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Harvard Business Review



JULY-AUGUST 2013
REPRINT R1307A

HOW I DID IT...

The CEO of IMAX On How It Became A Hollywood Powerhouse

The Idea: **The company experimented with business models to grow from its modest roots in nature documentaries into a major player in multiplexes around the world.** *by Richard Gelfond*



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by Richard Gelfond

THE IDEA

The company experimented with business models to grow from its modest roots in nature documentaries into a major player in multiplexes around the world.

When I came to IMAX, in 1994, I had been an entrepreneur, a lawyer, and an investment banker. I didn't know much about the movie business, but I recognized that the moviegoing experience IMAX offered had great potential if we could find the right way to grow.

A partner and I had acquired the company through a leveraged buyout, and we took it public a few months later. On paper the transaction was a success, and the company's market cap grew rapidly. But at the time, most IMAX movies were nature documentaries shown in the theaters of science museums, and figuring out how

to move into mainstream markets proved much more difficult than we'd expected. That was due in part to the technology constraints of the predigital era; it took years to find ways to make it easy and cost-effective to show IMAX movies in a large number of multiplexes. We also faced cultural challenges. The Hollywood movie industry is an interconnected system of studios, directors, and theaters that has evolved over 100 years, and it has a traditional way of doing things. As newcomers we spent years trying and failing to persuade the industry to adapt to our model. Even after we began adapting our strategy to fit the Hollywood way of doing business,

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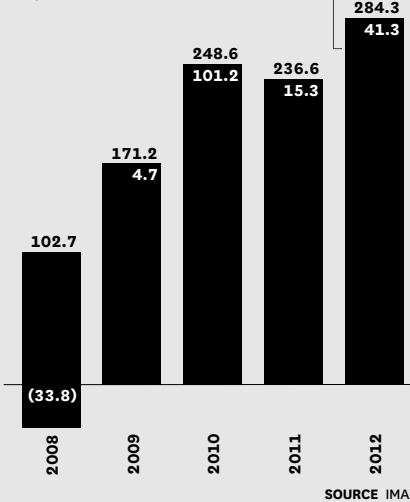
IMAX Facts & Financials

FOUNDED: 1967

HEADQUARTERS: Mississauga, Ontario

SALARIED EMPLOYEES: 509

**REVENUE
AND
NET INCOME**
US\$ IN MILLIONS



it took a while to find a model that benefited us and our partners.

Over the past five years, however, we've developed a business model that makes sense. Since 2008 our network of theaters has grown from 351 to 738. Five years ago eight movies were released in the IMAX format, and so far this year we've announced 27, including blockbusters such as *Star Trek into Darkness* and *The Hunger Games: Catching Fire*, both of which were filmed with IMAX's extremely high-resolution cameras. We're growing quickly in China and other new markets and releasing local-language titles in Japan, India, and Russia. Directors such as Christopher Nolan, J.J. Abrams, and James Cameron are huge fans of our technology—they have come to view IMAX as the perfect canvas on which to execute their artistic vision. We have a large base of “fanboy” enthusiasts who wait in line—and pay a \$5 premium on their tickets—to see a release in an IMAX theater.

The biggest lesson I've learned in nearly two decades of leading IMAX is that you have to be flexible about your business model. It took us many years and several wrong turns before we found the right one, and that's not atypical. When I meet with entrepreneurs who want me to invest in a start-up, the first thing I look for is how attached they are to their business model: Would they consider a plan B or plan C? You're really lucky if your business model works well from day one. Iteration is key.

A Classic Chicken-and-Egg Problem

IMAX's roots trace back to 1967, when four Canadians, three of whom had been friends in high school, created a system for projecting movies onto a giant curved screen that seemingly immerses viewers. The initial public experiment with their technology took place at Expo '67, in Montreal. During its first 25 years, IMAX installed its system in museums, and most of its films were nature documentaries. The company chose that strategy because it didn't have much capital. By focusing on museums, it could get funding from the National Science

Foundation and the National Film Board of Canada to build theaters. It produced nature documentaries because if you film whales, bears, or seals, you don't have to pay them. In those years IMAX was run almost like a nonprofit. Its culture felt like a university's.

When we bought the company, we thought we could send a few new people up to the Toronto headquarters and transform the culture into something nimble and entrepreneurial. It didn't happen—I overestimated the pace at which we could change. We had to replace more people than I'd expected.

The bigger problem, however, was the business model. We'd gotten involved with IMAX because we recognized the potential to shift from science museums to mainstream theaters showing Hollywood movies. But finding the right way to finance that shift proved really challenging. During the 1990s and into the early 2000s, IMAX was licensing its technology to theaters. Theater owners would pay us up front to install our projection and sound systems, and we'd receive a very small percentage of box office revenue. At that time it cost about \$5 million to adapt a theater to IMAX—about \$3 million to create the space and \$2 million to put in the technology.

The huge up-front cost was an obstacle, but not the only one. Very few movies were being offered in the IMAX format. It was a classic chicken-and-egg problem. Studios didn't want to film a movie in our format (which required bulky, expensive cameras and lots of film) unless thousands of theaters were equipped to show IMAX films. Theater owners wouldn't convert to IMAX until many more IMAX films were available.

We attacked these problems as best we could. We brought the cost of the technology down from \$2 million to \$1.2 million, and we figured out how to retrofit existing multiplexes for IMAX, to eliminate the expense of building from scratch. But other disadvantages remained. In the predigital era, studios had to provide every theater with an individual print, and IMAX prints were horrendously expensive: The film reels for a regular movie might cost \$1,000 and fill a couple of canisters, whereas each print of an IMAX film cost \$30,000 and was much larger—you literally needed a forklift to get it to the projection room. Although watching an IMAX film was enthralling, it's understandable why theater owners and studios were reluctant to sign on.

To increase the number of IMAX films available, at one point in the 1990s we even tried producing movies ourselves. It didn't work. I specifically recall a movie we made in 1998 called *T-Rex: Back to the Cretaceous*. We'd hoped it would have crossover appeal to both the science museum crowd and mainstream moviegoers. But the science museums hated it because it wasn't scientifically accurate (they said the dinosaurs had too many fingers), and mainstream theaters felt that it lacked excitement (they'd have been happier if the dinosaurs had eaten some people). Ultimately, we had to find a way to get both theater owners and moviemakers enthusiastic about the IMAX format.

Finding the Formula

Our first break came in 2001, when a computer scientist in our Toronto office figured out how to use computer algorithms to convert existing movies into the IMAX

format. This was huge. Instead of persuading studios and directors to film with IMAX cameras, we could come in after the fact and turn a movie into IMAX. We paid for the conversions ourselves, and in return the studios agreed to give us 12.5% of the gross box office receipts on the IMAX versions.

By 2006 we'd begun to innovate on our business model as well. Rather than charging theaters \$1.2 million for our technology, we started installing IMAX in them at no up-front charge. The theater still had to pay for renovating the physical space—typically about \$150,000 per screen—but the conversion was now fairly affordable. In exchange for our technology investment, we received about 20% of the box office receipts for IMAX films shown on that screen.

This new business model works because consumers will pay a premium to see an IMAX movie, and we've found a way to divide that premium among the various players to create a win-win-win scenario. If it costs \$10.50 or \$11 to see a new release in a theater, a ticket to the IMAX version will cost about \$15 or \$16. That means that even if the studio pays us 12.5% and the theater owner pays us 20%, they still wind up with more revenue than if the moviegoer had bought a regular ticket. And theater owners see that simply having an IMAX theater installed tends to increase overall attendance at their multiplexes.

The final development that propelled us to success was the shift to digital. Since the late 1990s it's been clear that movie theaters were eventually going to shift away from old-fashioned film projection systems, just as homes were shifting from VHS cassettes to DVDs. There was a lot of uncertainty about when to make the change, however, because it would entail high costs, and theater chains had taken on a lot of debt building big multiplexes around that time. By 2006 this uncertainty was really hobbling IMAX: Theaters didn't want to install our film projection system because they figured they'd be converting to digital soon. So we decided to move aggressively into digital, and we began installing the new systems in 2008. The switch provided huge benefits to the company: Those \$30,000 film prints that required a forklift were replaced by \$150 plug-and-play hard drives. Showing a film in the IMAX format became cheap and easy.

We had all the pieces in place to begin growing, but IMAX almost didn't get to enjoy the success. We went through two or three periods of crisis along the way. In the early 2000s most of the major theater chains in America (and many around the world) filed for bankruptcy, and we were left with big receivables we couldn't collect. IMAX still carried a lot of debt as a result of the 1994 LBO, and sometimes we

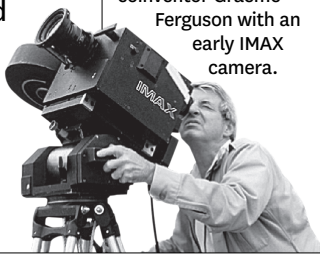


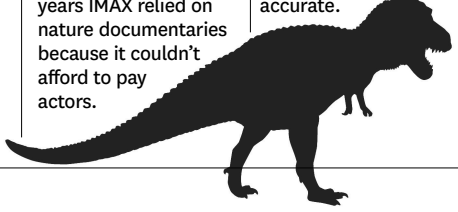
doubted whether we would earn enough to meet those obligations. At one point in 2001 our stock traded for 55 cents a share, and some of our bondholders began buying equity and trying to force us into bankruptcy. In 2006 we actively tried to sell the company, but our future was so uncertain that no one was willing to pay a reasonable price.

These were tough times: IMAX's existence was being tested, as was my resolve. This experience underscored the crucial role leaders play in inspiring and motivating teams through difficult situations.

Thank You, Avatar

We finally began demonstrating real traction in 2009. Our results improved, and we had money to pay down some of our debt. The stock popped, we were given a new bank line, and doubts about our survival faded. The moment I knew we'd make it came in December, when *Avatar* opened. The IMAX version was a global phenomenon. In China there were six-hour lines to get in, and scalpers were charging \$100 a ticket. *Avatar* did \$250 million globally on IMAX screens; because we shared in that revenue, it was a financial turning point for us.

That success helped convince theater owners that IMAX could drive business. Since 2000 the industry has been very concerned that as televisions become big-

<h1>IMAX</h1> <h2>FRAME BY FRAME</h2> <p>For more than half its history, IMAX was heavily focused on nature documentaries and had a culture that felt like a nonprofit's. That began to change in 1994, when Richard Gelfond brought in a new team intent on growing the company.</p> 	<p>1970</p> <p>IMAX technology premieres at the world's fair in Osaka, Japan. The first film shown in THE NEW FORMAT: a 17-minute feature called <i>Tiger Child</i>. Below, IMAX coinventor Graeme Ferguson with an early IMAX camera.</p>	<p>1985</p>  <p><i>The Dream Is Alive</i>, IMAX's FIRST SPACE DOCUMENTARY, was shot by 14 NASA astronauts during three space shuttle missions. It includes footage of launches, landings, space walks, and living in space.</p>	<p>1994</p>  <p><i>Into the Deep</i> uses a specially designed UNDERWATER CAMERA to capture unique marine life and magnificent underwater vistas. For years IMAX relied on nature documentaries because it couldn't afford to pay actors.</p>	<p>1998</p> <p>To get more IMAX movies into theaters, the company PRODUCES ITS OWN FILM, designed to work in both science museums and mainstream theaters. But museums complain that <i>T-Rex: Back to the Cretaceous</i> isn't scientifically accurate.</p> 
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LEFT: The first permanent IMAX theater, housed in a light-studded dome, opened in a Toronto theme park in 1971.



RIGHT: The IMAX theater in London, run by the British Film Institute, contains the largest movie screen in Britain.

ger, home theater systems become more affordable, and streaming allows viewers to access a wide range of movies anytime, people will become less inclined to pay to see first-run movies in theaters. To ward off that threat, theater owners have tried to create a more differentiated experience with bigger screens and better sound systems. (They also invested in 3-D, which generally hasn't lived up to its promise.) This trend has positioned IMAX quite well, as more of the world's leading filmmakers, studios, and exhibitors turn to the format to deliver experiences that audiences cannot find anywhere else. Our commitment to quality and providing a cutting-edge entertainment experience, combined with the differentiation we're able to create by working closely with these key partners, has enabled us to build IMAX into a globally recognized and sought-after brand.

Over the past few years we've been adding 150 to 200 new theaters a year to our network. We used to have to beg studios to make films in the IMAX format, but now a

lot of Hollywood people say you can't really make a blockbuster except in IMAX. As a result, we've become much more profitable. Our business is a little bit like HBO's: Every new subscriber provides additional revenue but hardly any additional cost. It's been a long time getting to this point, but when I reflect back, I think that's probably a good thing. If it hadn't been so difficult to find a way to scale up this business, we wouldn't have been able to buy it for as little as we did. One of the studios would probably have beat us to it.

These days I spend a lot of time traveling overseas, where IMAX is experiencing very fast growth. I started going to China 15 years ago, and that market has always had an affinity for IMAX. Today our brand awareness in China is above 90%. When the 117 theaters awaiting construction have been completed, we will have 250 screens there, and demand is still exploding.

As our network has grown, so has the importance of our brand. From day one I recognized the significance of the IMAX




name and communicating its values: quality, innovation, and providing exciting new entertainment experiences. By consistently delivering on these, we've earned substantial trust in the marketplace, which has allowed us to move beyond our traditional theatrical business.

For many years people have wondered whether we could re-create the IMAX experience in a home theater system. Our recent launch of IMAX Private Theatre will set a new benchmark for the ultrapremium home theater market.

When I first came to IMAX, my background was mostly in transactions. I'd started businesses and sold them, and I'd helped buy and sell companies on Wall Street, but I'd never run a business for a long time. I didn't intend to do that at IMAX—originally my partner and I figured that we'd hire a CEO to run it, or we'd sell it quickly. But I discovered that I really liked running this business, so I stayed. When I was a lawyer or a banker, people didn't understand what I did at work, but everyone likes talking about IMAX. My daughters are grown now, but for years I took them to movie premieres, which was very rewarding.

In this business I've met people with many different motivations—creative, artistic, financial, competitive. It's hard to keep everyone, internally and externally, focused on the bottom line and create win-win scenarios. I've also developed friendships with studio executives, exhibitors, actors, and directors who've become enthusiasts and boosters of our technology and brand. Running this company has had its share of thrills and has helped me lead a very interesting life, but none of it would have happened without experimentation and determination and a great management team. 

HBR Reprint R1307A

2002	2004	2010	2013
 <p>IMAX announces its DIGITAL REMASTERING (DMR) technology, which converts existing movies into IMAX format. The first IMAX DMR release: <i>Apollo 13</i>.</p>	<p><i>The Polar Express</i> is THE FIRST FULL-LENGTH IMAX 3-D Hollywood feature.</p> 	 <p>The IMAX version of James Cameron's sci-fi epic <i>Avatar</i> becomes a global phenomenon (Chinese moviegoers wait six hours in line to get in), grossing \$250 million at the box office and representing A FINANCIAL TURNING POINT for IMAX.</p>	<p>Just a few years ago IMAX offered only eight films a year to theaters, but by the middle of 2013 it has already ANNOUNCED 27 NEW RELEASES, including <i>Star Trek into Darkness</i> and <i>The Hunger Games: Catching Fire</i>.</p> 