Darth’s Dominion

A case study of the Cineplex Odeon empire

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Garth Drabinsky, Chairman and CEO of Cineplex Odeon, has never been known to shy away from a fight. On June 30, 1989, facing a group of angry shareholders, he was true to his reputation. Neither the hostile questions from shareholders, nor the specter of lawsuits pending against him, could mute his forceful style.

Two weeks earlier, under rumoured pressure from securities regulators, Cineplex Odeon had revised its financial statements to show that its day-to-day operations had been less profitable during 1988 than initially reported. The action came on the heels of four separate lawsuits in U.S. Courts alleging irregularities in Cineplex Odeon’s accounting practices. These unsettling developments were much on the mind of the shareholders gathered for the company’s annual meeting at a Cineplex Odeon theatre in downtown Toronto.

To shareholders who rose to demand specific details about the company’s finances, Drabinsky responded in a firm and unequivocal fashion: “I am not here today to give a line-by-line, detailed analysis of the accounting statements at this meeting. I’m only going to deal with the economic direction of this corporation.”

The response reflected a hardball approach to business that had earned Drabinsky the nickname Darth, after the screen supervillain Darth Vader. But this reputation was based on more than just an aura of toughness and fast-dealing; it was founded on significant accomplishments in the movie industry. Through a combination of innovative theatre formats, bold acquisitions, and strong financial alliances, Drabinsky had developed Cineplex Odeon into the second largest theatre chain in North America. In the process, he had singlehandedly changed the face of film exhibition, rejuvenating what had become a stagnant part of the industry.

As long as Drabinsky continued to pile success upon success, his aggressive style and disregard for conventions were tolerated. But now, with doubts being raised about the financial health of Cineplex Odeon, Drabinsky’s reputation as a brilliant strategist was under increasing scrutiny.

A CONSUMING PASSION

Garth Drabinsky’s determination to beat the odds began early in life. Struck by polio at the age of three, he spent most of his childhood checking in and out of hospitals. After a long period of infirmity, he was finally able to walk without a brace, although he has a pronounced limp to this day. The same willpower and concentration that allowed Drabinsky to confront his illness eventually served him in other ways. Although he excelled in a wide variety of activities, it was the silver screen that ignited his passion.

It was during his law studies at the University of Toronto in the early 1970s, that Drabinsky began to make movies his life’s work. He took a keen interest in the emerging field of entertainment law, and later wrote a textbook on the subject which became a standard reference source. His law studies, however, did not prevent him from producing a half-hour TV show starring William Shatner, and launching a movie magazine that was given away free at cinemas.

In 1976, Drabinsky made a foray into movie production. His first film featured Donald Sutherland, but it was never completed. The following year, he teamed up with producer Joel Michaels to form a film production company that remained active for several years. Among the movies that the company produced were The Silent Partner, starring Christopher Plummer; The Changeling with George C. Scott; and Tribute, a vehicle for Jack Lemmon. Although acclaimed critically, none of these films brought in much money at the box office.

A MULTIPLEX STRATEGY

In 1979, Garth Drabinsky joined forces with Nathan Taylor, an industry veteran who had long believed in the concept of theaters with multiple screens. Drabinsky found the idea appealing, and together the two formed Cineplex. Their first multiplex theatre was located in Toronto’s Eaton Centre, and it contained as many as 18 separate theaters, each with a seating capacity ranging between 60 to 150 people.

Cineplex saw itself as a niche player. The company countered an industry trend whereby exhibitors used large theaters to present potentially lucrative releases from the Hollywood distributors. Instead, the newly developed multiplex chain used its small screens to show specialty movies, in particular foreign films and art films that could not be shown productively in large theaters. As Taylor put it, Cineplex was not out to challenge the major chains, but to complement them:

“We are seeking to develop a market that to some extent doesn’t exist. We are taking specialized markets and filling their needs. It’s a latent market and a different niche than the major chains go after.”

Joe Lampel and Jamal Shamsie study and teach business policy.
But Cineplex could also try to get the successful U.S. films after they had completed their run with the larger theatre chains. It was an industry dictum that the share of box office receipts passed to the distributor decreased with the length of a film’s run. However, although exhibitors kept more of the revenues, an inevitable decline in attendance ordinarily forced large theaters to discontinue exhibition once the number of empty seats exceeded a certain level. It was at this point that Cineplex could pick up the films, and by virtue of its small theaters keep most of the seats full.

The primary advantages of the multiplex concept were due primarily to a carefully planned use of shared facilities. A single box office and a single concession stand served all the theaters in a location. The use of advanced projection technology made it possible for a handful of projectionists in a centralized projection booth to screen films in several theaters at once. Show times were staggered in order to avoid congestion. The company even lowered advertising costs by using a single ad for all the films playing at a particular location.

The success of the multiplex concept spurred Cineplex to expand its operations across Canada. The company also made an entry into the large U.S. market with the development of a 14-screen theatre complex in Beverly Hills. By the end of 1982, Cineplex had inaugurated almost 150 screens in as many as 20 different locations.

A CLOSE BRUSH WITH BANKRUPTCY

The company’s rapid rate of expansion soon brought Cineplex face to face with financial and market realities which its owners had not anticipated. During its expansion, Cineplex had amassed $21 million in debt, mostly in high and floating interest rates. This development came in the midst of an economic recession which cut deeply into the company’s earnings. To make matters worse, U.S. distributors were increasingly reluctant to supply Cineplex with the hit films for fear of alienating the two large Canadian exhibition chains, Famous Players and Canadian Odeon. Without the revenues of major U.S. releases, the company’s future looked bleak.

Only drastic measures could avert imminent bankruptcy. Throughout 1983, Cineplex took steps to reduce its debt and improve its cashflow by selling off some of the company’s assets, raising funds through the public offering of more shares, and persuading the banks to extend further credit. But these measures did not address the company’s blocked access to major releases. To break through the barrier, Drabinsky sought government intervention. Using his legal training, he marshalled evidence and convinced the Canadian government that strong grounds existed for launching an investigation into the existence of a conspiracy aimed at depriving Cineplex of access to major releases.

In the face of government investigation, and possible sanctions, the U.S. distributors modified their stand and agreed to a system of competitive bidding that would ensure more equitable access to their films. With this hurdle surmounted, Drabinsky was able to secure more firm financial backing, particularly from institutional investors. One large investment came from a holding company owned by the Bronfmans, the powerful Canadian business family.

To Drabinsky, the close brush with bankruptcy revealed a basic flaw in his company’s position. He became acutely aware that his small theaters generated insufficient revenues to bid for early runs of the most lucrative U.S. films. So when the principal owner of Canadian Odeon died, Drabinsky saw an opportunity that he could not miss. Canadian Odeon had been greatly weakened by the new bidding system that Drabinsky had helped to bring about, and alarmed by their company’s poor performance, the heirs finally accepted Drabinsky’s offer of little over $22 million for the entire chain.

The acquisition of Canadian Odeon in the spring of 1984, at what many viewed as bargain-basement price, ended a remarkable turnaround for a company which two years earlier had faced bankruptcy. Now, with over 450 screens in as many as 170 different locations, Cineplex was a major player in the industry. Drabinsky relished his comeback, and was not above taking a shot at his detractors: “A lot of people who were waiting for me to go under were disappointed. Well, they didn’t get their jollies.”

A LARGER-THAN-LIFE EXPERIENCE

The formation of Cineplex-Odeon crowned Drabinsky’s comeback from the verge of bankruptcy, but he was not content to rest on his laurels. Now that he controlled one of North America’s major theatre chains, he set out to transform the moviegoing experience itself in the face of new competition from pay-television channels and pre-recorded video cassettes.

Drabinsky aimed to lure the public from their homes by renovating the theatres, beginning with their look. Cineplex Odeon discarded the uniformly drab design common in most theatre chains in favour of artwork in the lobbies, lush wooden carpets enhancing marble floors, and coral-and-pearl colour coordinated walls. The screening auditoriums featured scientifically contoured seats, digital background music, and state-of-the-art projection systems. As a final touch, the company re-introduced real buttered popcorn in the concession stands, and cafés that offered freshly-made cappuccino.

But the metamorphosis could not be completed without a new company logo in the form of a curved bowl reminiscent of a Greek amphitheatre, and coloured imperial purple and fuschia. For him, the logo was no static symbol, it was intended to make people sit up and take notice. As Drabinsky put it: “I felt that this would be more of a bravado kind of statement. I don’t think anyone was ready for that.”

Cineplex Odeon’s new format differed sharply from the prevailing industry response to the threat posed by pay TV and video cassettes. Most theatre chains sought to cut their fixed costs by slcing old movie palaces into tiny cinemas, and eliminating many services that were deemed unnecessary. Drabinsky, on the other hand, believed that the moviegoing experience should not be limited to what was shown on the screen. As the customer entered the theatre, he/she was meant to leave...
behind mundane existence and gradually move into a different reality. Said Drabinsky:

We are determined to give back to our patrons the majesty and excitement and anticipation and curiosity that should be theirs when they leave the theater-regimented world of their daily lives for the fantasy world of escape that is the movies.

The transformation of reality is, however, very costly. Cineplex Odeon spends almost $1 million on a typical six-screen multiplex, a third more than the average for the industry. But as far as Drabinsky is concerned, the additional investment bears fruit not only at the box office, but at the concession counter as well. The classier, upscale atmosphere is meant to entice customers into spending more time in the theaters before and after the movie, resulting in higher sales at the concession counter. Indeed, the concessions at Cineplex Odeon's theaters have usually taken in almost $2 per moviegoer, which is close to twice the industry average.

**CUTTING COSTS**

Unfortunately, the additional revenues generated by higher concession sales covered only a small fraction of the fixed costs of a typical Cineplex Odeon theater. In an effort to reduce them, Drabinsky has imposed stringent cost controls throughout his organization. Odeon's management was Drabinsky's first target. Upon acquisition of the company, Drabinsky dismissed about two-thirds of Odeon's head office staff and cut the payroll of the remaining personnel by 10 percent. He also cancelled the company credit cards as an incentive to frugality. As he put it at the time, "When you make people use their own money they think hard about the justification they'll have to provide when filing their expense claims." The cost-cutting campaign has not left any facet of the company's operations untouched. Even the traditional cardboard containers used to sell popcorn have been replaced with bags, a move that has saved Cineplex Odeon close to $1 million per year.

Because these measures were insufficient, Drabinsky has had to look for other sources of revenues to make up the difference. He raised admission fees well above the competition in most markets, and began to show commercials before the screening of the main feature. Both moves were highly unpopular, and irate patrons have expressed their anger in a number of cities, sometimes by protesting outside Cineplex Odeon's theaters. The most publicized of these protests occurred in New York City, where Mayor Ed Koch, Woody Allen, and actor Tony Randall joined picketers in a call for a boycott of the chain because of its price increase.

Drabinsky tempered criticisms against him with promotional gimmicks. Most significant among these is the lower admission prices offered on Tuesdays. Attendance at Cineplex theaters has climbed substantially for these Tuesdays, generating additional revenues, as well as much needed goodwill among customers.

**A POWERFUL COMPETITOR**

With Drabinsky at the helm, Cineplex Odeon launched a major expansion into North America's main movie markets, mainly through a series of acquisitions in the United States. In an industry known for long negotiations and agile deal-makers, Garth Drabinsky has gained a reputation as a tenacious and abrasive businessman. He uses his stamina and his adversarial style of bargaining to wear his opponents down, and then in a burst of energy, he clinches the deal. His biggest acquisition involved the Cineplex Odeon chain, which had run almost 600 screens in over 210 locations.

Drabinsky is impulsive to his competitors. In every market he enters he has used all the means at his disposal to gain market share and keep the competition on the defensive. He pursued Famous Players, his long-standing rival in Canada, with special vengeance. In 1986, for example, Drabinsky seized an opportunity to lease part of a building in Toronto that housed the Imperial Theatre, a sea-theater complex operated by Famous. Since part of the building contained the main entrance to all of the theaters in the complex, Drabinsky could thereby control the show's public access. He used armed security guards with dogs to enforce the blockade. Ultimately, Famous Players was forced to close down and sell this key location to Cineplex Odeon, but not before it extracted a public apology from Drabinsky, and a commitment that the facility would be used to show motion pictures.

Drabinsky has also tried to use the size of his chain to obtain added deals with film studios and distributors. He has consistently obtained potential deals on even favorable terms, but his insistence on having his own way has also created tension in his relationships with his suppliers. The tensions erupted into the open in 1987 when Columbia Pictures rejected Drabinsky's demands that Bernardo Bertolucci's oriental epic The Last Emperor be made available for wide release during the Christmas period. In retaliation, Drabinsky refused to exhibit another of the studio's films that was slated for Christmas release. The episode created tensions in Cineplex's relationships with Columbia, resulting in a number of the studio's films being diverted to other chains, such as Famous Players.

Drabinsky's readiness to challenge industry conventions has upset many who feel that he does not play by the rules. Walter Senior, the president of Famous Players, considers Drabinsky's tactics to be destructive. As he put it in the aftermath of the Imperial Theatre affair: "We all learn in school that when you set out to destroy someone, it becomes weakness." Drabinsky's Chief Administrative Officer, believes that much of the hard treatment meted out to Drabinsky in the press reflects his impact on the industry, rather than simply his style:

There's been a lot of press about Garth, and some of it has been negative up until now. Some of it has been because of his aggressiveness, but more it is because of the antagonism to the moves he's created in the industry.

**VERTICAL MOVES**

In 1982, at a time when Cineplex was still a small company screening foreign and art films, Drabinsky moved to consolidate and expand the company's other film-related activities. These consisted mainly of a filmmaking subsidiary originally started by Nathan Taylor, and a film distribution arm launched by Drabinsky in 1979. The filmmaking subsidiary was located just north of Toronto, and was one of Canada's largest facilities, rented out for both film and television productions. It included two sound stages, dressing and wardrobe rooms, a carpentry mill, a plaster shop, and editing and screening rooms. The distribution arm had originally been created by Drabinsky to provide foreign and art films to the newly developed Cineplex chain. It quickly developed into one of the largest distribution companies in Canada, acquiring the right to distribute films to theaters and on video cassettes, as well as on network and pay television.

In 1986, Drabinsky increased the involvement of his company in filmmaking through the acquisition of Film House, a Toronto-based facility consisting of a large film processing laboratory, as well as a fully equipped post-production sound studio. Subsequent deals in the foreign and art film arena expanded the capacity of the film laboratory and upgraded the sound facilities.

Meanwhile, Drabinsky expanded the film production and distribution activities of his company into the United States. With the move into its new market, Cineplex Odeon was able to step up its participation in filmmaking. The company began to contribute to the production of smaller-budget films such as Paul Newman's The Glass Menagerie, and Prince's concert film Sign 'O' the Times.

Finally, Drabinsky entered into a collaborative venture with MCA, a large U.S. entertainment conglomerate. The two companies agreed to jointly develop and operate a large film studio and theme park in Orlando, Florida, that would compete with Disneyworld. The move reflects Drabinsky's determination to make Cineplex Odeon into a corporation that straddles every part of the movie industry. As he has said:

"It's an amalgamated company with revenue from theaters, distribution, production, the studio, and, down the road, like theatre. People aren't buying a..."
share in this company just to have a share in a motion picture. They're getting a share in a vertically integrated entertainment company. ③

A ONE-MAN SHOW

Cineplex Odeon is, for now at least, firmly under the control of Garth Drabinsky, who, over the years, has consolidated power in his hands. He became President of the company in 1980, added the title of Chief Executive Officer in 1982 and was confirmed as Chairman of the Board in 1986. The titles reflect Drabinsky's total involvement with the company and it is well known that no one else is allowed to speak on Cineplex's behalf.

In both deed and word, Drabinsky attempts to communicate to his employees the total commitment that is expected of them. The managers who work in close proximity to Drabinsky find his driving energy both exhilarating and exhausting. Lynda Friendly, Vice-President of Marketing and Communications since 1982, who sits in on all of Drabinsky's interviews with the press, is inspired by his stamina and drive:

Garth is so bloody energetic. I don't know how he does it. It's mind boggling. He stretches people to their absolute limit. He is a teacher, a mentor - a leader. ③

Other officers, however, feel Drabinsky's energy difficult to emulate. They do not appreciate the midnight phone calls they regularly receive from the Chairman, nor do they agree that they must be ready to sacrifice everything to their work. As a former Cineplex Odeon executive described it, the pressure that Drabinsky puts on managers is relentless:

He works seven days a week and doesn't believe in holidays. Holidays are a disloyalty to the corporation and he is the corporation. He is tireless and he expects the same amount of dedication and effort from everyone else. ③

Some of Drabinsky's immediate subordinates may have found his drive for total control unacceptable. His consolidation of power has been accompanied by a significant turnover among the top executives of the company. Several of the present executive officers have been appointed since 1986. Those who survived the transition are for the most part people with close personal ties to Drabinsky, like Lynda Friendly, for example, or those who have attended synagogue together as teenagers.

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RELENTLESS GROWTH

Cineplex Odeon has not slowed the pace of its expansion in spite of growing financial constraints. The company continues to construct new theaters and to refurbish existing ones. At the present rate of expansion, Cineplex Odeon will have 2,100 screens by 1992, in North America alone. For Drabinsky, the expansion has a dual purpose. First, he would like to secure his competitors and capture an increasing share of the North American market. Second, Drabinsky believes that only a larger Cineplex Odeon can force the major distributors to give him full-time entrepreneurs, who have observed Drabinsky in action observed:

"Anything that is not absolutely perfect drives him crazy. He leaves people with a lasting impression when they screw up." ③

BIG BUCKS BUT ...

As of January 1, 1989, Cineplex Odeon estimated the total value of its equity at $375 million. It is believed that the combined holdings of Drabinsky, Gottlieb and other directors of Cineplex Odeon account for $5 million, or almost 16 per cent of the publicly issued shares.

Cineplex made the transition from private to public financing in 1982 when the company was listed on the Toronto Stock Exchange. In a subsequent deal, Drabinsky sold a large block of shares to MCA, the U.S. entertainment conglomerates which owns Universal Studios.

The deal allowed MCA to purchase up to 50 per cent of the company's outstanding shares. In theory, this move gave MCA control of Cineplex Odeon, but in practice control was restricted by Canadian law, which limits voting shares by foreign companies to 33 per cent. MCA's total ownership is therefore represented by specially created, subordinate, restricted voting shares.

In 1987 Cineplex Odeon consummated its first offering of shares in the U.S., and was listed on the New York Stock Exchange. However, as of December 1987, it was listed on the New York Stock Exchange. However, in spite of these substantial enlargements of the company's equity base, most of the financing during 1987 and 1988 was through the use of debt. Not surprisingly, the price of Cineplex Odeon's shares has fluctuated. It reached a high of almost CDN $25 a share around the time of the MCA purchase, but has dropped considerably since then.

In spite of the decline, Drabinsky continues to defend his gross margins and insists that his chain boasts the highest return on equity among major exhibition chains. The fault, Drabinsky has claimed on one occasion, is to be found in the brokerage industry, and not in the performance of Cineplex Odeon:

The brokerage industry is just full of people who like to hear themselves speak, but there's not a lot of substance there. This company is complete substance from top to bottom. ③
In the risky business of producing big-budget movies, Drabinsky has also extended his production activities to other entertainment areas. For example, the company is converting the Toronto theatre (the Pantages) it wrested from the Famous Players chain into a 2,100-seat centre for the performing arts. The theatre, which was a vaudeville palace in its previous incarnation, will be restored to its former glory, and used to stage the Canadian production of Andrew Lloyd Webber's *The Phantom of the Opera*, this autumn. It is estimated that its initial production cost will total over $6.5 million.

**A PERFORMANCE UNDER SCRUTINY**

Drabinsky's continuous drive for growth has been putting pressure on the company's finances. During 1988, Cineplex Odeon asked the banks to boost its line of credit by another $175 million to $750 million. More recently, the company sold off 50 per cent of Film House, as well as most of its share in the Florida theme park. The company has also been raising capital by selling off some of its theaters and then leasing them back.

In the opinion of a number of industry observers, the true financial position of Cineplex Odeon is masked by the company's liberal accounting practices. In 1986, the company extended the period over which it would depreciate its properties and its goodwill, resulting in much higher values of its total assets. The observers also believe that the company's operating profits are overstated because of its inclusion of one-time sales of assets as part of operating revenue.

The financial uncertainty has created apprehension among the company's stockholders, who can still recall Drabinsky's narrow escape from bankruptcy six years ago. Drabinsky, however, denies that he is undermining Cineplex Odeon by involving the company in activities it can ill afford. He frequently reiterates his conviction that he must, at all times, be ready to take advantage of emerging opportunities and promising deals. When asked in a recent interview to predict the company's future development he had this to say:

> If you asked me five years ago what Cineplex would look like today, I wouldn't have predicted what we have today. So when you ask me today what Cineplex will look like in five years, I can't tell you exactly. 

Publicly, Drabinsky has rebuffed his critics, and has sought to allay shareholders' fears. In private, however, he has moved to gain control of Cineplex Odeon by making a $127 million offer to buy the 30 per cent stake held by an investment group headed by the Bronfman family. As the two sides were putting the finishing touches on the deal, MCA obtained an interim injunction preventing the Bronfman group from selling its 7.5 million shares to the Drabinsky consortium.

MCA is seeking to prevent Drabinsky from gaining control, partly because it is unhappy with his management, and partly because it fears the loss of a guaranteed avenue of distribution. Over the last several years MCA had become increasingly imitated and mystified by many of Drabinsky's forays into areas it considers risky. These feelings were widely shared in the industry, as one analyst put it:

> No one understands what Drabinsky and Gottlieb are up to. They pulled off the Florida deal, they sold off Film House, they are taking bigger risks in film production, and now the Bronfmans are getting out. From MCA's point of view there are probably lots of reasons to stop Garth from getting control. 

### NOTES