.

In this paper, the above four data sources are used in a comparative and complementary way, and the quality of the data is evaluated against Scott's (1990) four criteria, namely, authenticity, credibility, representativeness, and meaning.

In the third phase, the collected data was analyzed around the research questions. As John Hartley has pointed out, “the industry itself does not describe a necessary empirical fact on the ground, they are abstract aggregations of agents, prices, commodities, firms, transactions, markets, organizations, technologies, and institutions” (Hartley, 2009, p. 232). Therefore, when using industry data to answer research questions, the data must be analyzed in a systematic way. In this research, the analyzing of data comprised three parts: The first part was analytic induction, which means inferring meanings from the data collected. To conduct analytic induction of the data in a more systematic way, this research borrows some analytic models from previous research, such as the industrial organization model which has been used
by Douglas Gomery and other media economists to assess the media industry. Then, after tentative findings were induced, theoretical interpretations were conducted to consider these findings within China’s particular political economy circumstances and thus answer the research questions. The theories used in this research come from different disciplines, including media economy, political research, and communication studies on the Internet and film. And, in some situations, case study was also used as a supplementary method.
To conclude, this research uses multiple methodological procedures to examine the Internet's impact on the film exhibition industry in China. To enhance the validity and reliability of this
research, the data from various sources and the theories from different disciplines have been used in a comparative and complementary way to answer the research questions that have come from long-time participatory observation and extensive literature review.
Chapter 2: The Structure of China’s Film Exhibition Market

To understand the Internet’s impact on film exhibition in China, it is necessary to first know the structure of China’s film exhibition market, especially the structure that existed before the Internet emerged as an important exhibition channel. Therefore, this chapter analyzes the four characteristics of China’s film exhibition market, and explores the political economy factors behind these characteristics.

A market mainly depending on theatrical exhibition

Film is a cultural product with specific economic features. The production costs for a film are so high that a film has to attract the biggest audience possible in order to make a profit. Fortunately, film is a product similar to public goods with joint consumption attributes. It is non-rivalrous, which means viewing by one audience does not use up the product or detract from the enjoyment of other viewers (Vogel, 2011, p. 94). The cost of making the prototype (the film negative or original digital recording) is high, but the marginal cost of offering additional viewings or copies is low and flat, which means the bigger the audience the film attracts, the higher the profits. Therefore, to maximize revenues, film distributors make great efforts to develop new exhibition platforms and outlets to attract more viewers.

Theatre was historically the only exhibition outlet for films. But with the development of technology and the film market, more and more exhibition channels have emerged, such as television since the 1950s, cable television and video since the 1980s, DVDs since the
mid-1990s, and online streaming and downloading in the 2000s. These outlets for film exhibition, which are generally defined as ancillary markets, have played an increasingly important role in transforming the film industry’s economic structure, especially since the 1980s.

In Hollywood, which is the world’s biggest film industry, theatrical screenings still accounted for more than half of all exhibition revenues as recently as 1980, but since then, with the development of new exhibition channels, the revenues from ancillary markets have quickly overshadowed the revenues derived from a film’s theatrical release. As table 2.1 shows, in 2007, theatrical exhibition only accounted for about a fifth of all revenues (Vogel, 2011). In recent years, with new exhibition platforms, such as Blu-ray discs, online streaming and downloading, continuously emerging, the proportion of revenues resulting from theatrical exhibition have further decreased. But the expansion of ancillary markets has in turn provided the Hollywood studios with more revenues with which to finance increasingly expensive projects, which aim at conquering the worldwide markets with spectacular special effects and top stars.

However, there are also conflicts of interest among different ancillary markets since they are selling the same content. For instance, it is widely deemed that the development of Blu-ray and the online availability of films have led to falling DVD revenues in recent years. According to data from the industry trade organization Digital Entertainment Group, U.S. consumer spending on buying and renting Blu-ray discs rose 53 percent in 2010 to US$2.3
billion, and consumer spending on video-on-demand and digital downloads increased 19 percent to US$2.5 billion in 2010. In contrast, spending on DVDs in 2010 was US$4.47 billion, down from US$7.97 billion in 2009 and a high of US$10.13 billion in 2007, and the average number of units sold per title dropped by more than half, to 545,000, from 1.14 million in 2009 (Fritz, 2011).

To decrease the conflicts among ancillary markets and get the maximum profits they can from their films, distributors in Hollywood have developed a corollary strategy of market-segmentation by price⁴ (Vogel, 2011, p. 126). With this strategy, films are made available to consumers through different channels at different prices over time through a series of well-defined and exclusive space-times (Scott, 2005). In general, Hollywood films are always first released to the market that generates the highest marginal revenue — theatrical exhibition — and then sequentially released in the windows that contribute less marginal revenue, including pay-per-view on premium television, DVD and Blu-ray, online streaming, pay-television, and then network television and syndicated television. Viewers who want to watch the latest film in the theatre pay a high price. Viewers who not want to pay to watch the film can wait to view it when it is broadcast on network television, although they generally have to wait a long time and have to watch advertisements along with the film.

⁴ Also known as a “release windows” strategy.
Table 2.1 Worldwide revenue receipts for Hollywood major studios, in US$ billions (2007 dollars), 1948-2007

<table>
<thead>
<tr>
<th>Year</th>
<th>Theatre</th>
<th>Video/DVD</th>
<th>TV</th>
<th>Total</th>
<th>Theatre share (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1948</td>
<td>8.5</td>
<td>0</td>
<td>0</td>
<td>8.5</td>
<td>100.0</td>
</tr>
<tr>
<td>1980</td>
<td>4.9</td>
<td>2.2</td>
<td>4.1</td>
<td>9.2</td>
<td>53.3</td>
</tr>
<tr>
<td>1985</td>
<td>3.3</td>
<td>2.6</td>
<td>7.4</td>
<td>13.3</td>
<td>24.8</td>
</tr>
<tr>
<td>1990</td>
<td>6.8</td>
<td>6.5</td>
<td>10.1</td>
<td>22.4</td>
<td>30.4</td>
</tr>
<tr>
<td>1995</td>
<td>6.2</td>
<td>11.9</td>
<td>11.6</td>
<td>29.7</td>
<td>20.9</td>
</tr>
<tr>
<td>2000</td>
<td>6.5</td>
<td>13.1</td>
<td>15.5</td>
<td>35.1</td>
<td>18.5</td>
</tr>
<tr>
<td>2005</td>
<td>7.0</td>
<td>22.6</td>
<td>16.9</td>
<td>46.5</td>
<td>15.1</td>
</tr>
<tr>
<td>2007</td>
<td>8.8</td>
<td>17.9</td>
<td>16.2</td>
<td>42.9</td>
<td>20.5</td>
</tr>
</tbody>
</table>


The release windows system has been the cornerstone of Hollywood’s strategy for a long time. However, in China, the revenues of the film industry still largely come from theatrical exhibition. As shown in table 2.2, the theatrical box office accounted for more than 80 percent of the revenues of Chinese film market from 2005 to 2012, while the revenues from other exhibition channels accounted for less than 20 percent. As table 2.3 shows, the number of theatres and screens in China has increased remarkably in recent years, which has made China the second box office market in the world, just behind the U.S.
Table 2.2 Domestic Revenues for the Chinese Film Market, 2007-2012

<table>
<thead>
<tr>
<th>Revenue (millions yuan)</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
<th>2012</th>
</tr>
</thead>
<tbody>
<tr>
<td>Theatre Box Office</td>
<td>3327</td>
<td>4341</td>
<td>6206</td>
<td>10172</td>
<td>13115</td>
<td>17073</td>
</tr>
<tr>
<td>Revenue from other exhibition channels (estimated)</td>
<td>650</td>
<td>790</td>
<td>1070</td>
<td>1640</td>
<td>2640</td>
<td>2900</td>
</tr>
<tr>
<td>Revenue from TV channels</td>
<td>370</td>
<td>390</td>
<td>440</td>
<td>510</td>
<td>620</td>
<td>690</td>
</tr>
<tr>
<td>Revenue from DVDs/Blu-rays</td>
<td>50</td>
<td>30</td>
<td>20</td>
<td>20</td>
<td>20</td>
<td>10</td>
</tr>
<tr>
<td>Revenue from online exhibition</td>
<td>10</td>
<td>40</td>
<td>90</td>
<td>150</td>
<td>320</td>
<td>500</td>
</tr>
<tr>
<td>Theatre Share</td>
<td>83.7%</td>
<td>84.6%</td>
<td>85.3%</td>
<td>86.1%</td>
<td>83.2%</td>
<td>85.5%</td>
</tr>
</tbody>
</table>

Source: China Film Industry Report 2012-2013 from Entgroup

Table 2.3 The number of theatres and screens in China

<table>
<thead>
<tr>
<th>Year</th>
<th>2005</th>
<th>2006</th>
<th>2007</th>
<th>2008</th>
<th>2009</th>
<th>2010</th>
<th>2011</th>
<th>2012</th>
</tr>
</thead>
<tbody>
<tr>
<td>Theatre Number</td>
<td>1243</td>
<td>1325</td>
<td>1427</td>
<td>1545</td>
<td>1687</td>
<td>2000</td>
<td>2800</td>
<td>3680</td>
</tr>
<tr>
<td>% change vs. previous year</td>
<td>7%</td>
<td>8%</td>
<td>8%</td>
<td>9%</td>
<td>19%</td>
<td>40%</td>
<td>31%</td>
<td></td>
</tr>
</tbody>
</table>
After the box office, the most important revenue source for Chinese films is the advertisement revenue from television channels. The most important of these is the Film Channel of China Central Television (CCTV6), which is aired all over the country. There are another six provincial film channels that belong to the six state-owned film conglomerates, namely East Movie Channel under the Shanghai Film Group, Western Movie Channel under the Western Film Group in Shanxi province, Jilin Film Channel under the Changchun Film Group in Jilin province, Emei Film Channel under the Emei Film Group in Sichuan province, Zhujiang Film Channel under the Zhujiang Film Group in Guangdong province and Xiaoxiang Film Channel under the Xiaoxiang Film Group in Hunan province. These are local channels whose influence and revenue sources are quite limited compared to the Film Channel of China Central Television.

In general, the seven film channels are mainly supported by the revenues they receive from advertisers. According to the *Research Report of the Chinese Film Industry 2011*, the total advertisement revenue for all seven film channels were 2.03 billion yuan in 2010 (The Industry Research Center of the China Film Association, 2011). Part of the revenues was used to buy the broadcasting rights for films. Under the arrangement of the SARFT, CCTV6 buys
the television broadcasting rights of around 90 percent of the domestic films produced every year. However, the price paid by CCTV6 is quite low based on its monopoly position. It only pays an average price of 700,000 yuan per film for a long period of 50 years with an additional fee of 80,000 yuan for each rerun (Interview with Tang Ke, the Deputy Director of the Program Center of CCTV6, 2013). Compared to the ever-increasing production cost, the price paid by CCTV6 is minimal. In 2012, the seven film channels’ expenditure on film broadcasting rights was estimated to be 690 million yuan (Entgroup, 2013), which was not very much when compared with the revenues for Hollywood films from television broadcasting.

In the film DVD exhibition field, the gap between the Chinese and Hollywood film industries is even wider. Among all the exhibition channels, DVDs have produced the most revenue for Hollywood films, whereas in China, the revenue produced by DVDs for film companies is trivial. According to the 2013 report from General Administration of Press and Publication, in 2012, although there were 611 new DVD film titles published in China, the total distribution number was just 7.27 million and the distribution revenue were only 27 million yuan. The revenue that the film production companies can get from DVD exhibition was trivial. It was estimated that the total DVD copyright revenue for Chinese films were only 10 million yuan in 2012 (Entgroup, 2013). Chan Ho Sun (陈可辛), a distinguished director and producer, said in an interview that a Chinese blockbuster with a 200 million yuan box office record can only generate 3 million yuan from sales of home video products (Yeh, 2009).
And the domestic DVD rights price for a Chinese blockbuster is just 700 thousand yuan, or less (Xu, 2011).

Besides the above exhibition channels, there is another exhibition channel in the Chinese film market: screenings in rural areas. These screening activities are generally maintained through government subsidies. Since 1998, the Chinese government has initiated a rural film “2131 Project” that aims to “realize projecting one movie per month in a village in the beginning of 21st century”. In 2005, with the development of digital film technology and equipment, the Chinese government further launched the “Rural Digital Film Project”, in which the government has allocated to villages, in groups of 23, film screening equipment and paid each administrative village for 12 movies a year with financial subsidies of 100-200 yuan for each movie. From 2006 to 2010, China’s central and local government had invested more than 5 billion yuan in the rural film market (Tong, 2010, p. 9).

There are mainly two film exhibition models in the rural areas of China. One is screening for public welfare. In this model, for every screening a film’s copyright holders receive 10 yuan. Another model is commercial screenings. In this model, a film’s copyright holders can set the price for a screening up to 50 yuan under the policy of the SARFT. Moreover, the trade between film exhibitors and film copyright holders is operated solely through the Digital Film Ordering Platform established by China Film Group. The platform gets 3 yuan from every screening as an operating fee. It is reasonable to argue that the market value of films in Chinese rural market has not been sufficiently explored under such a planned economy.
system. According to the data from SARFT, in 2010, there were 8,473,319 film screenings purchased through the Digital Film Ordering Platform, among them, 7,010,208 were for public welfare, and 1,463,111 were commercial screenings. But for Chinese film production companies, the total revenue from the rural market did not surpass 100 million yuan in 2010 (Administration Center of Digital Film Content, SARFT, 2011a). Even *Let the Bullets Fly*, the Chinese film with the highest box office until 2011, which made 659 million yuan from the urban market, took just 1,113,328 yuan from 157,544 screenings in the rural areas in the first half of 2011 (Administration Center of Digital Film Content, SARFT, 2011b).

To summarize, although there are multiple exhibition channels in the Chinese film market, all the channels, except theatrical exhibition, are underdeveloped. Unlike Hollywood, theatrical release is still the most vital revenue source for Chinese film companies and determines whether a movie is commercially successful or not. To some extent, this film exhibition structure is too reliant on theatrical exhibition to sustain a robust film industry. Therefore, exploring exhibition channels other than theatres has been deemed an urgent task for the development of the Chinese film industry.

**A market with strict entry barriers imposed by the government**

The second characteristic of the Chinese film exhibition market is that it is a market with strict entry barriers imposed by government (Yeh & Davis, 2008, p. 37). Although the Chinese government has initiated market reforms of the Chinese film industry since the 1980s, the reforms have not been thorough. Due to the legacy of the planned economy and
ideological concerns, the Chinese government still maintains many entry barriers or forbidden areas for investment by foreign and private capital in the Chinese film industry.

With regard theatrical exhibition, only the state-owned studios have the right to distribute films, foreign companies are strictly excluded from this field. And for a long time, private distribution companies could exist only by providing services for the state-owned studios. It was not until 2003 that private companies such as Bona Films and Huayi Brothers Films eventually got the right to directly distribute films in China according to the *Interim Provisions on the Access of Operational Qualifications for Movie Production, Exhibition and Projection* (SARFT, 2003). However the private film distribution companies are still not allowed to distribute imported films. According to government policy, only the China Film Group has the right to import foreign films, and only the two state-owned and interlocked companies China Film Group and Huaxia Film Company have the right to distribute foreign films in Chinese theatres. Besides, the foreign films shown on Chinese screens are subject to government censorship and a quota system. Before 2011, only 20 movies could be imported every year, through box office split deals\(^5\), most of which were Hollywood blockbusters. And no more than 50 foreign movies a year were imported through buying the rights outright. For instance, in 2010, China imported 62 foreign films for theatrical release, 42 of them were flat-rate deals and 20 were revenue sharing.

To win a place in the limited revenue-sharing quota for film imports, foreign film companies

\(^5\) This situation was changed in February, 2012. The Chinese government now allows 34 foreign films to be imported annually through box office split deals, but the additional 14 films must be 3D or Imax films.
have to maintain a good relationship with the administrative department, SARFT, and the
exclusive importer, China Film Group, by carrying out public relations activities and even the
bribery of officials and managers. In April 2012, the US Securities and Exchange
Commission began an investigation into whether some of Hollywood’s biggest movie studios
had made illegal payments to officials in China to gain the right to film and show movies in
China (Wyatt, 2012).

A quota system is also imposed on the screen time for foreign films in China. According to
the Regulations on Administration of Film issued by SARFT in 2001, the annual screen time
for foreign movies in theatres cannot exceed one-third of the total screen time. To maintain its
control over theatres, the Chinese government requires that the share of foreign investment in
Chinese theatres does not exceed 49 percent. This share was once enhanced to 75 percent in
seven big cities in 2003 according to the Interim Provisions for Foreign Investment on
Chinese Cinema (SARFT, 2003), but this was soon cancelled. The policy’s revision is widely
seen as stemming from an incident in 2005 when a theatre held by a foreign company refused
SARFT’s request to screen a propaganda film released to commemorate the 60th anniversary
of the end of World War II. Thereafter, the government required that all theatres be held by
Chinese companies. In 2006, Warner Brothers International Cinemas (WBIC), which was the
first foreign investor in Chinese theatres, decided to withdraw its shares in six Chinese
cinemas because of the change in policy (Nakashima, 2012).

This case vividly reflects the internal conflict within the reform of the Chinese film industry.
On one hand, the Chinese government wants to attract foreign investment to help upgrade the country’s cinemas and help transform the domestic film industry, but on the other hand, the Chinese government wants to retain its ideological control of the film industry. These two ambitions frequently collide with one another, resulting in the government’s repeated policy changes towards foreign investments.

Although the Chinese government hopes to construct an internationally competitive film industry, maintaining its ideological control of film culture is still its first concern. Film continues to be regarded as an important ideological tool by the government. In the socialist era of China, some film critiques even initiated large-scale political movements. Therefore, although the government has been struggling to promote the marketization of the Chinese film industry since the 1980s, a stringent censorship apparatus is still in place (Zhu, 2003, p. 521). All the films produced or shown in China are required to go through a strict censorship procedure. Chinese filmmakers need to submit script outlines before they begin filming and they must submit a rough cut of the film to state film bureaucrats for approval and make any changes they require; otherwise their films will not get approval for release.

The Chinese film censorship system is notorious because it has no clear criteria. Except some general principles such as no direct criticism of the party or state is allowed. The party-state refuses to spell out in any detail what is acceptable and unacceptable in terms of subject matter (Pickowicz, 2006, p. 6). The film censoring committee is composed of approximately 20 or so members, whose backgrounds are very diverse, spanning movie professionals.
delegates from the Women's Federation, the Communist Youth League, Religious Committee and various governmental administration departments (Branigan, 2011). Besides obeying the broad principles, these committee members are censoring films from the perspectives of the departments and organizations they come from, so any negative depictions of their departments will probably need to be cut or revised. Therefore, the films that are distributed in China are the safest films. This is not just the case for films distributed in theatres, but also for films distributed through television or DVDs.

The television exhibition of films in China is also subject to strict administration. No private company or foreign corporation is allowed to establish a film broadcast channel or cable channel in China. A film needs to get the *Permit for Film Projection* (电影公映许可证) before it can be aired on television. More importantly, according to the *Management Regulation on the Importation and Broadcasting of Imported TV Shows* (境外电视节目引进、播出管理规定) executed in 2004, imported films are not allowed to be broadcast during primetime (19:00-22:00), and imported films can not constitute more than 25 percent of the total daily broadcasting time for each film channel.

Different from theatrical exhibition and television exhibition, which are administrated by SARFT, the DVD exhibition of films is administrated by other departments. Before 2009, the General Administration of Press and Publication was responsible for the production, publication and duplication of film and audio-video products, while the Ministry of Culture was responsible for the wholesale, retail, renting, showing and importing of film audio-video
products" in China. Then in 2009, the General Administration of Press and Publication took over all of the administrative responsibilities for audio-video products previously supervised by the Ministry of Culture.

For a long time, audio-video products in China were required to be published by a state-owned publishing house to assure the content of these products accorded with the party-state's requirements. State-owned publishing houses are institutional organizations supported by the state fund, they have little incentive to explore the film DVD market, which is high risk because of piracy. Therefore, the film DVD products in China are mainly developed by private companies, who acquire the DVD copyright from the film production company then design and produce film DVDs, but since they do not have the right to publish audio-video products, they have to purchase a license, also known as code number, from a state-owned publishing house in order to publish. This procedure considerably increases the burden on the private film DVD companies and limits the profitability of the film DVD market in China.

However, unlike the theatrical exhibition and television exhibition of foreign films in China, which are subject to a quota system, the foreign film DVD exhibition in China is not restricted to a quota. To exemplify, between 1997 and 2000, the Ministry of Culture issued more than 800 licenses allowing foreign audio-video products to be imported into China, which is much more than the licenses granted to imported films to be exhibited on theatrical screens and television (Wang Shujen, 2003, p. 63). But this does not mean that
foreign films are freely distributed in the Chinese DVD market. The administrative department maintains a strict censorship procedure for all imported titles. Indeed, it can often take more than one year for a title to pass through the censorship process, at which point the DVD has already been widely circulated in the piracy market (UNESCO, 2007). Therefore, the revenue from the Chinese market is quite limited for foreign film DVDs.

In summary, the film exhibition market in China is imposed administration by the party-state in three ways. Firstly, the state-owned companies or institutions are given a favorable status in the distributing of films, while private companies and foreign corporations are subject to various entry barriers. Secondly, all films publicly distributed in China are subject to stringent censorship. Thirdly, the Chinese government tries to limit the influence of foreign films in China by applying a quota system and a long censorship procedure.

A market mainly controlled by state-owned institutions

The exhibition of films mainly involves three parties: distributors, exhibitors and audiences. The distributors deliver films to the exhibitors, which then show the films to the audience. In the planned economy era Chinese film distributors and exhibitors were solely state-owned. After the reform and opening-up of the Chinese film industry initiated in the early 1990s, the private film companies in China were allowed to engage in production, exhibition and distribution.

However, China's film distribution and exhibition markets are still controlled by state-owned
corporations because of the privileges they enjoy (Yeh & Davis, 2008, p. 42). According to the China Film Industry Report 2012-2013 from Entgroup, China Film Group (中影集团) and Huaxia Film Distribution Corporation (华夏电影发行公司) accounted for 61.75 percent of China’s film distribution market in 2012 (As shown in Table 2.4). Their oligopoly position is mainly because they have the exclusive right to distribute foreign films in China (Yeh & Davis, 2008, p. 42).

This gives the two corporations a big advantage, since the distributing of foreign films is the most lucrative part of China’s film market. In China, film box office revenues are divided among production, distribution and exhibition parties on a proportional basis after deducting 5 percent for the Film Development Fund (电影专项发展基金) and 3.3 percent in business tax. However, the profit-sharing systems are very different for domestic and foreign films. When distributing domestic films, the production companies generally get 28-35 percent, the distributors get 10-15 percent and the exhibitors 55-57 percent from the remaining box office. When distributing foreign films, on the other hand, the exhibition party can still get 55-57 percent from the deducted box office, but the share of the box office for foreign copyright holders and domestic distributors are different to those for domestic films. For revenue-sharing imported blockbusters, the foreign copyright holder can get 13 percent of the remaining box office if the total box office of the film does not exceed 40 million yuan. If the box office surpasses 40 million yuan, for each additional 10 million yuan, the foreign copyright holder can get 0.5 percent more, but no more than 17.5 percent of the deducted box
Therefore, the domestic distributors of revenue-sharing imported blockbusters can get 25.5-32 percent of the box office, which is much higher than their share of the box office for domestic films. For foreign films imported through buyouts, the share of the box office domestic distributors receive is even higher, because the price of a film can be as low as tens of thousands of dollars. Moreover, the average box office performance of imported films is much better than that for domestic films, since the imported films are mainly Hollywood blockbusters or high quality films carefully selected from the output of foreign countries. Therefore, the privilege of distributing foreign films gives the state-owned China Film Group and Huaxia Film Distribution Corporation an incomparable advantage over other Chinese film distributors.

### Table 2.4 Chinese Film Distribution Companies’ Market Share in 2012

<table>
<thead>
<tr>
<th>Company Name</th>
<th>Market Share (%)</th>
</tr>
</thead>
<tbody>
<tr>
<td>China Film Group</td>
<td>38.24</td>
</tr>
<tr>
<td>Hua Xia Film Distribution Corporation</td>
<td>23.51</td>
</tr>
<tr>
<td>Huayi Brothers Media Group (华谊兄弟传媒有限公司)</td>
<td>10.22</td>
</tr>
<tr>
<td>Beijing Enlight Media Corporation (北京光线传媒有限公司)</td>
<td>7.37</td>
</tr>
<tr>
<td>Bona Film Group (博纳影业)</td>
<td>3.34</td>
</tr>
<tr>
<td>Guang Zhou Mei Ah Hua Tian Xia Film Distribution Corporation (广州美亚华天下电影发行公司)</td>
<td>2.21</td>
</tr>
</tbody>
</table>
Secondly, the exclusive right to distribute foreign films also helps the two state-owned corporations to distribute domestic films. In the analog era of theatre exhibition, the number of copies made of each film was limited since the cost of making a copy was high. Therefore, the theatres had to maintain a good relationship with China Film Group and Hua Xia Film Distribution Corporation by accomplishing the quota of screening domestic films and other requirements; otherwise they might not get a copy of the foreign blockbusters so important for their operations.

China Film Group and Hua Xia Film Distribution Corporation can also take advantage of the theatre chains controlled by them to achieve a privileged position in the film distribution and exhibition market. Until the end of 2011, there were 39 theatre chains in China. As table 2.5 shows, China Film Group was the sole shareholder or main shareholder in seven of them. These seven theatre chains generated 4.54 billion yuan at the box office in 2011, which accounted for about 35 percent of the China theatre exhibition market. For Hua Xia Film
Distribution Corporation, although it does not own any theatres, as a corporation consisting of the China Film Group, several state-owned studios, and eight theatre chains, it has a close relationship with many theatre chains. Therefore, it is difficult for a private film company to compete with these two state-owned corporations in the distribution and exhibition market. However, what should also be noticed is that the privileged position of the state-owned corporations in the distribution and exhibition market has diminished with the deepening of reform in Chinese film industry and the emergence of digital screening.

<table>
<thead>
<tr>
<th>The name of theatre chain</th>
<th>China Film Group’s Share</th>
</tr>
</thead>
<tbody>
<tr>
<td>Digital Theatre Chains under China Film Group (中影数字院线)</td>
<td>100%</td>
</tr>
<tr>
<td>China Film Stellar Theatre Chain (中影星美院线)</td>
<td>60%</td>
</tr>
<tr>
<td>China Film Sothern New Line (中影南方新干线)</td>
<td>56%</td>
</tr>
<tr>
<td>Jiangsu Oriental Theatre Chain (江苏东方院线)</td>
<td>51%</td>
</tr>
<tr>
<td>Liaoning Northern Theatre Chain (辽宁北方院线)</td>
<td>50%</td>
</tr>
<tr>
<td>Sichuan Pacific Ocean Theatre Chain (四川太平洋院线)</td>
<td>50%</td>
</tr>
<tr>
<td>Beijing New Film Association (北京新影联院线)</td>
<td>34%</td>
</tr>
</tbody>
</table>

Source: Personal Interview.
A market permeated with piracy

Besides the above-mentioned characteristics, copyright infringement or piracy is another important issue when discussing China’s film exhibition market.

Film piracy means the unauthorized copying and exhibition of a copyrighted film. Technological developments mean there are many ways of pirating a film, such as optical discs, peer-to-peer downloading, online streaming, etc. It is a worldwide problem that invades the interests of the film industry, and is more serious in China for complex historical, economic and political reasons. According to the Annual Report on the Development of the Chinese Culture Industry published in 2003, 92 percent of the audio-video market in China was pirated products (Ye, 2003). In 2006, a research report by the Motion Picture Association of America (MPAA) revealed that the Chinese film industry lost about US$1.5 billion in revenue to piracy last year, while the major U.S. studios lost US$565 million to piracy in 2005 (Landreth, 2006). With the development of the Internet, online piracy has gradually become the most prominent piracy form in China’s film market, even the pirated DVD industry has been hit, not to mention the damage it does to the legal film industry.

Why is film piracy so widespread in China? This is not a question that can be answered easily; it has to be examined in the context of China’s political economy.

From the economic perspective, as Choi (1999, p. 2) notes, there is a close correlation between per capita GDP and piracy levels, with the highest piracy rates to be found in those countries with the lowest incomes. Whereas consumers in “developed” countries are more
able, and more likely, to prefer "legitimate" goods, "pirated" products have greater appeal for those whose incomes make the "legitimate" goods prohibitive. Moreover, nowadays the price of both copying and exhibition equipment continue to fall due to technological developments, which reduces start-up costs and increases profit margins, thereby encouraging more people to enter the pirate film market.

From the historical perspective, as Montgomery has explained, "copyright" was really a concept that emerged in China with the reform process towards a capitalism economy. Formal copyright law did not become a significant factor in China's intellectual property environment until the 1990s. That was because the "copyright" concept was generated from capitalism, which is based on a system of private property (Hesmondhalgh, 2007). But in China's socialist era before opening-up, the idea that individuals or companies would own an exclusive right to a creative product was in many cases viewed as a notion that contradicted the "communist" goal of the state. Therefore, the films created by state studios were considered common property and the studios themselves saw little or no need to protect their products from unauthorized use. The concept of "piracy" simply did not exist (Montgomery, 2007). This situation is best exemplified by an often-cited maxim of the time: "Is it necessary for a steel worker to put his name on a steel ingot that he produces in the course of his duty? If not, why should a member of the intelligentsia enjoy the privilege of putting his name on his intellectual product?" (Priest, 2006, p. 805). This kind of socialist thinking still has an influence on copyright protection today.
After China began its opening-up in 1979, the formulating of a copyright law was finally incorporated in the state’s agenda with the aim of attracting foreign investment and keeping in line with international standards. In 1990, after a decade of intense debate on the appropriateness of copyrights in a socialist system, the National People’s Congress finally issued the PRC’s first Copyright Law. Then in 2001, the Copyright Law was amended to conform to the Agreement on Trade-Related Aspects of Intellectual Property (TRIPS) of the World Trade Organization and deal with the challenges posed by new technologies. To comply with the requirements of the copyright law, the Criminal Code was amended in 1997, to include a section on intellectual property crimes. According to this section, “Those who commit for-profit, unauthorized copying that results in a ‘relatively large’ (50,000 yuan in profits for an individual or 200,000 yuan in profits for a company) amount of illegal gains are subject to a fine and a maximum of three years in prison, while those who copy and earn a ‘huge’ (200,000 yuan in profits for an individual or 1000,000 yuan in profits for a company) amount of illegal gains are subject to a fine and/or three to seven years in prison” (Priest, 2006, p. 813). This criminal provision greatly increased the legal risks for the copyright infringement violators who were just subjected to fines before this law was introduced. Then in 2004, in the judicial interpretation of the Criminal Law issued by China’s Supreme Court, the criminal liability threshold for copyright infringement was further lowered.

With these developments, China has progressively constructed a complete copyright system of laws that meets international standards in most of its provisions. However, whether the
copyright law can be effectively implemented in China is questionable.

As Wang Shujen (2010) has indicated, there are many obstacles arising from the administrative departments themselves when cracking down on piracy in China, such as local protectionism, conflicts of interests between different departments, and official corruption. Among these factors, scholars consider local protectionism to be the largest obstacle (Wang, 2010; Priest, 2006). Although China’s central authorities understand that copyright protection will benefit China’s economic development in the long run, and China’s central government has made substantive progress in the legislative processes of copyright protection, yet this kind of “elite attention” probably does not extend to local bureaucracies who have other more pressing and immediate priorities. For many local officials who are under tremendous pressure for economic development, copyright infringement may provide far more revenues than its licit counterpart can. Sometimes, the local leaders even have a direct interest in the piracy industry, thus creating obstacles for copyright protection.

Secondly, there were still many structural problems in the organizations responsible for copyright administration in China. Confusion can easily arise because the implementation of copyright protection is spread among different government agencies and offices such as the State Copyright Bureau, the State Administration of Radio Film and Television, the Ministry of Culture, the Ministry of Information Industry, and the Ministry of Public Security. Moreover, many copyright infringement cases provide good opportunities for the bureaucratic agencies to reap benefits, since the copyright infringement criminals are willing to pay fines
or even bribes to avoid criminal prosecution.

However, since the central government is trying to support the culture industry, which includes the film industry, as a new engine for the development of the national economy and for the transformation of the economic structure from an economy depending on investment and exports to an economy driven by domestic consumption (Li, 2011), improving copyright protection has became an urgent affair for the government because copyrights are deemed to be essential for the development of culture industry. Moreover, foreign governments and international organizations are pushing the Chinese government to enhance its copyright protection and combat piracy. Thus, we will see more and more copyright laws issued and implemented by the government to improve the copyright protection of film and other cultural products.
Chapter 3: The Rise of Two Competing Online Film Exhibition Networks in China

The history of the Internet in China is not as long as the history in the U.S.. It was not until September 1987, that a research group built up an email node at the Beijing Computer Application Technology Research Institute and successfully sent an email to Germany on September 20, with the symbolic title “Across the Great Wall we can reach every corner in the world”. On April 20, 1994, the state-supported National Computing and Networking Facility of China (NCFC) project opened a 64K international line dedicated to the Internet, which made China officially recognized as a country with fully functional Internet accessibility. Then in 1997, the Chinese Internet project was listed on the construction agenda for the state information infrastructure, and the China Internet Network Information Center (CINIC) was set up to trace the future development of the Internet in China. The CINIC soon published the first Statistical Report on Internet Development in China, which announced there were 299,000 computer hosts and 620,000 Internet users in China as of October 31, 1997. Since then, as the construction of an Information Highway has become a national project, the Chinese Internet has developed rapidly.

However, before 2000, the online exhibition networks for films were underdeveloped in China because the Internet speed was too slow to support the transmission of big video files. This situation began to change as the three major telecom operators including China Mobile, China Unicom, and China Network Communications initiated their broadband service plans
for family users around 2000. Since then, broadband has increasingly become the main means of Internet access for Chinese users. The constantly improving Internet speeds have enabled users to watch and share video files online more conveniently, and Chinese Internet users are no longer satisfied with just sending emails or browsing websites, they want to enjoy more online entertainment, including watching films. Against this background, two competing online film exhibition networks have been established. One is the legal online video websites; the other is the online piracy network.

The rise of Chinese online video websites

The beginning of Chinese online video websites based on piracy

Online video websites refer to the websites that stream online videos to an audience. Their emergence follows the permeating process of broadband, since the streaming of video needs high-speed access to the Internet. On November 2004, letv.com was launched as the first specific online video website in China. In 2005, tudou.com, 56.com and joy.cn successively went online. Then in 2006, youku.com and ku6.com were founded. These “early birds” became the major players in the Chinese online video market thereafter. Although in 2007, there were already more than 300 online video websites competing in the market.

However, the early development of most of the Chinese online video websites was ignoble. By providing a great deal of piracy film and television content to Internet users and selling their users’ attention to advertisers, these online video websites accumulated their primary
capital.

The Safe Harbor Principle was generally used by the online video websites as a shield to avoid the legal risks accompanying their piracy content. According to this principle, the Internet service providers were exempt from the copyright infringement claims made against them based on the conduct of their customers or users, if these providers promised to implement a “notice-and-takedown” procedure, which means the quick removal of infringement content upon receipt of a takedown requirement from the copyright owner. The Safe Harbor Principle for the Internet industry was first established in the *Digital Millennium Copyright Act* introduced in the U.S. in 1998, and then adopted in China’s *Regulations on the Protection of the Right to Network Dissemination of Information* issued in May, 2006. The Safe Harbor Principle was intended to protect the freedom of information on the Internet. However, in practice this principle was, and is, frequently used as a shield by the Internet service providers to conduct copyright infringements.

In the early development phase of Chinese online video websites, they generally encouraged users to upload content. Some of this content was created by users, but the majority of the content was unauthorized uploads, including classic movies and popular television programs. Although the operators of these websites clearly knew their users' actions were infringing copyrights, they just turned a blind eye to it. They were reluctant to delete the piracy content unless the copyright holders threatened to sue them in the court. Sometimes, the online video websites even uploaded the piracy content themselves. As Lu Wensheng, the board chairman
of a major video website Joy.cn in China, once admitted, much of the uploaded content on the website at the beginning was compressed files from DVDs. The equipment necessary for the compression cost at least 30,000 yuan, which was beyond the means and intentions of ordinary users. Actually much of the piracy content was uploaded by employees of the video websites pretending to be ordinary users (Computer Newspaper, August 28, 2009).

The development of Chinese online video websites driven by foreign venture capital

Based on the attractive content derived from piracy, the Chinese online video websites developed at a rapid pace. Unsurprisingly, the booming online video market drew the attention of many venture capitalists seeking investment opportunities in China. The participation of venture capital further facilitated the development and restructuring of the online video industry in China. According to data from China Venture, venture capital of more than US$1 billion was invested in the Chinese online video market from 2004 to 2011. As table 3.1 shows, the investment increased dramatically year by year, although it fell in 2006 and 2009 due to policy changes and the economic crisis. The two leading Chinese video websites youku.com and tudou.com received the most venture capital: youku.com receiving US$160 million and tudou.com US$135 million before their IPOs (imeigu.com, 2011).
Table 3.1

Venture Capital invested in Chinese Video Websites, 2004-2011

<table>
<thead>
<tr>
<th>Year</th>
<th>Venture Capital Invested in Chinese Video Websites (in US million dollars)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2004</td>
<td>3.5</td>
</tr>
<tr>
<td>2005</td>
<td>56.86</td>
</tr>
<tr>
<td>2006</td>
<td>29.20</td>
</tr>
<tr>
<td>2007</td>
<td>141</td>
</tr>
<tr>
<td>2008</td>
<td>158</td>
</tr>
<tr>
<td>2009</td>
<td>84.78</td>
</tr>
<tr>
<td>2010</td>
<td>207</td>
</tr>
<tr>
<td>2011</td>
<td>338</td>
</tr>
</tbody>
</table>

Source: imeigu.com, 2011

Most of the venture capital invested in Chinese video websites was from foreign countries, especially from U.S. companies such as International Data Group, Bain Capital and Maverick Capital. But according to Chinese government’s Measures for the Administration of the Publication of Audio-Visual Programs through the Internet or Other Information Network, “No solely foreign-owned, Sino-foreign joint venture or Sino-foreign cooperative institution may undertake the business of publication of audio-visual programs through an information
network” (SARFT, 2004). Moreover, the government imposed a 50 percent cap on foreign investment in value added telecommunications services and a 49 percent cap on foreign investment in basic telecommunication services.

Therefore, foreign venture capital could not invest directly in Chinese online video websites, it had to establish a Variable Interest Entities (VIE) structure to complete the investment. The VIE structure, also known as contractual control, uses various contractual arrangements to avoid direct foreign ownership that may trigger restrictions in domestic markets (Hogan Lovells, 2012). As shown in Figure 3.1, under a typical VIE structure, the founders of Chinese video websites who have Chinese nationality first register as the shareholders of a domestic capital company in China. This company is then used to hold the required licenses and permits which are needed to operate an online video business in China (shown in figure 3.1 as "OpCo"). Then these founders also set up an offshore company, typically in the Cayman Islands for taxation purposes. This company is used for the purpose of offshore financing, which can be invested by foreign venture capital and listed on the foreign stock market (shown in figure 3.1 as "HoldCo"). Then this offshore holding company establishes a wholly foreign-owned enterprise (WFOE) in China. This company then becomes the actual controller of the domestic capital company ("OpCo") through the contracts, such as Equity Interest Pledge, Proxy and Call Option with the shareholders of domestic capital company. The revenues of domestic capital company will flow to the wholly foreign-owned enterprise ("WFOE") in the form of cooperation/technical/consulting services fees. There are many
Chinese internet companies controlled by foreign capital in this way, including the biggest companies such as baidu.com and sina.com which have already been listed on the foreign stock market through their foreign parent company. According to a report by the China Securities Regulatory Commission (CSRC), by August 2011, there were already 40 Chinese Internet companies listed on foreign stock market (primarily on Nasdaq and the New York Stock Exchange) with a VIE structure, having a total market value of approximately US$160 billion (CSRC, 2011).

Figure 3.1 A typical Variable Interest Entities (VIE) structure
By October 2011, there were already four Chinese online video companies that had gone public, including Letv.com (August 12, 2010, listed on Shenzhen Stock Exchange), Ku6.com (August 17, 2010, listed on Nasdaq), Youku (December 8, 2010, listed on the New York Stock Exchange), and Tudou.com (August 17, 2011, listed on Nasdaq). In addition, there were another five Chinese online video websites owned by public companies, including video.sina.com.cn (owned by Sina, listed on Nasdaq in 2000), tv.sohu.com (owned by Sohu, listed on Nasdaq in 2001), v.qq.com (owned by Tencent, listed on the Hong Kong Stock Exchange in 2004), qiyi.com (owned by Baidu, listed on Nasdaq in 2006), and 56.com (owned by RENN, listed on NYSE in 2011).

With the growing number of online video users in China, foreign venture capitalists' interest in Chinese online video providers has been sustained. According to *The 31th Statistical Report on Internet Development in China*, issued by CNNIC, the number of online video users in China was 372 million at the end of December 2012, 47 million more than the end of December 2011 (CNNIC, 2013). Online video users accounted for 65.9 percent of all Internet users by the end of December 2012 (CNNIC, 2013), and there is still room for the number of users to grow. Furthermore, as a report by McKinsey & Co. reveals, the average Chinese user spends four hours a week watching online video content, which is double the time spent watching video by users in the U.S. (Lau, 2011). The large amount of online video users in China and their relatively long viewing hours has made the Chinese online video market an increasingly lucrative market.
According to the data from Iresearch, the spending on online video advertisements in China increased from 100 million yuan in 2006 to 2.2 billion yuan in 2010, representing a compound annual growth rate of approximately 115.3 percent. And according to the estimation of a research report from Research and Markets, in the next five years, the market size of the online video industry in China will maintain an annual growth rate of over 30 percent (Reuters, 2011). This is why although most of these websites are remaining in the red; they are still favored by the domestic and foreign venture capital.

Exploration of the profit model and the legalization of Chinese online video websites’ content

With the rapidly increasing number of users for online video websites, the cost of bandwidth and operations also increasing, and thus imposes great pressure on the online video websites. In order to make a profit and then be listed on the stock market, the video websites have actively explored their profit models and completed the legalization of their content accordingly.

In general, the video websites earn revenues from three profit models. The most important one is the advertising-supported model, under which users can watch videos for free but they have to view some advertisements. The advertisement formats include pre-roll or post-roll video advertisements, in-roll logos, background advertisements, and the advertisements are banners, buttons, or links. The second model is the pay-per-film model, under which the users
watch films by paying in micro-charges (3-5 yuan) for each viewing. The third model is the subscription model, under which users purchase a pre-determined time period.

In order to expand the channels of making profits, most of the Chinese video websites employ all three models at the same time and apply a segmentation strategy on content, price, broadcasting time and service quality, which aims at making the three models work in coordination. Usually the content of the pay-per-film model are high-quality films that have just finished their theatrical runs. Without attached advertisements, this content usually has a fast buffering speed and most of them have high-definition image quality. Then the subscription model is usually applied for some old but high-quality films, such as the classic films made by Hollywood. Under the advertising-supported model, the content is more diverse but with lower market value, including the content that has moved out of the pay-per-view database after their window has expired, as well as the videos uploaded by users, or the ordinary entertainment programs and TV series purchased from TV stations.

For the content copyright holders, the online video websites were threatens at the beginning, but then gradually became benefit sources as the websites began to remove the pirated content and extensively purchase content from copyright holders. This reversal, for the reasons illustrated below, is an inevitable choice for the online video websites if they intend to make their profits above board and draw the interest of venture capitalists.

Firstly, the launch of the pay-per-film and subscription models, made the video websites unable to use the Safe Harbor Principle indulging piracy videos uploaded by users, because
the content library under the two models has limited videos that can be screened by video websites, and those high-quality contents are also valued most by the copyright owners. If the video websites make profit by broadcasting those contents in an unauthorized way, they will face risks of lawsuits.

More importantly, video websites face pressures from advertisement agencies when they develop the advertising-supported model, especially the pressure from those international branding firms that could bring huge revenues. According to Gong Yu, the CEO of Qiyi, because of the piracy problems in Chinese video websites, many large international brand firms and advertisement agencies are reluctant to launch advertisement on those websites in order to avoid the legal and branding risks (Gong, 2010). To expand revenues by alluring the advertisements from those big brands, Chinese online video websites have to complete the authorization of contents. Take Youku for example, its advertisement revenues reached 119 million yuan in the first quarter of 2011, an increase of 165 percent with the first quarter in 2010. According to the company's financial report, the increase was mainly attributable to the increase in advertisers, who showed more interests in advertising on Youku after it made great efforts to reduce the unauthorized content on the website. The high quality content for which Youku obtained the exclusive broadcasting rights from the copyright holders had the most appeal for advertisers (Youku, 2011).

Secondly, when the Chinese online video websites planned to be listed on the stock market, their piracy content and related lawsuits could seriously affect the confidence of investors.
The listing process of some video websites was postponed because of copyright infringements. For example, Xunlei.com, one of the main Chinese online websites, submitted its IPO application to NASDAQ in June 2011, with the intention of rising up to US$200 million from the U.S. stock market. However, its IPO was postponed several times, and was eventually cancelled in October, 2011. According to many industry analysts, Xunlei’s notorious reputation for copyright violations was one of the main reasons for this (Science Times, December 1, 2011). It was subject to a total of 108 lawsuits in China for alleged copyright infringements in 2009, 126 lawsuits in 2010, and 10 lawsuits in the first quarter of 2011. And there were 32 copyright infringement lawsuits pending against it, at the time it submitted IPO prospectus (Xunlei’s IPO prospectus, 2011, p. 18). As the U.S. has a much stricter copyright protection system than China, Xunlei’s terrible performance on copyright protection was considered a big risk by potential investors.

The last, but most important reason, for the legalization of content on Chinese online video websites was the Chinese government greatly improved its enforcement of copyright protection in recent years. As mentioned previously, the government is trying to erect the culture industry as a new engine for the development of the national economy and for adjusting the economic structure from an economy dependent on investment and exports to an economy dependent on domestic consumption. The 12th Five-Year Plan of the Chinese Communist Party (2011-2015) has made it clear that the culture industry should contribute at least 5 percent of the total GDP by 2015, whereas it currently accounts for less than 2.5
percent (Li, 2011). Therefore, improving copyright protection has become an urgent affair for
the government.

Against this background, we are seeing more and more copyright laws introduced, and
policies have been issued and implemented by Chinese government to improve the copyright
protection of films and other cultural products. The State Council issued the *Outline of the
National Intellectual Property Strategy* in June 2008 and the *Cultural Industry Promotion
Plan* in November 2009. The two documents upgraded IPR protection and the fight against
piracy to a national strategy.

Under these two documents, related government departments have released a series of
concrete measures to enhance the copyright protection of cultural products. For instance, in
2005, the National Copyright Administration of China (NCAC), the Ministry of Public
Security, and the Ministry of Industry and Information Technology launched an annual
campaign to combat Internet piracy. According to a regulation issued by SARFT and the
Ministry of Industry and Information Technology in 2007, all providers of online audio and
video have to apply for an "online Audio-Visual Broadcasting License". In September 2010,
the National Copyright Administration of China puts 15 major video websites on its checklist
and ordered them to launch self-inspections and remove any unauthorized videos; otherwise
they would be shut down. In 2011, the number of video websites on the checklist increased to
18. Under these regulations, the Internet copyright environment in China improved
significantly, and the ability to end copyright violations therefore became a life-and-death test.
for video websites.

**The rise of online film piracy network**

However, when considering the Internet's impact on the film exhibition industry in China, the rise of legalized Chinese online video websites is just one side. There is another side, namely the online piracy network, which is generally deemed harmful to the Chinese film industry. However, if we look at this illegal online film exhibition system more closely, we will see that it also has a positive role. Thus, based on insight of the technological, economic and social factors behind the rise of online film piracy network, this section tries to construct a dialectical framework to understand online piracy.

**The history of the online piracy network**

Online film piracy refers to the unauthorized sharing of films via the Internet. It has various forms, such as unauthorized streaming through websites or client software, file sharing between friends through Internet relay chat software, file sharing among wider users through peer-to-peer (P2P) networks, and file transfer protocol or online storage sites. Among these forms, P2P network sharing is the most popular and mainstream way of online film piracy, due to its technical innovations.

P2P piracy requires an installation of P2P software, such as EMule or Bittorrent. After the software has been installed on a computer, that computer becomes both a client and a server in a P2P network. By basing a user's allowable download speed on the amount he offers in
uploads, the P2P network harnesses an individuals' unused upload bandwidth for other users, and the bandwidth cost for file uploading is redistributed among the downloaders (Cohen 2003). By using swarming technology, the large files on P2P networks are disintegrated into smaller chunks, and then the downloader can simultaneously obtain different parts of a single file from different sources. Based on these technical innovations, P2P networks dramatically accelerate the speed of file sharing. The more people download the same file, the faster the speed is. Therefore, P2P downloading is strongly favored by Internet users. By the end of 2004, BitTorrent, the most popular P2P network, reportedly accounted for as much as 30 percent of all Internet traffic. Not surprisingly a large proportion of P2P traffic is film files (Cachelogic, 2005).

According to a report by the MPAA on January 2011, approximately 23.8 percent of global Internet traffic infringes copyrights, with BitTorrent accounting for almost half of the traffic. Cyberlocker traffic contributed 5.1 percent of infringing traffic and video-streaming sites, such as as MegaVideo and Novamov, contributed 1.4 percent. Other peer-to-peer networks (e.g., eDonkey and Gnutella) and file sharing arenas such as Usenet were responsible for the rest of the infringing traffic (MPAA, 2011).

However, with the rise of online video websites, Internet users increasingly tend to watch the streaming video, rather than watch after downloading from P2P networks. Therefore many piracy video websites have emerged. They operate in a similar way to the legal video websites, except their content is unauthorized. Due to their illegal status, piracy video websites are
always subject to the risk of being shut down by the administrative department. And since it is
difficult for such kind of illegal websites to attract advertisers, the advertisements that appear
in these websites are generally from businesses that operate in the grey areas of the law, such
as the sex industry. Sometimes these websites even contain computer viruses that steal users’
information for profit.

As online piracy increasingly threatens the survival of film and other sectors of the culture
industry, the Chinese government has taken action to control it in recent years. For instance,
more than 500 P2P websites were closed in 2009, including the biggest piracy content sharing
websites verycd.com and Btchina.com. However, online piracy is evolving to escape the
crackdown. For instance, new Internet software called Raysource has emerged as an
important piracy platform. With this software, the user can upload files or download files
from the related cyberlockers on rayfile.com. Cyberlockers provide users with online storage
space to preserve and share files. Cyberlockers are not a new technology, but Raysource has
introduced technological innovations that allow users to upload and download files more
quickly. When users upload files, Raysource can quickly assess whether these files already
exist in the database using Hash comparison technology. If the file exists, it will be
automatically transferred to the user’s account, thus reducing the time-consuming upload
process for users. When users download files, Raysource accelerates the speed by combined
FTP and P2P download models, which allows the file to be downloaded from Raysource’s
server and also other users’ computers at the same time. To reduce the legal risks, Raysource
does not allow stored content to be searched for on its own website. Instead, users must search via a third-party index site. Furthermore, users usually upload files anonymously and add secret code to the files and then share the file downloading link and code with friends. Only people who have been given the password can download the file. Therefore, it is quite difficult for copyright protection agents to ascertain whether the content stored on Rayfile.com is copyright infringing content. Internet piracy technology is evolving all the time, which makes combating piracy much tougher.

The challenges brought by online piracy network to film industry

Actually before the emergence of online piracy networks, there were already many forms of film piracy, such as copying and distributing films in disc format, or the unauthorized public exhibition of films using illegal copies. However, compared to the traditional forms of film piracy, online piracy is a more serious challenge to the film industry because of two prominent characteristics.

Firstly, the Internet piracy network is transnational. Domestic users can access foreign piracy conveniently. Some domestic piracy websites even have their servers in a foreign country to evade the Chinese government's administration. In theory, the availability of online supply is available all the time, everywhere. Therefore, the Internet has dramatically increased the ability of film pirates to reach customers overseas, creating further opportunities and incentives for pirates and more challenges for copyright protection. Cyberspace has
“deterritorialized” nation states, as global technological and economic progress and integration between countries increasingly erases the boundaries of nations. Therefore, as Appadurai argues, “the imagined communities” in this new era are linked more by technical systems of media and communication than by geographic locale (Appadurai, 1996, p. 49). The autonomy and sovereignty of the individual nation-state is inevitably being lost in this globalization process.

Secondly, the online piracy network does not fall under the laws of scarcity economics. Since cultural commodities often tend to act like public goods, culture industry companies respond by limiting the right to copy and charging for the right to copy, thus making cultural goods scarcer than they might otherwise be. This kind of false scarcity is considered to be the one of the baselines for the culture industry (Hesmondhalgh, 2007). However, the online piracy network violates this rule by encouraging users to copy, share and distribute for free. Actually, the more people share a file, the quicker the download speed is.

Based on these characteristics, online piracy has caused increasingly larger losses to film industry. According to The Cost of Movie Piracy issued by the MPAA in 2008, the major U.S motion picture studios lost US$6.1 billion in 2005 to piracy worldwide. 62 percent of the US$6.1 billion loss results from piracy of hard goods such as DVDs, while 38 percent was the result of online piracy. Nowadays, the percentage of online piracy is probably much higher than 2008 as the number of Internet users significantly increased in recent years.

The above-mentioned report also investigates the piracy problem in China. It accused China
of having the highest piracy rate (90 percent) of all countries surveyed. This figure was given by Li Guo Ming (李国明), the vice-president of the China Film Copyright Protection Association, in a talk in 2008. He also admitted that online piracy had overtaken DVD piracy as the main source of copyright infringements (Beijing Business Today, Feb 18, 2008).

The growth of online piracy has become a prominent obstacle for the development of the Chinese film industry. Since piracy films are available almost immediately after the legal release of a film, investors are unwilling to put money into any film exhibition platform other than theatrical exhibition, which seriously limits the overall profitability of Chinese film industry.

**Online piracy network as a tool of radical democracy**

However, not all scholars deem the online piracy as a crime past forgiving. Some scholars argue that the damage done to the culture industry by online piracy is overestimated, and they advocate that sometimes piracy can even be of benefit to the culture industry and society.

Some scholars criticize the copyright protection alliance’s method for calculating losses due to piracy. The method used assumes each viewer of an illegal online copy would have otherwise been a paying customer (Walls, 2009). For instance, according to the report *The Cost of Movie Piracy* prepared by the MPPA in 2006, consumers’ spending on the movie industry was US$18.2 billion less in 2005 than it would have been in the absence of all counterfeiting and piracy activity. Of this, US$7 billion was deemed to be the consequence of
illegally downloading movies from the Internet. But critics, such as Lessig (2004), argue that every download does not equal a lost sale. It is apparent that at least some file sharers download content they would not have purchased. This is especially true if the consumers live in a relatively poor country, like China, because many of them would not be able to pay the films and music they download.

Scholars also argue that the role of online piracy in the culture industry should be dialectically evaluated. On the one hand, the content producers and legal distributors and exhibitors are losing money due to illegal downloads. But on the other hand, online piracy may also benefit the culture industry in other aspects. Firstly, file sharers may download to sample content before making a purchasing decision. This kind of piracy provides free publicity for the content and can lead to the purchase of the legal product. Secondly, online file sharing can expose people to films they wouldn’t ordinarily pay to see through traditional channels, which means increased fans and revenues for the movie industry in the long run. Thirdly, in some cases, Internet users are using online piracy networks to access content otherwise unavailable, for example, the films that are not published anymore because the films are deemed not to have a large enough audience to make a profit for the copyright holders. In these cases, piracy is unlikely to harm the culture industry. Instead they will benefit it by promoting the circulation of cultural heritage and enhance the cultural literacy of public. As Lessig argues in his book *Free Culture*, online piracy systems such as P2P downloading networks actually give many cultural works a new lease of life. Furthermore, access to works that would be
otherwise noncommercial "is extremely important to the spread and stability of culture, if the cultural products only have a commercial life but no second life, access to our culture will be limited to what the current market demands" (Lessig, 2004, p. 113). In Lessig’s opinion, it is necessary to distinguish the different nature of piracy when taking copyright protection actions.

Furthermore, there are radical theorists that advocate that Internet piracy can be used as a democratic tool to resist the oppression of authority. As Mark Poster (2008) has argued, “file sharing through peer-to-peer software promises to radically democratize the production and exhibition of culture.” (p. 209). In the highly developed capitalist countries, such as the U.S., the culture industry have developed to a mature level with a well-established market system and copyright protection system. However, in the eyes of radical critics, powerful conglomerates have distorted these systems to serve their own commercial interests. For instance, under the influence and lobbying of these conglomerates, the U.S. government has increasingly expanded the boundaries of copyright protection. People’s fair use of copyrighted content is subject to more and more restrictions. In the last forty years, U.S. Congress has extended the terms of existing copyrights 11 times, and extended the term of future copyrights twice. In 1973, the average copyright period was just 32.2 years, but nowadays the average copyright period is 95 years. Extending the duration of copyrights has dramatically delayed the passing of cultural works into the public domain, which in Lessig’s eyes, serves the interests of cultural conglomerations by crippling the public’s interests (Lessig, 2004, pp.
134-135). Therefore, in the view of some liberal scholars, online piracy can be used as a tool of radical democracy to show people’s resistance to the oppression of profit-oriented media conglomerates.
Chapter 4: The Impact of Online Exhibition Networks

Based on last chapter’s analysis of the two competing online exhibition networks in China’s film market, this chapter further examines how the development of online exhibition networks has impacted on different kinds of film exhibition in China. In general, the films circulated in China can be simply classified into three categories: Chinese commercial films, foreign films and Chinese independent films. Their different destinies under the influence of the Internet in the context of China’s particular political economy are discussed in turn within this chapter.

Online exhibition networks’ impact on the exhibition of Chinese commercial films

Online video websites as a new revenue source for Chinese commercial films

In this thesis, Chinese commercial films refer to films produced and distributed in China under the government’s approval. These are biggest player in China’s film market. According to SARFT, China produced 893 commercial films in 2012 (Liu, 2013). For the producers and distributors of these films, the development of the Internet has brought greater piracy challenges, but also brought new opportunities. And, in general, Chinese film practitioners are welcome the emergence of online exhibition.

This is actually an interesting phenomenon when compared with the situation in Hollywood.
Since Hollywood has a mature release window system to maximize film revenues, distributors have to consider the balance between online exhibition and other exhibition channels when they try to incorporate the online exhibition into this system. On the one hand, as the home video window still generates the most revenue for Hollywood films, if the online exhibition of a film is too early, the interests of the home video window will be cannibalized. On the other hand, if the online release is delayed too much, there is the risk of pirated copies flooding the Internet. The revenues that could have been generated from a timely online release may thus be lost to piracy (Currah, 2006, pp. 450-451). Therefore, Hollywood distributors are continually making efforts to incorporate the Internet into the long-established release windows with the minimal disruption.

However, in China, no such dilemma exists. As explained in chapter 2, the dominate revenue source for films in China is theatre exhibition, and the profits Chinese films make from DVD sales and pay-to-view television are quite limited due to the piracy problem. Therefore, the disruption brought by online exhibition to the Chinese commercial film exhibition structure is minimal. Unlike Hollywood companies, Chinese film companies are pleased to sell their films to the online video websites.

Currently, most of Chinese commercial films are available on online video websites soon after their theatre runs have ended. Many films are even directly exhibited through online video websites. They are first provided as pay-per-view content on the video websites, which charge 3 to 10 yuan per film for a watching time of 48 hours. Then after 15 to 30 days of
pay-for-view, these films are free-to-view on the video websites, although the audience needs to watch some advertisements before they can watch the film content.

Online video websites, therefore, have become an increasingly important exhibition channel for Chinese commercial films. In China, although the number of cinemas and screens is increasing dramatically — there were 13,118 commercial screens nationwide at the end of 2012 — the cinemas all follow a similar screening pattern, rather than a differentiated plan. As movie theatres can only show a few films to the audience several times a day, the number of films that can be accommodated by the theatres is quite limited. According to the data from SARFT, among the 893 Chinese films produced in 2012, only 220 of them were screened in cinemas. And half of the total box office revenue for Chinese commercial films was generated by just a dozen of the films released in theatres (Liu, 2013). Since the majority of screen time is occupied by domestic and foreign blockbusters, the screen time for low-budget films is quite limited. It is common for dozens of low-budget Chinese films to rush into cinemas at the same time, and then quickly disappear because of the intense competition and poor marketing (Yu & Wang, 2011).

Unlike the limited inventory provided by theatres, the inventory provided by online video websites is virtually infinite. Therefore, the Internet opens up new opportunities for the long-tail exhibition of Chinese commercial films. As Chris Anderson explained in his book *The Long Tail*: "In an era without the constraints of limited shelf space and other bottlenecks of exhibition, narrowly targeted goods and services can be as economically viable as
mainstream fare”(2006, p. 52).

Furthermore, as there are a dozen big video websites competing for market share in China, acquiring Chinese commercial films is considered an important tactic for attracting a bigger audience.

For example, according to data from Iresearch (2012), during October 2012, Chinese Web users spent around 380 million hours watching films through online video websites. The majority of the most popular films were Chinese commercial films. As listed below (table 4.1), among the top ten films that attracted the most viewers, eight were the latest Chinese commercial films, the only Hollywood films were The Hunger Games and The Grey.

Table 4.1 The top 10 films viewed through Chinese online video websites during October, 2012

<table>
<thead>
<tr>
<th>Title of film</th>
<th>Number of views (in millions)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Painted Skin: The Resurrection (画皮 2，2012)</td>
<td>2247</td>
</tr>
<tr>
<td>The Lion Roars 2 (河东狮吼 2，2012)</td>
<td>2026</td>
</tr>
<tr>
<td>The Hunger Games (2012)</td>
<td>991</td>
</tr>
<tr>
<td>The Grey (2011)</td>
<td>976</td>
</tr>
<tr>
<td>Decrepit Dream (残梦，2012)</td>
<td>971</td>
</tr>
<tr>
<td>Holding Love (Hold 住爱，2012)</td>
<td>958</td>
</tr>
<tr>
<td>Lethal Hostage (边境风云，2012)</td>
<td>950</td>
</tr>
<tr>
<td>The Unfortunate Car (车在囧途，2012)</td>
<td>771</td>
</tr>
<tr>
<td>Naked Soldier (绝色武器，2012)</td>
<td>724</td>
</tr>
<tr>
<td>-------------------------------</td>
<td>-----</td>
</tr>
<tr>
<td>Due West: Our Sex Journey (一路向西，2012)</td>
<td>557</td>
</tr>
</tbody>
</table>

Source: Iresearch

Therefore, Chinese online video websites spend a lot on purchasing the online broadcasting rights for Chinese commercial films. There are now (January 2013) dozens of Chinese online video websites containing hundreds of Chinese films in their inventory. The price for a film’s online exhibition rights has continuously risen in recent years due to the high competition among video websites.

Between 2007 and 2009, the purchase cost for content was less than 10 percent of the total expenses of Chinese online video websites. But in 2010, this percentage dramatically increased to 22.71 (Yang, 2011). Before 2009, the cost of acquiring the online exhibition right for an ordinary Chinese film was as low as 100,000 yuan, even the online exhibition right for Red Cliff (赤壁, 2008) was only 1 million yuan. But in 2011, the average price of Chinese film’s online exhibition right reached more than 1 million yuan (Liu, 2011). The price for some blockbusters was more than 10 million yuan. For example, the online exhibition right for The Lost Bladesman (关云长, 2011) was 10 million yuan (Liu, 2011). And according to the 2011 Annual Report of Bona Films, the online exhibition right for Flying Swords of Dragon Gate (龙门飞甲, 2011) was sold for 22 million yuan.
Online video websites' strategy to enhance their bargaining power with copyright holders

The explosive growth in the price of the online exhibition rights for Chinese commercial films has increased the great cost pressures on the online video websites. Therefore, the major online video websites are making efforts to enhance their bargaining power with the Chinese film copyright holders.

On the one hand, the major online video websites are trying to construct an oligopoly market structure through expansion, acquisition and strategic alliance. Using capital from the stock market or venture capitalists, the leading online video websites in China have consecutively expanded their market share by attracting the audience with a better service and higher quality content. For example, the websites have invested heavily in expanding their bandwidth, so the audience can access films quicker. They have also provided higher and higher resolution video, so the audience can enjoy a clearer image. Through these tactics, the leading Chinese online video websites have successfully established their competitiveness in comparison with the small video websites that lack the capital to invest in upgrading their content and service.

Moreover, the leading Chinese online video websites have been strengthening their market power through restructuring or acquisitions. The most noticeable example happened on February 16, 2012, when, with the support of its major stakeholders include International Data Group, GGV Capital, General Catalyst and Temasek Holding, the biggest Chinese online video website Youku announced it would acquire the number 2 Chinese online video
website Tudou through a stock-for-stock transaction. After the merger was completed on August 2012, these two websites became Youku Tudou, which now accounts for a 35 percent share of the Chinese online video market, far ahead of its competitors (Chen, 2012).

The expansion and merger of major Chinese online video websites has made the online video market reach a high concentration level. According to Iresearch (2012), during October 2012, Chinese Internet users spend 3.48 billion hours watching online videos, 71.54 percent was spent on the four biggest online video websites, Youku Tudou, Iqiyi, TV.sohu, and Letv.

According to EnfoDesk (2012), another consultancy company that tracks the development of the Chinese online video market, the advertisement market for online video websites is also quickly becoming more concentrated. In the third quarter of 2012, the top eight Chinese online video websites had 75.55 percent of the advertising market.

As a near oligopoly market has been achieved, the leading Chinese online video websites have begun to develop some practices to enhance their bargaining power with the content copyright holders. For instance, on April 24, 2012, Tv.sohu.com, v.qq.com, and Iqiyi.com, three of the five biggest video websites in China, jointly announced the establishment of an alliance called “Video Content Cooperation” (VCC) for content copyright joint purchasing. By cooperating, rather than competing with each other, they can ask for a lower price when purchasing the online broadcasting rights for films.

On the other hand, Chinese online video websites are also trying to decrease their dependence on content copyright holders by increasing their user-generated content (UGC) and
self-produced online video content. According to Youku.com, in 2012, 70 percent of its content was acquired from professional copyright holders, 25 percent was user-generated content, and 5 percent was produced by the website itself. However, user-generated and self-produced content is seeing a steady increase (Chen, 2012).

User-generated content has been a major part of the online video websites' content from the beginning. But since this content is mainly low quality video or unauthorized clips from copyrighted content, it does not attract viewers and advertisers. To improve this situation, the online video websites have begun to provide revenue sharing to encourage users to produce high quality content. For instance, the video website PPS.com has established a specific channel called ipd.pps.tv. Users can upload their original content to this platform and share the advertisement revenue based on the number of clicks for those videos (Wei, 2012).

Moreover, the online video websites have also started to invest in producing content themselves. Some of them have invested in feature films, for instance, Letv.com invested more than 50 million yuan in Metallic Attraction: Kungfu Cyborg (机器侠) in 2009 (Zhou, 2009). This kind of investment helps the video websites to get the film's online broadcasting rights in advance. However, producing a feature film is a high-risk business requiring a lot of money and the patience to wait for a return. Therefore Chinese online video websites have not participated in many feature film projects. Instead, they are more enthusiastically producing a kind of online video content called "micro movie" (微电影). Essentially, micro movies are similar to traditional short films except they are mainly circulated through the online video
websites and social networks. Compared with the ordinary user-generated content, most of the micro movies are made by professional filmmakers who can provide a higher quality product. The online video websites are the main backers for micro movies. For them, micro movies are not just content that can help them to decrease their dependence on external content, but also a revenue source that can allure product placements from brands. Therefore, they are pleased to invest in micro movies. These productions are generally produced in series following the inspiration of *The Bright Eleven* (十一度青春), which is a famous series of micro movies produced by Youku.com and Chinese film Group in 2010. By inviting 11 young directors to produce 11 works reflecting the theme of Youth, this set of micro movies successfully touched the hearts of Chinese citizens and they were viewed more than 200 million times (Dai, 2010). After this, many series of micro movies by online video websites have emerged. And some of them have even involved famous directors and stars. For example, in 2012, Youku.com initiated a project called “Beautiful 2012: Master Micro Movies” (美好2012：大师微电影), which invited four distinguished directors Ann Hui (许鞍华), Gu Changwei (顾长卫), Tae-Yong Kim (金泰勇) and Tsai Ming-liang (蔡明亮) to participate. And Letv.com as well as Video.sina also proposed a micro movie project called “The Power of Dreams” which included the participation of celebrities such as Han Han (韩寒) and Hai Yan (海岩) (Donews, 2012).

Using the above strategies, the leading Chinese online video websites have decreased their dependence on external content, and therefore reduced the power of copyright holders to a
certain extent in the negotiations for the online broadcasting rights for commercial films or television programs. According to Xu Bing, vice president of online video website PPS, the average price for Chinese television series’ online broadcasting rights has decreased 30-40 percent during 2012, even the most popular television series’ price has fallen by 15-20 percent (Xu, April 12, 2012). The prices for the online broadcast rights of Chinese commercial films have not dropped as much as the prices for TV series, but they have also fallen significantly, especially for low-budget films.

The paradox within the online exhibition of Chinese commercial films through video websites

The falling prices for the online broadcasting rights of Chinese commercial films and television programmes has lightened the burden on online video websites. But unfortunately, there are many problems in the business model of online exhibition developed by video websites for Chinese commercial film. The most fatal problems can be described as two paradoxes.

The first paradox is caused by online piracy. Due to the prevalence of the piracy challenge, it is difficult for online video websites to profit from pay-to-view. As the online audience for a film can conveniently find the content provided by video websites through piracy networks for free, they have little motivation to pay to watch a film. According to Zhu Hui Long (朱会龙), vice president of the biggest Chinese video website company YoukuTudou, as of
November 2012, YoukuTudou’s had just 2 million paying users, less than 1 percent of the total users (Imeigu, November 9, 2012).

Therefore, Chinese video websites have to depend on the revenues from advertisements. However, the websites cannot add too many compulsory-viewing advertisements to the video content, because the Internet is an interactive media and users have the autonomy to do other things when waiting for long periods of advertisements to finish, therefore devaluing the advertisements, which is obviously not favored by the advertisers.

Nowadays, on the Chinese online video websites, there are typically 45-60 seconds of advertisements before a 45-minute programme, which is minimal when compared with the 9-12 minutes of advertisements per hour on Chinese television. Furthermore, the average price of an online video advertisement is still quite low. It is estimated that the Cost Per Thousand (CPM) price for an online advertisement is just one-ninth of the CPM price for a television advertisement (Ye, 2012). Therefore, although the users of online video websites total viewing time is one-third of the time the Chinese audience watches television (Ye, 2012), the online video websites’ advertising revenue accounts for less than 5 percent of a television station’s advertising revenue. According to the data from Analysys International, in 2011, the overall revenue from advertisements for online video websites was 4.84 billion yuan, whereas Chinese Central Television alone received 12.7 billion yuan from advertisements during the same year. Although the revenue from advertisements for online video websites has increased dramatically in recent years, it still cannot counterbalance the soaring costs of content
acquisition, bandwidth and operations.

Another paradox is caused by the demise of geographic exclusivity and temporal exclusivity on the Internet, which makes a strategic alliance among online video websites ineffective. In the traditional film exhibition business, cinemas or DVD retailers, generally just provided service for the customers near them, therefore they enjoyed a kind of geographic exclusivity and therefore avoided direct competition with each other. With their geographic exclusivity, these exhibitors could form an alliance to purchase the same content for a lower price without threatening each other's interests, even though they provide the same product.

But with the developments of technology, this geographic exclusivity have been broken by television and the Internet. For example, the film channel of China Central Television can broadcast films to millions of Chinese residents around the country. Fortunately, as the television is a linear media, different film channels can still enjoy temporal exclusivity and avoid too direct competition if they do not show the same content at the same time.

However, in the environment of the Internet, both geographic exclusivity and temporal exclusivity have been transcended. As explained in the previous chapter (p.76), in theory, the availability of online supply is the same everywhere all the time. Although the online video websites have the technology to achieve geographic exclusivity, for example, sometimes those websites are required by foreign copyright holders to just allow the users within China to watch, yet the video websites are unwilling to do this, because that means shrinking their user base and site traffic, which are important for their profits. Moreover, temporal exclusivity
is also broken by the video websites. In most cases, users can access their content any time they want. Therefore, although online video websites can form an alliance to purchase the content from copyright holders at a lower price, it is hard for them to establish their unique competitiveness when they provide the same content.

Under these two paradoxes, most of the Chinese online video websites are still losing money. For example, by the end of 2011, Youku.com’s net loss was 172 million yuan, not much of an improvement on 2010, while Tudou.com reported a net less of 511.2 million yuan.(Chen, 2012). For Chinese online video websites, their future profitability depends on stronger of copyright protection. As this will enable them to make money from pay-per-view or subscription services, and also raise the prices they can charge for online advertisements.

**Online exhibition networks’ impact on exhibition of foreign films in China**

For foreign films, the Internet’s impact on their exhibition in the Chinese market combines opportunities and threats. On the one hand, with the strengthening of copyright protection, Chinese video websites have begun to purchase lots of content from foreign film companies, which have helped expand foreign films’ market share in China. But on the other hand, foreign films are widely distributed in China via the online piracy networks.
Online video websites as an outlet for foreign films to bypass the entry barriers in Chinese market

With the legalization of content on Chinese online video websites, the purchase of foreign films by those websites is expanding. In the beginning, Chinese video websites made bulk purchases of old foreign films which had been imported into China and formerly distributed through theatres, television or DVDs. The Chinese distributors that had imported these old foreign films sold them for a cheap price, but they were not attractive enough for Chinese audiences. Then as the competition became increasingly intense, Chinese video websites began to take further steps to seek direct cooperation with foreign film companies. For instance, on June 28, 2012, the leading Chinese video website Youku.com and Warner Brothers made an agreement to provide a video-on-demand service for Chinese netizens through the Youku Premium Channel. Under the three-year agreement, Warner Brothers will provide 400 to 450 films to Youku, including many films which have not been distributed in mainland China before, such as Hollywood films such as Red Riding Hood and Green Lantern. After this deal, other Chinese video websites followed suit. As shown in table 4.3, several Chinese video websites have established close partnerships with the major Hollywood studios. It was estimated that Chinese video websites imported around 700 foreign films in 2011 (Yu, 2012). And the cooperation model between those video websites and foreign film companies also evolved. On January 13, 2013, Tecent Video, the video website of China’s Internet giant Tencent, announced it had entered into partnerships with Warner Brother,
Universal, Miramax, Lions Gate. With the content support from these Hollywood companies, Tencent Video established a new platform called "Hollywood VIP". On this platform, users can watch one of the latest Hollywood films for just 5 yuan or pay a monthly membership fee of 20 yuan to watch an unlimited number of movies. They might be just a lag of just a few weeks after a Hollywood film has premiered in the North American market before they are exhibited through this platform. For example, *Argo* was available on Tencent Video on November 21, 2012, just 40 days after its premiere in the U.S. (Tech in China, 2012).

**Table 4.2 The major co-operations between Chinese video websites and Hollywood since 2011**

<table>
<thead>
<tr>
<th>Date</th>
<th>Copyright co-operations</th>
</tr>
</thead>
<tbody>
<tr>
<td>June 28, 2011</td>
<td>Youku.com and Warner Brothers made an agreement to provide a VOD service for Chinese netizens through the Youku Premium channel.</td>
</tr>
<tr>
<td>July 15, 2011</td>
<td>Video website Joy.cn announced its strategic cooperation with 20th Century Fox and Sony Pictures. Joy.cn established Hollywood Theatre on its pay channel to provide classic and new releases from those two Hollywood studios.</td>
</tr>
<tr>
<td>September 14, 2011</td>
<td>Chinese Internet firm Sohu's online video subsidiary, TV.sohu.com, announced it had secured the online broadcast rights to more than 400 films from 20th Century Fox over the next three years.</td>
</tr>
<tr>
<td>December 20, 2011</td>
<td>TV.sohu.com announced it had reached a strategic cooperation agreement with Lions Gate Entertainment Corp, which would enable Sohu to have access to more than 300 films and TV series</td>
</tr>
</tbody>
</table>
Youku.com announced it had reached an agreement with 20th Century Fox that would grant Youku Premium the right to offer Fox’s new releases over the next two years, as well as some of Fox’s classic franchises, including X-men, Alien and Speed.

TV.sohu.com announced that it had signed a cooperation agreement with Sony Pictures. Over the next three years, Sony Pictures would provide Sohu Video with the broadcast rights to 600 films, some of which would not be shown in China’s cinemas, such as The Girl with the Dragon Tattoo.

Letv.com announced that it had reached a strategic cooperation agreement with Metro-Goldwyn-Mayer (MGM). MGM would provide films for Letv.com from its gigantic library.

Tencent Video announced it had reached partnership agreements with Warner Brothers, Universal, Miramax, and Lions Gate. These companies would provide films to support Tencent Video’s new service “Hollywood VIP”.

The cooperation between Chinese video websites and foreign film companies are reciprocal. For the online video websites, the foreign films are highly attractive content at a reasonable price. As shown in table 4.5, in October 2012, the top 10 popular foreign films on Chinese online video websites attracted an audience of more than 50 million in just one month. Foreign films have helped online video websites establish their competitive advantages over other entertainment media such as television.
Table 4.3 The top 10 popular foreign films on Chinese online video websites during October, 2012

<table>
<thead>
<tr>
<th>Film Title</th>
<th>Covering audience amount (in thousands)</th>
</tr>
</thead>
<tbody>
<tr>
<td>The Hunger Games (2012)</td>
<td>9910</td>
</tr>
<tr>
<td>The Grey (2012)</td>
<td>9760</td>
</tr>
<tr>
<td>Mirror Mirror (2012)</td>
<td>5110</td>
</tr>
<tr>
<td>When He's Not a Stranger (1989)</td>
<td>4680</td>
</tr>
<tr>
<td>My Mom's New Boyfriend (2008)</td>
<td>4040</td>
</tr>
<tr>
<td>The Mechanic (2011)</td>
<td>3920</td>
</tr>
<tr>
<td>Black Gold (2011)</td>
<td>3760</td>
</tr>
<tr>
<td>Taken (2008)</td>
<td>3290</td>
</tr>
<tr>
<td>The Expendables (2010)</td>
<td>3200</td>
</tr>
<tr>
<td>Spy Kids: All the Time in the World (2011)</td>
<td>3190</td>
</tr>
<tr>
<td><strong>In total</strong></td>
<td><strong>50860</strong></td>
</tr>
</tbody>
</table>

Source: IvideoTracker of Iresearch

For the foreign film companies, Chinese video websites act as good partners for distributing more films and making more profits in China. As explained in chapter 2, foreign films are subject to a strict quota system and the rigorous censorship imposed by the Chinese authorities when exhibited via the cinema, television or DVD exhibition outlets. However,
online exhibition is relatively free for foreign films. They are not subject to a quota system and many of the films have never been submitted to SARFT for approval. Actually, many foreign films shown on the video websites would not pass the censors because of their sexual and violent content (*For example, When He's Not a Stranger* which is listed in the above table). Why have the online video websites become the freest platform in China for foreign films? It is an interesting question that needs to be considered in the political economy context of China.

**Why can foreign films be circulated more freely through the Internet than other exhibition channels?**

To answer this question, we should first consider the ownership of those film exhibition channels in China. As explained in Chapter 2, the traditional film exhibition channels in China, such as theatres, television and DVDs, are mainly controlled by state-owned companies. For these state-owned film exhibitors, political correctness rather than the maximization of profits is their first concern. Therefore, they will strictly impose the state’s quota and censorship for foreign films. However, the Chinese video websites are mainly invested by foreign venture capital. Therefore, when they purchase copyright content, the main concern is market benefits, which is quite different from state-owned companies. Through exhibiting foreign films, especially Hollywood films, they can successfully enhance their attraction to Chinese Internet users. Therefore, importing more foreign films is a reasonable choice for them.
Actually, the Chinese government had tried to nationalize the Internet companies that provide audio-video programs. For example, in 2007, SARFT and the Ministry of Industry and Information Technology (MIIT) released the *Regulation on Administration of Internet-Based Audio-Video Program Services*. It stipulated that from Jan 31, 2008, applicants for Internet-based audio-video program services should be a state-owned sole proprietorship or state-holding unit. The regulation aroused panic among the operators of the Chinese video websites. As mentioned in Chapter 3, the main enterprises that provide Internet-based audio-video program services in China are controlled by foreign venture capital via the VIE structure. If the regulation was implemented, the majority of video websites would be at risk of bankruptcy.

As mentioned in Chapter 3, online video is one of the hottest fields of the Chinese Internet industry for foreign investment. The foreign investment in video websites has reached more than US$1 billion from 2004 to 2011 (Imeigu, 2011). If those websites were shut down because they were not state-controlled companies, it would not just be a disaster for the foreign investment, but also be negative for the reputation of Chinese investment environment to attract foreign investors, especially for the Internet industry, and hamper the implementation of Chinese government's "information economy" strategy.

Therefore, in implementing the policy, the government made some adjustments. On February 3, 2008, the state's explanation of the regulation stipulated that before the regulation took effect, those legal companies without a law or regulation breaking record could re-register and
continue to operate (Beijing Commercial News, 2008), which retained the space for the circulation of foreign films through Chinese websites.

Moreover, the unclear supervision from the Chinese government on parts of the Internet-based audio-video programme, and the conflicts between the two administrative departments SARFT and MIIT around power and interests, also give space for the exhibition of foreign films through Chinese websites.

In China, the operation of a video website is administrated by the SARFT and MIIT. Every legal video website has to obtain an Internet Content Provider License from MIIT, which has a term of five years. And to get the right to transmit audio and visual programmes online, video websites also need to get the Permit for Broadcasting Audio-Visual Programs through Information Networks from SARFT, which has a term of three years. In short, the two administrative departments supervise the “hardware” (Internet connection) and “software” (content) of the video websites, which determines their different interest concerns.

MIIT is responsible for the construction and maintenance of the telecommunication networks and mobile telecommunication networks in China, which include the administration of the three oligopolistic state-owned telecommunication operators: China Mobile, China Telecom and China Unicom. Every website operated in China has to provide their services to consumers via the high-cost broadband or wireless networks from those three operators. Chinese Internet users also have to pay one of the three companies for the access to Internet.

Generally, the cost to the websites and part of the cost to consumers is for the amount of data
flow. As the video data provided by video websites is much larger than pages, pictures, files or music, the telecommunication service providers can charge a much higher flow fee to the video websites and users. For example, according to the annual financial report of Youku and Tudou.com, they spent US$842 million on broadband access in 2012, which is around 29 percent of their revenues. Against this background, the more high-quality foreign films that can be accessed through video websites, the more consumers will be attracted to the websites, and the revenues for telecommunication service providers will be increased. Therefore, because of the interests of state-owned telecommunication service providers, MIIT does not tend to control the content of video websites. It even holds an ambiguous attitude towards piracy content. During the previous campaigns against online piracy launched by Chinese government departments, MIIT always played a subordinate role and it has not individually initiated a campaign to crack down on online piracy.

But SARFT has a quite different standpoint. As the main administrator of the Chinese film industry, SARFT’s main responsibilities are constructing a strong domestic film industry and making sure films fulfill ideological and educational purposes. Too many imported films are deemed harmful to the development of domestic film industry and damaging to society because they spread of Western ideology and culture in China. Therefore, SARFT has introduced a lot of policies to limit the exhibition of foreign films through traditional platforms in China and continuously tries to transplant a similar supervision system on online film exhibition.
For example, the *Measures for the Administration of the Publication of Audio-Visual Programs through the Internet or Other Information Networks*, which was released in 2004, stipulated that each film, TV series, TV animation, feature or documentary film to be broadcast online in China must first obtain a permit from SARFT. The same regulation appeared again in the *Notice on the Content Management of Internet Audio-Visual Programs*, which was released in April 2009, and the *Law for Promotion of the Film Industry (Draft)* which was released on December 15, 2011.

However, this regulation on Internet audio-visual programmes was released solely by SARFT. In the *Regulation on Administration of Internet-Based Audio-Video Program Services*, which was jointly released by SARFT and MIIT in 2007, this measure is missing. It clearly shows that the two administration departments have different ideas on this issue, which gives space for the circulation of foreign films through Chinese video websites.

But the situation may change in the near future. In May 2011, the State Council announced the establishment of a new department, the State Internet Information Office (with the involvement of the State Council Information Office, MIIT, SARFT and the Ministry of Public Security). The primary role of this new agency is to facilitate policy-making and legislative development in this field to direct and coordinate with the relevant departments on the issue of online content administration and to deal with cross-ministry regulatory matters in relation to the Internet industry. However, whether these intentions be realized remains to be seen.
Online exhibition networks’ impact on the exhibition of Chinese independent films

As illustrated in Chapter 1, Chinese film production and exhibition are subject to strict censorship. All films distributed through theatres, DVDs and television need to obtain a license from SARFT or the General Administration of Press and Publication. However, there are also many unlicensed films, which are known as independent films in China. Since the early 1990s, independent films have developed as a new and active player in Chinese cultural production based on the efforts of independent filmmakers, such as Zhang Yuan (張元), Jia Zhangke (賈樟柯) and Wang Xiaoshuai (王小帥). Independent Chinese films generally focus on exploring marginal people and their marginalized life (Zhang, 2006, p. 30), such as the disabled, rock musicians, alcoholics, gays or avant-garde artists. To some extent, independent films reveal hidden realities in society that are not viable for mainstream Chinese films, and they are therefore hated by the Chinese authorities.

The confined exhibition history of Chinese independent film in China before the rise of online exhibition channels

In the early and middle 1990s, most of Chinese independent films were inaccessible to domestic audiences since they cannot enter the exhibition channels controlled by the state-owned institutions. To maintain the reproduction of films, Chinese independent filmmakers sent their works to International Film Festivals to win awards, chase foreign
funding, and seek foreign exhibition opportunities. The domestic audience could only appreciate independent films through some underground channels, which hardly made any profits for the independent filmmakers.

According to the memory of Wu Wenguang (吳文光), the godfather of Chinese independent documentary films, in the early and middle 1990s, the main way for his films to reach the domestic audience was a screening in his home with a video projector. All the members of the audience were his friends, and they numbered no more than ten at every screening. While the friends were watching his films, Wu was frequently in the kitchen preparing food. After the screening, there were no formal discussions, but conversation eating (Wang, 2010). This kind of private screenings organized by independent filmmakers or their friends, are just a gathering of friends, rather than a public activity.

However, with the advent of VCD and film clubs in the 1990s, the inaccessibility of Chinese independent films for the Chinese audience began to change. Some Chinese independent filmmakers began to burn VCDs (and later DVDs) of their works and gave them away to their friends and people within the independent film community. These VCDs were then circulated to a broader audience through various ways, such as private borrowing or semi-overt screenings at cafés (Zhang, p. 159).

Along with the prevalence of VCDs, film clubs also began to emerge in the big cities, which brought together people with a common interest in film. Typically these film clubs were established for watching and sharing films together. The film screenings were usually
arranged in cafés, bars, bookstores or college classrooms. For instance, in April 2000, students and teachers from the Beijing Film Academy established a film club called Shi Jian She (实践社), which was the first organization to regularly screen Chinese independent films.

From 2000 to 2003, Shi Jian She screened almost all of the main Chinese independent films produced up to then. Typically, there would be a discussion session after the screenings. The filmmakers were invited to attend the discussions and answer questions from audience, most of whom were university students. Besides Beijing, similar clubs also began to emerge in the other big cities of China, such as Yuan Ying Hui (缘影会) in Guangzhou, the 101 Film Club (101 电影工作室) in Shanghai and the Independent Film Club (独立电影社) in Shenzhen.

In the early 2000s, as Chinese independent film had developed for more than ten years and many film clubs had been established in the big cities around the country, an impulse to summarize and promote Chinese independent film through a nationwide event emerged. Therefore during September 22-27, 2001, the First Independent Image Exhibition (首届独立影像展) was held on the campus of the Beijing Film Academy, it was organized by Shi Jian She and several other film clubs, and sponsored by the Beijing Film Academy and Southern Weekend (南方周末), a liberal newspaper in China. More than one hundred independent film works (including feature films and short films) were screened during the exhibition. However, this event was interrupted by the authorities on the last day and had to cancel the planned activities (Zhang, 2004).

After the First Independent Image Exhibition, many other Chinese independent film festivals
or exhibitions have been staged. Some of them even became annual events, such as the Chinese Independent Film Festival (中国独立电影节, CIFF) founded in 2003 at Nanjing, the Yunnan Multi Culture Visual Festival (云之南纪录影像展, Yunfest), a documentary film festival launched in 2003 based at Kunming, Yunnan, and the Beijing Independent Film Festival (北京独立电影节) launched in 2006. However, all these independent film events had the same fate as the First Independent Image Exhibition and were frequently interrupted by the authorities and had to cancel scheduled activities or even the whole event. For example, the Chinese Independent Film Festival of 2012 was totally shut down because it was considered unsafe to hold it before the 18th National Congress of the Communist Party of China, which was held around the same time.

The development of Internet mediated exhibition for Chinese independent films

The offline exhibition of independent films, whether through pirated VCDs or screenings at clubs and festivals, were confined to quite a narrow audience and subjected to frequent interruptions from the authorities. It is actually the development of Internet mediated exhibition that has significantly extended the audience for Chinese independent films.

Firstly, the Internet provides far-reaching networks for the domestic audience to share information and organize offline screenings of Chinese independent films, mainly through online forums and social networks.
The first Chinese online film forum Ying Xing Tian Xia (影行天下) was established in 1998 on sina.com, a Beijing-based website. Later, a cinephile Wei Xidi (卫西谛) set up an Internet forum named Rear Window (后窗) in Nanjing in December 1998. Then in 2000, Dian Ying Ye Hang Chuan (电影夜航船) was established by a group of students from Peking University. These three forums, as well as others, quickly became a hit with cinephiles around the country.

By posting their film reviews and comments and discussing users’ reviews and sharing film screening information, the users constructed a virtual community based on their common enthusiasm for films. In the forums, the information on Chinese independent films, such as their awards and reception at international film festivals, and their “banned” status in China, generated a certain curiosity among the users, which mainly consisted of Chinese urban intellectuals; many of whom are now famous filmmakers or critics.

The Internet’s facilitating effects were further enhanced with the development of online social networks, which made the fans of Chinese independent film form into more well-organized online communities. Take the Shen Zhen Independent Film Association as an example, it established official accounts on both Douban (豆瓣) and Weibo (微博), which are the two most influential social network websites in China. As of February 2013, by posting news and screening information related to Chinese independent films, its Weibo and Douban accounts have both garnered more than 4,000 fans. These fans have become the main participants of the weekly screenings of Chinese independent films organized by the Association. Frequently, the producers of these independent films attend the after-screening discussions through online
chatting. If there was no convenient way to bring these people with a common interest together, such discussions and regular screenings would be difficult to achieve. This is where the Internet plays an important role in Chinese independent film.

Moreover, with the rise of online exhibition networks, the Internet has provided a much more direct, convenient and freer circulation channel for Chinese independent films. Nowadays, more and more Chinese independent films can be directly circulated to a wider Chinese audience through online exhibition networks such as video websites. As explained in last section, the Chinese government’s control on online exhibition is much looser than on traditional film exhibition channels. Therefore, it is possible for some independent films to be uploaded onto online video websites by users or by the independent filmmakers themselves. In some cases, the online video websites even pay for the broadcast rights to some independent films, for instance, Fu Xin Hua’s *Ba Gua* (八卦) and Xu Tong’s *Fortune Teller* (算命), which were sold to Qiyi.com.

In an article published in 2002, film scholar and producer Zhang Xian Ming (张献民, 2002) listed 42 films that had been banned by the government between 1992 and 2002. However, 28 of them are now available through the online video websites, which means they are just one click away from the domestic audience in China. The ordinary Chinese audience now has access to the films that were previously inaccessible. For most Chinese independent filmmakers, the emergence of online exhibition networks is regarded as a helpful thing for the circulation of their works.
Can the online exhibition act as a resistance strategy for Chinese independent film?

For Chinese independent filmmakers, it is natural for them to want their films to be seen by a bigger domestic audience. As Zhang Yuan, a pioneer of Chinese independent film, said in 1997, “I am desperate to produce independent films. But foreign audiences and foreign festivals are not enough. I hope to communicate with the Chinese audience. I hope the subject of my films can be wider. I do not want to become part of ‘small community culture’. I do not want my films to become avant-garde films.” (Jiao, 1997). Then in 2001, after the producing Seventeen Years (过年回家), Zhang Yuan’s first film released in China, he said: “I have made up my mind to let this film pass the censorship when shooting. I hope it will reach the audience. Because I have already graduated from Beijing Film Academy for more than 10 years, I will be very disappointed if I can never see any of my films released in the theatres.” (Wang, 2001, p. 166)

Zhang’s attitude and experience is typical of Chinese independent filmmakers. In an environment where the film exhibition channels are tightly controlled by the authorities, moving into the mainstream is their only choice if they want their works to be seen by a large domestic audience. There are many independent filmmakers that have done this, especially when the Chinese state makes friendly overtures to them by offering aboveground opportunities. For example, In November 2003, the SARFT invited a number of underground filmmakers, such as Jia Zhangke (贾樟柯), Wang Xiaoshuai (王小帅), Lou Ye (娄烨), Zhang
Xian Ming, Cui Zi’en (崔子恩), Zhang Ya Xuan (张亚璇), He Jian Jun (何建军), Wang Chao (王超), Li Yu (李玉), Lu Le (吕乐), to a dialogue at the Beijing Film Academy. In the meeting, SARFT delegates advocated that underground directors should be regarded as, “the new blood of the Chinese film industry to be guided and nurtured, rather than renegades whose creativity is choked at the source” (China Today, April 26, 2004). After this meeting, some independent filmmakers, such as Jia Zhang Ke, Wang Xiao Shuai and Wang Chao, began to work in the mainstream film system. For instance, in 2007, Jia Zhangke and Wang Xiao Shuai even accepted a 500,000 yuan subsidy from SARFT to produce their new works (Xu, 2007).

However, with the development of internet-mediated exhibition channels, it seems there are new possibilities for Chinese independent filmmakers to reach a broader domestic audience. Some critics even advocate that online exhibition can work as a resistance strategy for Chinese independent film.

To some extent, it seems that the Internet really provides ways for Chinese independent film to evade the bans and oppression from the authorities, especially through the online piracy network. Actually, the online piracy network has become the most far-reaching platform for the domestic circulation of Chinese independent films. The independent films appearing on online piracy networks come from various sources. Some are from DVDs that were secretly published with the independent filmmakers’ permission as mentioned before, some are pirated from the DVDs distributed in foreign countries or downloaded from foreign piracy websites.
The interesting thing is that although most of these independent films circulating through online piracy networks are infringing the intellectual copyrights of Chinese independent filmmakers, the filmmakers generally connive with or encourage the situation. Sometimes, Chinese independent filmmakers even upload their works to the piracy websites by themselves. For them, as their works are not allowed to be exhibited through the state-controlled exhibition channels in China to make any profit, circulating works through piracy networks can at least expand their domestic influence, although it too does not generally bring them a profit.

However, it may be too optimistic to argue that Chinese independent filmmakers can avoid the control of the authorities if they use the online exhibition networks. The release of Chinese independent films through these networks is not totally safe. When independent films with sensitive subject matter are made available online they gain the attention of Internet user and become the subjects of discussions, then they come to the attention of the authorities and the websites are usually ordered to delete them. For instance, Wang Bing’s *The Ditch* (央迫), which depicts the tragic experiences of hundreds of intellectual’s during the Anti-Rightist Campaign in China. This film was available in the main video websites such as youku.com and tudou.com in 2011, but after it became the subject of discussions about the cruelty of the Chinese Communist Party’s political movements, it soon disappeared from the video websites and even piracy catalogues.

Therefore, we cannot easily argue that online exhibition can work as a resistance strategy for
Chinese independent film. The Chinese authorities still have the ability to censor and control the online circulation of specific content. The much freer environment of the Internet for the time being is actually depends on two political economy factors.

Firstly, as explained in the last section, the conflict of interests among different Chinese government departments generate space for the freer online circulation of Chinese independent films. Secondly, in recent years, the Chinese authorities have not been inclined to enforce the bans on Chinese independent films in a rigorous way. As the above-mentioned 2003 SARFT meeting exemplified, the Chinese authorities are trying to tempt independent filmmakers to join the mainstream rather than preventing them from making and exhibiting their films. As Pickowicz has explained, this is because the cultural liberals in the Chinese Communist Party see independent filmmaking as a useful pressure release mechanism, and allowing independent film production in China, along with turning a blind eye to the limited screening of these films, makes China look good (Pickowicz, 2006, pp. 7-8). All in all, the online exhibition of Chinese independent films still depends on the Chinese government’s policy.
Chapter 5: Conclusion

Based on the analysis of the two competing online exhibition networks in China’s film market, this paper further examines how different kinds of film exhibition in China have been affected by the development of the online exhibition networks. For the convenience of discussion, this paper broadly classified the films circulated in China into three categories: Chinese commercial films, which are produced and distributed with the government’s approval; Chinese independent films, which are produced and distributed outside the state-controlled system; and foreign films, which are imported from other countries by revenue-sharing or buyouts. The different destinies of these three types of film in China under the influence of the Internet were discussed in Chapter 4.

For the producers and distributors of Chinese commercial films, the development of the Internet has brought greater piracy challenges, but also brought new opportunities. In general, Chinese commercial film practitioners are pleased to see the emergence of the online exhibition channel, because it has become an important exhibition channel, especially for low-budget films that cannot be shown in theatres. Nowadays, most Chinese commercial films are available on the online video websites soon after their theatre runs have ended. Unfortunately, there are still two serious paradoxes existing in the business model for the online exhibition of Chinese commercial films developed by video websites.

The first paradox is caused by the online piracy. Under the prevalence of the challenge from piracy, it is difficult for online video websites to make enough profits from pay-to-view.
Therefore, Chinese video websites have to depend on the revenues from advertisements. However, the websites cannot add too many compulsory-viewing advertisements to the video content, as explained in Chapter 4, and the advertising revenues for the Chinese online video websites still cannot counterbalance the soaring costs for content acquisition, bandwidth and operations.

Another paradox is caused by the demise of geographic exclusivity and temporal exclusivity on the Internet, which makes the strategic alliance among online video websites ineffective. Facing the cost pressures generated by the explosive growth in the prices for the online broadcasting rights of Chinese commercial films, the major Chinese online video websites have made efforts to enhance their bargaining power in their negotiations with the Chinese film copyright holders, such as forming an alliance to purchase the same content for a lower price from copyright holders. However, it is hard for them to establish their unique competitiveness when they provide the same content for the same audience due to the loss of geographic exclusivity and temporal exclusivity. For the Chinese online video websites, there is still a long way to go before they find an effective business model to make profits from Chinese commercial films.

For foreign films, the impact of the Internet on their exhibition in the Chinese market is also mixed with challenges and opportunities. On the one hand, foreign films are widely distributed in China via the online piracy network, which has been heavily criticized by foreign film companies. However, the online video websites also act as an important outlet for
foreign films to bypass the entry barriers in Chinese market. In the traditional film exhibition outlets in China, such as cinemas, television channels and DVDs, the foreign films are subject to the strict quota system and the censorship imposed by the Chinese authorities, whereas they can enjoy a much freer circulation through the online exhibition networks. With the process to legalize content on Chinese online video websites, more and more foreign films have been purchased by those websites. This is firstly because unlike the traditional film exhibition outlets in China, which are controlled by state-owned companies, the Chinese video websites are mainly funded by foreign venture capital. For those state-owned film exhibitors, political correctness rather than profit maximization is their first concern. Therefore, they will strictly obey the government's rules on the quota and censorship of foreign films. While for the Chinese online video websites, the main concern is market benefit. Therefore, importing more foreign films is a reasonable choice for them to enhance their attractiveness to Chinese Internet users. Secondly and more importantly, as explained in last section, the unclear supervision from the Chinese government on Internet-based audio-video programmes in some parts, and the conflicts between the two administrative departments SARFT and MIIT around power and interests also give space for the circulation of foreign films through Chinese websites.

For the circulation of Chinese independent films, the Internet has played a more important role. As cultural products that depict the dark side of contemporary Chinese society, Chinese independent films are subject to strict censorship from the Chinese authorities. In the early
and middle 1990s, most Chinese independent films were not accessible to the domestic audience since the films could not enter into the exhibition channels controlled by the state-owned institutions. Then, with the advent of VCD and film clubs in the middle of the 1990s Chinese independent films became more accessible to the Chinese audience. However, the offline exhibition of Chinese independent films, whether through pirate VCDs or screenings at clubs and festivals, was confined to quite a narrow audience and subject to frequent interruption by the authorities. It is actually the development of the Internet mediated exhibition that has significantly extended the influence of Chinese independent film to a wider domestic audience. Firstly, the Internet provides far-reaching networks for the domestic audience to share information and organize offline screening activities on Chinese independent films, mainly through online forums and social networks. Moreover, with the rise of online exhibition networks, the Internet has provided a much more direct, convenient and freer circulation channel for Chinese independent films. For most Chinese independent filmmakers, the emergence of the online exhibition networks is beneficial for the circulation of their works.

However, as this paper argues, we cannot easily say that online exhibition works as a resistance strategy for Chinese independent film. The release of Chinese independent film through these networks is not totally free. The Chinese authorities still have the ability to censor and control the online circulation of specific content. And the online appearance of Chinese independent film still depends on the Chinese government’s policy.
As I mentioned in my introduction, conducting research on the Internet's impact on the film exhibition sector in China can be immature, because the Internet as well as the landscape of the Chinese film industry are changing constantly. Many imponderable factors exist and make research difficult. For instance, when I was writing this thesis, I needed to update the industrial data all the time and cannot easily draw any conclusions since the data are changing all the time. Therefore, I cannot deny there are still many limitations in this study.

This paper has tried to give a clear and systematic description of the Internet’s impact on film exhibition in China by discussing the development of two online exhibition networks and their influences on the circulation of three kinds of film in Chinese market. However, this research is still not critical enough since it emphasizes more on the economical dimension rather than the political dimension. Although I have tried to discuss some political issues related to the Internet’s impact on film exhibition in this thesis, such as the conflicting interests among different government departments which result in the ineffective fight against piracy, there are still many untouched issues that need to be examined in any future research. For instance, with the increasing acquisitions and mergers among the online video websites, will a few websites dominate the online exhibition of films in China? Will they then enter into an alliance with the Chinese government and then limit the free circulation of specific films through the Internet as the state-owned film exhibitors do? And with future reforms and restructuring, will the conflicting interests among different government departments be eradicated and the balance of power between online video websites and online piracy
networks be changed? All of these issues need to be discussed in future research.

All in all, through a preliminary examination of the Internet’s impact on the film exhibition industry in China, this thesis hopes to provide useful information and analysis for future studies.


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CURRICULUM VITAE

Academic qualifications of the thesis author, Mr. PENG Kan:

- Received the degree of Bachelor of Arts from Beijing Normal University, July 2007.
- Received the degree of Master of Arts from Tsinghua University, July 2010.

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