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## **Entrepreneurship as a Part of the Creative Industries within the Cultural Sector in a Small Society**

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### **Abstract**

In the paper entrepreneurship is described as a part of the creative industries within the cultural sector by analysing the economic role of cultural activities in a small society, with Iceland as the prime example.

Section 1 includes a description of the contribution of cultural activities to GDP, emphasizing the importance of entrepreneurs and small and medium sized enterprises (SMEs) within the cultural sector and showing illustrations of public expenditures on cultural activities. There are numerous enterprises within the cultural sector in Iceland, most of them SMEs. The role of entrepreneurship is extremely important in cultural activities in most societies. Public expenditures on cultural activities have increased substantially in Iceland. Cultural activities are an important factor in most economies, and in the case of Iceland their contribution to GDP amounts to 4%, which is considerable in comparison with other industries.

Section 2 describes how the cultural sector in Iceland with quite many entrepreneurs fits in with the ideology of the creative industries, where creativity is a process that is engendered at the limits of three factors: culture, personal background and society. In the cultural sector creativity often occurs in clusters, where a number of entrepreneurs come together at the same time and changes occur.

In Section 3, Porter's five forces model is employed to describe the competitive position of enterprises and entrepreneurs in the music industry in Iceland as an example. This analysis is applied to the competitive position of Iceland in the music sector by the use of Porter's Diamond, whereby it is revealed that the small domestic market in Iceland can be exploited to achieve a competitive advantage owing to the extensive domestic awareness of the mainstreams of music in the world. The music schools play a key role in the strong position of music in Iceland, and the people employed in the sector are generally very well educated; this is offset, however, by a weak financial market.

In Section 4 there is a description of numerous ways within cultural policies to encourage the activities of entrepreneurs. Increased cultural activities as a part of the creative industries, especially by entrepreneurs, can be achieved by strengthening the school system in the field of culture, especially fine arts. There are also ways of using the tax system to encourage private initiative, both by granting general incentives to companies operating in the field of culture and also by focusing particularly on entrepreneurs and SMEs.

Section 5 contains conclusions and discussion.

**Keywords:**

Culture policy, creative industries, Icelandic music industry, Porter's models

## 1. Contribution of Cultural Activities in Iceland

Culture, defined as any human behavior or activity passed from one generation to the next, which describes, creates, preserves or transmits emotions or surroundings of human society, consisting of languages, beliefs, ideas, customs, arts, sports, or other related aspects, is the subject of cultural economics (Frey, 2000; Held *et al.*, 1999; Bendixen, 1998; Peacock, 1994). Goods are a material aspect of culture and make the categories of culture visible (Howes, 1996). Culture can be regarded as a public good, as in the case of cultural heritage. It is not possible to maintain, however, that every aspect of culture falls under the heading of pure public goods, because many aspects are in fact private goods, for instance concerts and art exhibitions in the case of fine arts. In such an event, this cultural activity or cultural element is excludable but not rival. In that case they are impure public goods (Serageldin, 1999).

Culture can be regarded as a positive externality, because increased cultural activities result in a more diverse society and offer more possibilities for a happier life (Sable and Kling 2000). Public initiatives in support of cultural activities for the purpose of increasing positive externalities are often very effective (Kaul *et al.*, 1999). Externalities are especially important in connection with public goods, which in contrast with private goods are non-excludable and non-rivalrous.

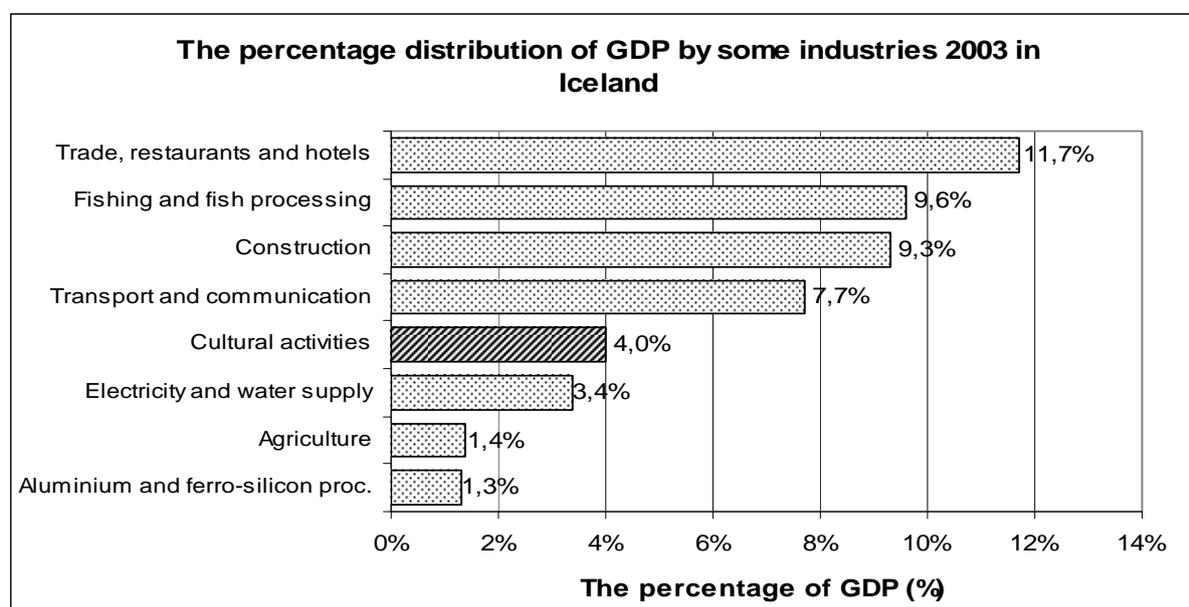
One of the problems of attaching a price tag to culture is that its value is not always immediately apparent, and the value may change from one generation to the next. There is also the problem of classification: the difference between culture and education. In economic statistics, the entire school system, including art schools and various institutions purely dedicated to the practice of culture, is classified under the heading of education rather than cultural activities. UNESCO has defined culture for the purpose of international economic statistics (Haydon, 2000), dividing the concept into nine categories: cultural heritage, printed matter and literature, music, performing arts, audio media, audiovisual media, social activities, sports/games and environment/nature.

Iceland, which is the example of the small society in this paper, is 103,000 square km in area, with a population of 290,000. Iceland is an independent country in the North Atlantic and the distance from the capital, Reykjavik, to the mainland of Europe is about 2,000 km. The country achieved independence from Denmark in 1944 and enjoys a very high standard of living. In 2003, Iceland's GDP in PPP in US \$ per head was 29,800, which put the country in the 8<sup>th</sup> place in the world in this category (*OECD in Figures*, 2004). Iceland is one of the Nordic countries and cooperates closely and extensively with the other Nordic countries, Denmark, Finland, Norway and Sweden. The contribution of cultural activities to GDP in Iceland's economy in 2000 is shown in table 1 (*Statistical Yearbook of Iceland*, 2003). The classification is very close to that of UNESCO.

**Table 1. Percentage of the contribution of cultural activities to GDP in Iceland 2000**

	<b>2000</b>
Printing and publishing	1.36%
Artists, theatre and orchestras	0.74%
Radio and television	0.48%
Sports	0.38%
Religious affairs	0.38%
Library and museums	0,27%
Motion pictures	0.14%
<b>Total</b>	<b>3.75%</b>

The percentage of cultural activities to GDP was 3.75% in the year 2000. Printing and publishing has the biggest share, followed by theatre, orchestras and other activities of artists. The creation of artistic works constitutes primary production, but their contribution increases many times through exhibitions, printing etc. over a period of many years, decades or even centuries after their original production. The number of books published in the Nordic countries per 1.000 inhabitants is by far the highest in Iceland, at more than double, and theatre visits and museums visits per capita are highest in Iceland. The Internet is an important medium for distribution of culture. The Internet access in the home in Iceland is the highest of all EU and EFTA countries in 2001 (*Media and Culture*, 2003). Figure 1 shows the contribution to GDP of several important industries in Iceland in 2003 (*Statistical Yearbook of Iceland*, 2003).

**Figure. 1. The percentage distribution of GDP by some industries 2003 in Iceland**

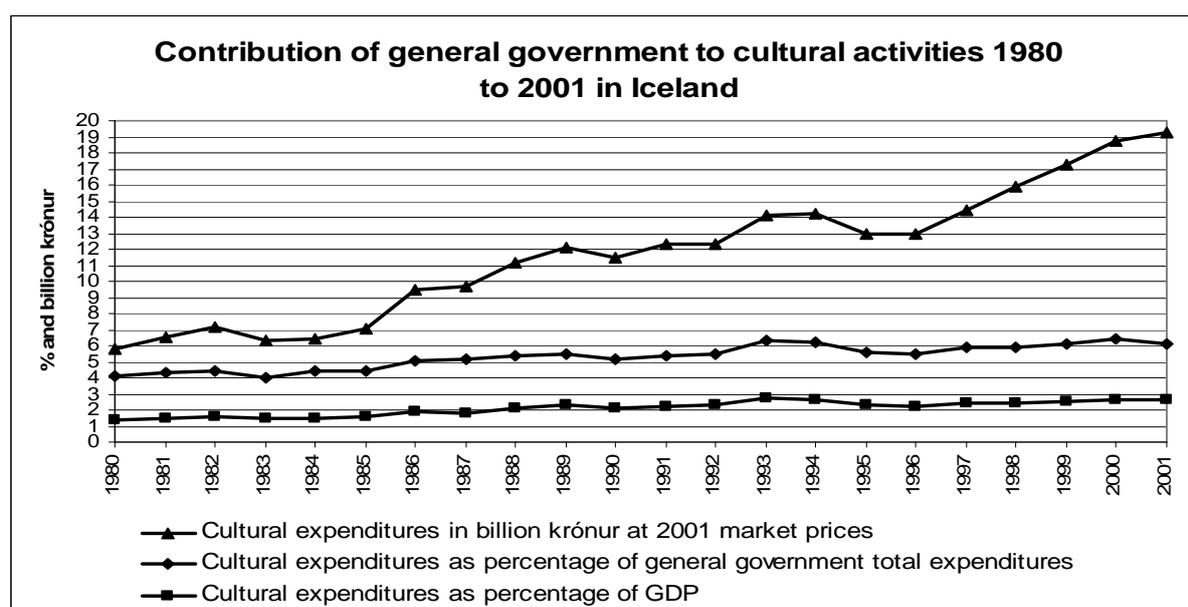
The contribution of cultural activities to GDP is higher than one might expect. Culture contributes more to GDP (4%) than agriculture (1.4%) and electricity and water supply (3.4%). The eight industries shown in Figure 1 contribute 48.4% to GDP in Iceland.

Most of enterprises involved in cultural activities in Iceland are SMEs or micro-enterprises. Of cultural enterprises in Iceland, 79% have 1-5 employees, 16% have 5-20 employees and 5% have more than 20 employees. In fact, most enterprises in Iceland are small or medium sized. Enterprises with fewer than 20 employees are defined as SMEs in Iceland. The business activities of artists are frequently conducted in very small units or organizations. Some large companies, but quite many small enterprises, characterise the printing and publishing sector, as well as radio and television. The cultural sector attracts entrepreneurs, and new enterprises in culture are very common in Iceland. If we take a closer look at enterprises in Iceland and divide them, on the one hand, into enterprises with 5–20 employees and, on the other hand, enterprises with 20 employees or more, this places 77% of all companies in the cultural sector in the category of SMEs (*Statistical Yearbook of Iceland, 2002*). Table 2 shows a comparison with other sectors.

**Table 2. Division of enterprises in several sectors into SMEs and larger enterprises**

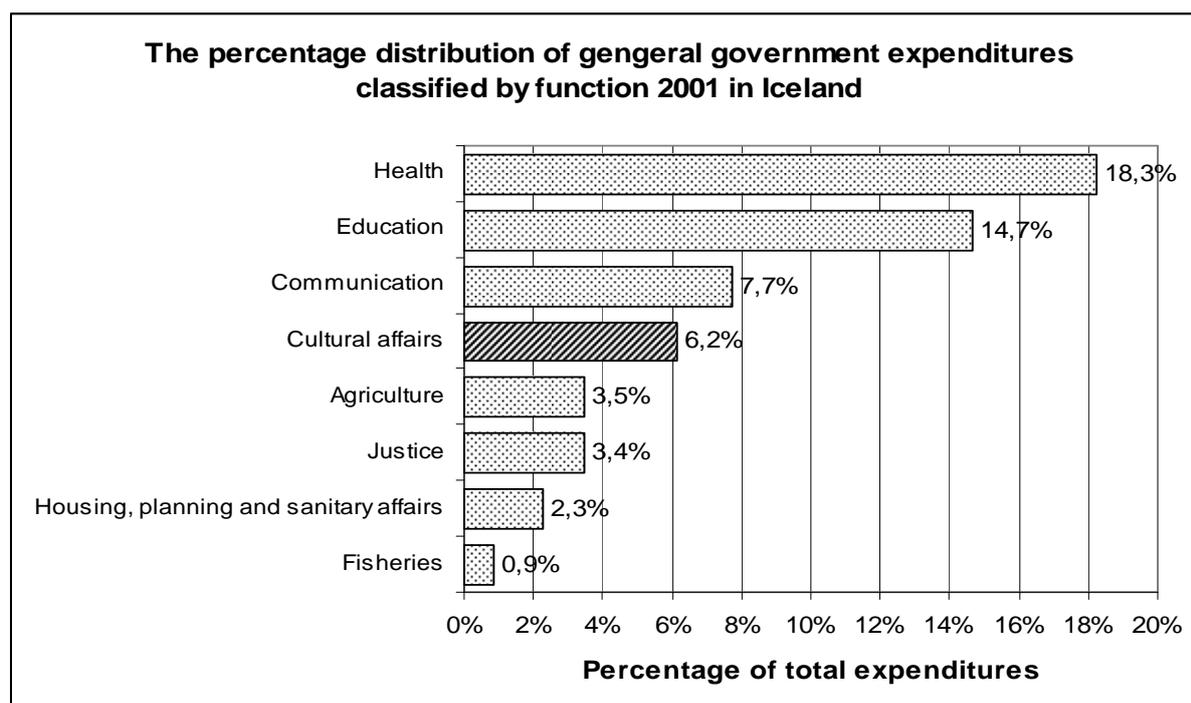
Industries	5-20 employees	Over 20 employees
Construction	81%	19%
<b>Cultural activities</b>	<b>77%</b>	<b>23%</b>
Transport and communication	70%	30%
Fishing	75%	25%
Fish processing	53%	47%

Table 2 shows that SMEs are most common in the construction sector, where there is an Icelandic tradition of small units, of which there are many. The second largest group of SMEs is in the cultural sector, reflecting the characteristic of cultural activities of being conducted in small units. In fish processing, which is an important sector in Iceland, there is a proportionally smaller number of SMEs than within the cultural sector. Figure 2 shows the expenditures of the general government, i.e. central government and local government, to culture in Iceland from 1980 to 2001 at 2001 market prices, and the share of these expenditures in total expenditures and in GDP (*Public Finances 1997-1998, 1999; Statistical Yearbook of Iceland, 2003*).



**Figure 2. Contribution of general government to cultural activities 1980-2001 in Iceland**

Figure 2 shows that general government expenditures on culture have increased greatly from 1980 to 2001. Expenditures increased from 6 billion krónur to 19 billion krónur at 2001 market prices. The percentage of total expenditures to cultural activities rose from 4.1% in 1980 to 6.2% in 2001. The share of GDP increased from 1.4% in 1980 to 2.6% in 2001. The expenditures of local government are higher than the expenditures of central government in the most years. Figure 3 shows the expenditures of the general government in Iceland, 2001, classified by sector (*Statistical Yearbook of Iceland, 2004*).



**Figure 3: The percentage distribution of general government expenditures classified by function 2001 in Iceland**

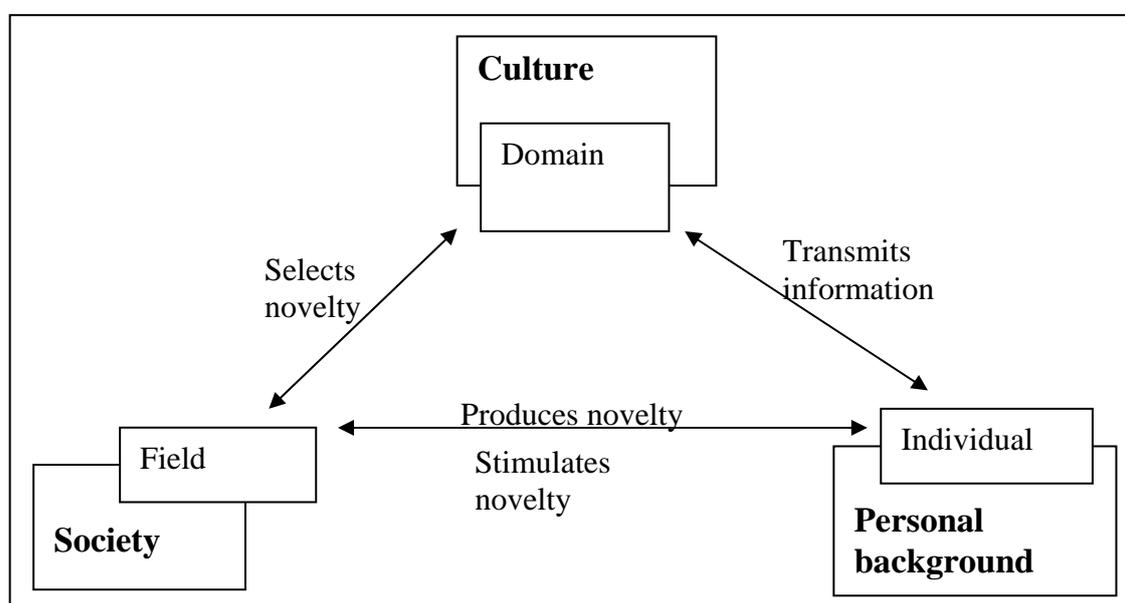
The sectors shown in Figure 3 represent 57% of total general government expenditures in Iceland in 2001. Public cultural spending is one third of health expenditures, almost half of the expenditures on education.

## 2. Creative Industries

The importance of entrepreneurs is significant in the cultural sector, particularly in the creative industries. Entrepreneurs work in the environment of culture, community and individuals, where the economic value of their initiative manifests itself as a change in traditional perspectives. Creativity has a certain meaning for a group of individuals; as a result, community recognition is a requirement for any work to be regarded as creative. SMEs and entrepreneurs enjoy a strong position in the cultural sector and economies of scale are not as prominent as in other industrial sectors. It is therefore important for governments to stimulate still further the activities of SMEs and entrepreneurs within the cultural sector.

The cultural sector is a creative industry, and creation is a positive aspect of the economy. Research into creative activities was first conducted principally within the social sciences and psychology, which centered on the creative individuals themselves or their creative work. Now, however, growing attention is being focused on the environment of creative work and the creative industries. Creative individuals can be studied on the basis of factors such as childhood background, life experience or character. Account can also be taken of the outward environment of creative individuals, which is of great significance, since the outward environment is the principal factor that outside players, such as administrators and politicians, are able to influence.

Creation normally refers to innovation. This is therefore not a definition which relates only to artistic creation, but a much wider concept. Three principal factors can be linked together in this context, i.e. culture, personal background and society, and represented graphically, where creation is shown as a process which is engendered at the borders of the three principal factors, as shown in Figure 4 (Csikszentimihalyi, 1997).



**Figure 4: The systems view of creativity (Csikszentimihalyi's Model)**

Figure 4 shows that culture is divided into several segments, i.e. domains, and information is transferred to and from individuals. In this context background is extremely important, e.g. musical education. Society is also divided into various fields, where the creative work of individuals, i.e. the creation of novelty, flows back and forth.

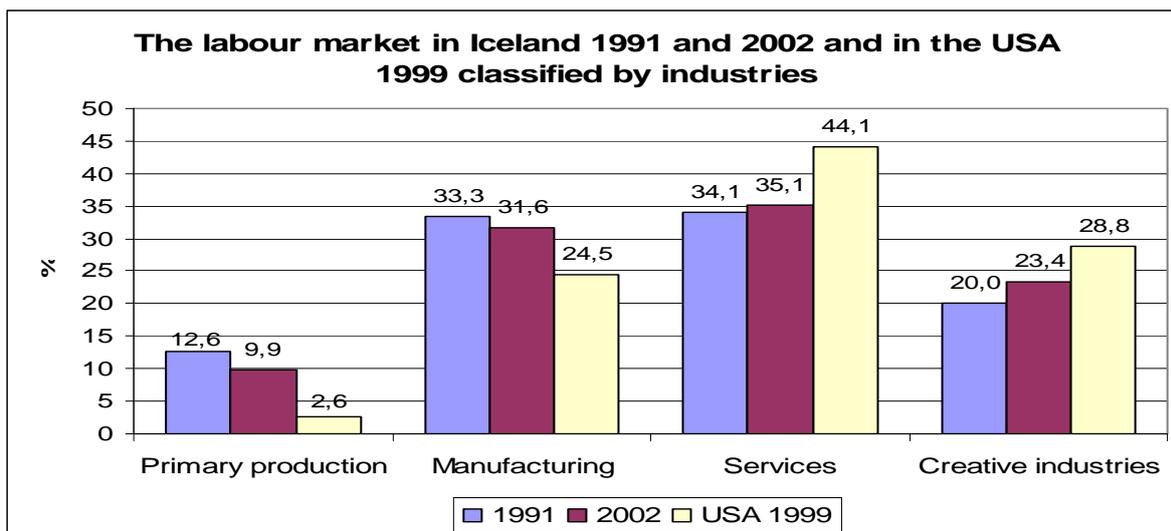
Culture should be understood as a delimited economic factor. However, culture is so variegated that it is difficult to discuss it as a single concept. Creation and entrepreneurship can be regarded as an activity within a certain framework of culture. If the innovation and the creation must be recognized as such by society, it follows that an audience is required, as is most frequently the case in cultural activities. Every society is composed of many smaller groups, and creation often stretches over a long period of time, even many years. The assumption is that it is the individual who will take the principal initiative, and not the group. However, this can be viewed from different perspectives within the cultural sector, which are also relevant to other aspects of creation, such as scientific work, where many individuals come together to work on the same idea. The approach of analyzing on the basis of three principal factors, as described in Figure 4, involves the interaction of individuals, which

shapes a framework that encourages creation and the activities of entrepreneurs, which in turn has a positive economic impact.

An important aspect of any discussion of creation is the realization that creation often takes place in clusters, where a number of individuals come together and a transformation occurs. It is important in all creative activity for individuals to have access to a fertile environment, e.g. with others working in similar activities in the close vicinity, as is commonly the case when people are working on scientific research in a university. A group is also needed, individuals or organizations, to participate, and the group needs to be strong enough for ideas to be encouraged and supported and carried out; in such cases differences in circumstances make a great deal of difference. Creation requires an audience to have any significance. It is not enough for the creation to take place only for the individual in question, except as a part of his or her development.

In the United States, where studies in this field are most advanced, the studies are conducted on the basis of sectors or professions. In the discussion of creative industries there are two different viewpoints. On the one hand, there is the approach of looking at the creative industries that produce goods and services which have a cultural and artistic value or a recreational value. Here, it is the goods and services produced that are at the center of gravity. From this point of view, sectors such as the film sector, music sector and publishing sector belong to the creative industries (Caves, 2000).

On the other hand, one can look at the individuals in separate sectors and classify their work into the four following categories: primary production, manufacturing, services and creative industries (Florida, 2002; Florida, 2005). The discussion of the creative industries in this paper uses this method. The industries that constitute creative industries are science, education, arts, design, journalism, sports, computer sciences, engineering, technology, architecture and management. Management is regarded as a part of the creative industries, as well as high technology, as it is a field where new ideas are shaped. Among other things, a creative industry involves the dissemination of knowledge, where all kinds of contact networks are formed, and it also concerns entertainment. Here, an assessment is made of how many of these jobs fall within the definition of the creative industries as they are defined above. Figures over a longer period in Iceland are compared, with reference to the figures for the United States. Figure 5 shows the division of jobs in Iceland by primary production, manufacturing, services and creative industries in the years 1990 and 2002, and a comparison with the United States in 1999 (Einarsson, 2004; Florida, 2002).

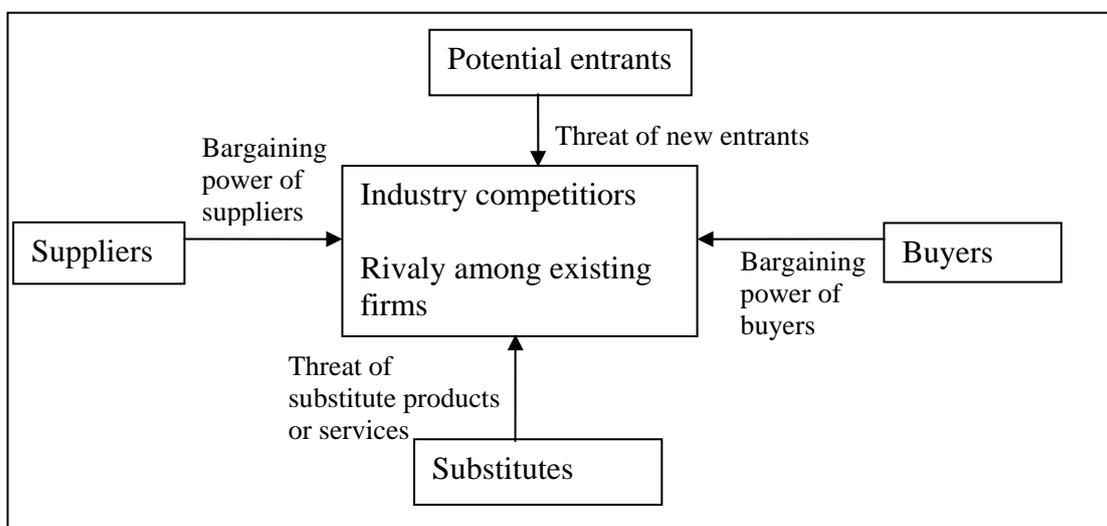


**Figure 5: The labour market in Iceland 1991 and 2002 and in the USA 1999 classified by industries**

Figure 5 shows that primary production in Iceland fell from approximately 13% in 1990 to just under 10% in 2002. Manufacturing went from a 33% share to 32% in these 12 years and services from 34% to 35%. The creative industries went from a 20% share in 1990 to 23% in 2002. The corresponding share for the United States in 1999 was 29%. The creative industries in Iceland account for slightly less than a quarter of the total jobs and their share is growing. This approach to the analysis of the labor market gives a good reflection of the division of labor in modern societies and illustrates the substantial changes that have occurred in the economies of individual countries in recent years, where entrepreneurs are playing a big role.

### 3. The Models of Porter in Describing the Music Sector

The competitive position of enterprises in the music industry can be shown using Porter's five-force model (Porter, 1980). Figure 6 illustrates this methodology.



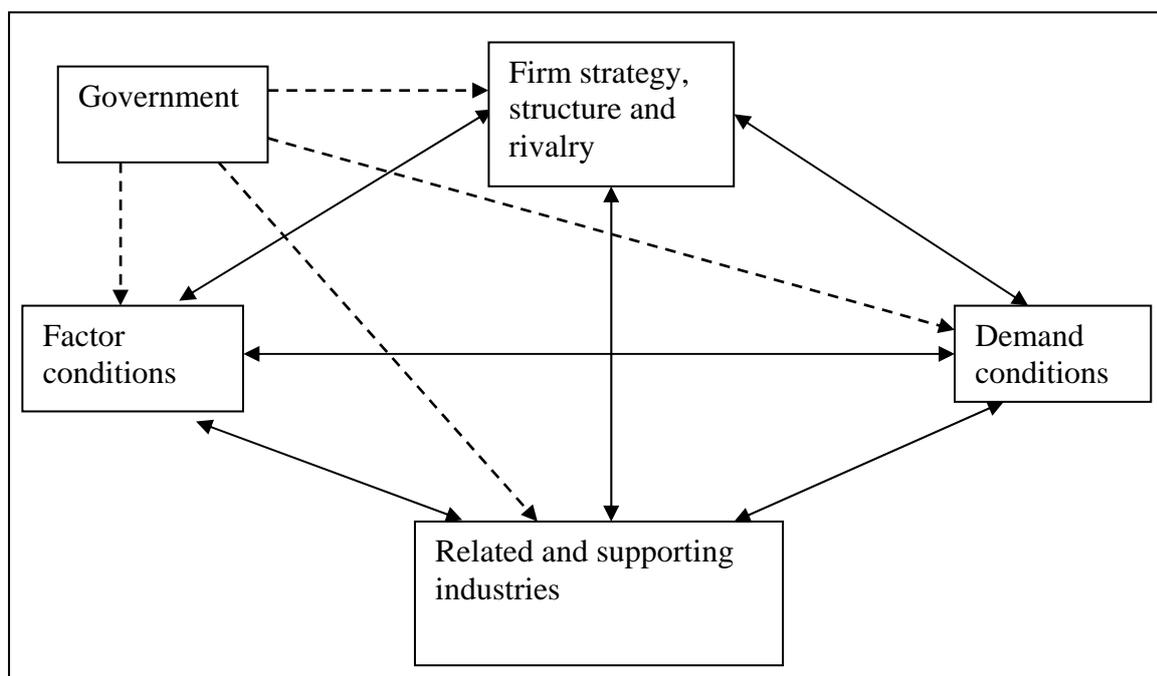
**Figure 6: Porter's five competitive forces**

The music industry is so diverse that a distinction needs to be made between individual enterprises and organizations for this approach to be useful. Nevertheless, there are many common features, such as the buyers. Most of the activities within the music industry focus on individuals as buyers, as shown to the right in Figure 6. The position of consumers is strong, as music is in competition with various other entertainments. The same applies to localized products and services, many of which are connected with music, e.g. other branches of art and various types of entertainment; these are shown at the bottom of the illustration.

Suppliers in the music industry, shown to the left in Figure 6, are of various kinds, e.g. musicians to publishers, music teachers to music schools and producers to the media. The competitive position of suppliers is usually not particularly strong in the music industry, as there are numerous competitors working in the same field. The key factor lies in the middle of the model, which shows the extent of the competition between enterprises within the industry. Competition between enterprises is usually extensive in most fields of the music industry.

The top of the illustration shows the possible new stakeholders in the music market. Barriers to entry are usually weak. This does not apply, however, to the parts of the market that require substantial capital investment, such as opera houses and concert halls. Analysis using this model to uncover competitive advantages can result in the conclusion that building upon a weak foundation in some area can later, by decisive measures, prove to hold potentials for competitive advantage.

This idea can be transposed to the competitiveness of nations (Porter, 1009). This model examines the so-called Porter's diamond, which is here applied to the Icelandic music industry and shown in Figure 7.



**Figure 7. The Diamond Model of Porter**

The production factors, shown on the left in Figure 7, are labor, natural resources, capital, knowledge, human resources, organization, technology and institutions. For the music

industry, qualified employees and capital are of the greatest importance. Unskilled labor, for instance, is not common in the music industry.

Demand, which is shown on the right in Figure 7, is somewhat special in the Icelandic music industry, as the domestic market is small. From a small, but professional domestic market, however, advances can be made into foreign markets, and there are several examples of this in Iceland. There are already numerous Icelandic musicians who have made a name for themselves outside Iceland.

Related industries and supporting industries, shown at the bottom of Figure 4, include music teaching and the media. Music teaching in Iceland is quite a strong sector in Iceland, but reinforcing it would undoubtedly strengthen the music industry still further. As regards strategy structure and rivalry, shown at the top of the figure, it is apparent that the financial market is weak in the music industry and it is difficult to obtain financing for new ideas, e.g. through the stock market. It is also of relevance here that jobs in the music industry are not very easily identifiable or respected in the labor market and are widely regarded as low-income jobs, which is accurate to a considerable extent. Competition in the music industries can help others and promote increased efficiency and greater creative energy within the industry. The principal advantages in the environment of the music industries are well educated employees, but the principal weakness is the small domestic market, which nevertheless can be used as a platform for cross-border expansion, since, as it happens, the people in the domestic market are quite enlightened and demanding.

Government, shown at the top left of Figure 4, can do a great deal to promote the competitiveness of the country in the music sector, e.g. through increased financial support, improved infrastructure or institutions, including facilities, tax incentives for the creative industries, strengthening the school systems, recognizing the economic significance of the music industry and promoting interest. The links with government are shown by a dotted line in the illustration, which means that the government can impact individual factors of the model directly. It is important in this context to employ the arm's length principle, i.e. the attitude to art and culture that politicians should only engage in providing the capital, but not utilizing it.

Music has a significant impact on exports from Iceland, particularly by indirect means, e.g. through the tourist industry. A number of tourists come to Iceland as a result of the influence of famous performers, such as Björk and Sigur Rós. Currency revenues from foreign tourists have increased substantially in recent years, partly as a result of cultural activities, including musical activities, as reflected, for instance, in the numerous music festivals held in Iceland.

Studies that have been conducted of the Nordic music industry show that the industry is in a stage of rapid growth, both as regards employees and turnover (*Behind the Music*, 2003). A growing part of the creation of value in the music industry is a result of related industries, such as the production of music videos, software, distribution of digital material, etc. Normally, there is a clear division in the industry between independent recording companies and the major players, who also possess their own separate brand names. Also, the division between individual aspects is unclear, e.g. between record companies, publishers, management and promotion. All of these factors are mixed together within single enterprises. The music markets in the Nordic countries are relatively small. This has the effect that their opportunities for expansion depend on exports. Some of the Nordic countries have been successful in this respect. Sweden, for example, is the third largest exporter of music in the world (*Denmark's Creative Potential*, 2001). It therefore appears to be a practical economic measure to set up some sort of support system to encourage musical tours and concerts abroad.

The number of music schools has grown by a factor of almost six over the last four decades. The number of students attending music schools has grown by a factor of almost eleven over the last four decades. The organization of music schools in Iceland, with its mixture of private and public enterprises, is excellent in comparison with many other countries. The key to this success is the good division of responsibility between the public and private sectors.

#### 4. Policies and Programs to Support Entrepreneurs and SMEs in the Cultural Sector

Activities designed to increase the share of cultural activities within an economy lead to economic growth and higher living standards. Increased cultural activities, especially by SMEs and entrepreneurs, can be achieved by strengthening the school system in the field of culture, especially fine arts. This has a twofold effect. First, it increases the knowledge of culture among the population and, second, it expands the interest of young people who will later participate actively as professionals in cultural activities. The school system is often used as a means of securing equality as regards the art and artistic work of young people with different economic backgrounds.

In some countries, public authorities have supported programs either by direct subsidies or through the tax system, e.g. by granting tax discounts to enterprises which support cultural activities (Schuster 1999; Einarsson, 2001). As an example, an enterprise spending USD 1,000 on the purchase of a work of art could be permitted to deduct double that amount from its tax base, in this case USD 2,000. In Table 3 this example is illustrated further using a company with earnings of USD 10,000 before taxes and cultural expenditures and an income tax rate of 30%.

**Table 3: Example of special income tax reductions for cultural expenditures in USD**

	No tax reduction		With tax reduction
Earnings before taxes and cultural expenditures	10,000	10,000	10,000
Cultural expenditures	0	1,000	1,000 (2,000)
	-----	-----	-----
Earnings before taxes	10,000	9,000	9,000 (8,000)
Taxes	3,000	2,700	2,400
	-----	-----	-----
Earnings after taxes	7,000	6,300	6,600

By implementing an income tax reduction of this kind, a company which spends USD 1,000 on cultural activities is only reducing its earnings after taxes by USD 400, i.e. earnings of USD 6,600 instead of USD 7,000. An arrangement of this kind would obviously increase the interest of enterprises in promoting cultural activities, as part of the contribution would be covered by lower income tax payments. Another way to utilise the tax system might be to impose lower taxes on SMEs, e.g. payroll taxes, especially in their first years of operation.

Although fine arts are only one element of culture, they feature prominently in the public debate. Financial income from artistic activities within fine arts is derived from direct public subsidies or from sales in the free market. This dichotomy in the market has resulted in a trend away from public support systems for artists and in the direction of specific support for certain classes of fine arts through the introduction of competition between artists and increased participation in buying works of art by public authorities, e.g. through indirect

stipends. An example of this is the 43% public share of the Dutch fine arts market (Rengers and Plug, 2001).

The latest development in Europe is the support for fine arts characterized, *inter alia*, by indirect support in the form of changes in tax regulations, technical support and payments for copyrights, which have to some extent replaced direct support, which was common in the seventies and eighties. Subsidies are now based to a greater extent on quality rather than on social considerations or membership of professional artists' associations. Special support plans for fine arts based on new technology have also increased, and public support in some countries is more closely connected with regional and social policies than before (*Cultural Policies in Europe*, 2005; *World Culture Report 2000*, 2002; Storm, 2003).

Yet another way to increase the scope of activities within culture is to seek to implement a new organisation within and outside public administration. To achieve this objective, it has often produced good results, e.g. in the Nordic countries and in France, to place culture under a separate government ministry. The tasks of such a ministry could include the administration of programs and supports for entrepreneurs and SMEs in the field of culture, e.g. by promoting increased research and by providing expert advice and funds for entrepreneurs. Setting up a ministry of culture would show the political priority of culture as a political issue; in many countries, cultural affairs are housed in ministries of education.

Yet another option is to focus specifically on the marketing of domestic culture across borders by a concerted effort of domestic institutions, associations and enterprises. This has been done with good results in the motion picture industry in Ireland, which has benefited from a system of public support. The motion picture industry is an example of a field of culture and entrepreneurship which features abundant opportunities and which has an indirect impact on the economy of the countries involved. Thus, a study of the motion picture industry in Iceland (*The Movie Sector in Iceland*, 1998) revealed that many tourists decided on a trip to Iceland after seeing a motion picture or other coverage in television broadcasts or movie theatres. These tourists spent cash in the country resulting in payments of VAT which were substantially in excess of the total public expenditures on the production of motion pictures. It was therefore an especially profitable investment on the part of the government to support motion picture production. Entrepreneurs are extremely important in this context, a good example being the Icelandic company Smekkleysa, which first marketed the world famous singer Björk outside Iceland. Support to such enterprises can result in a rapid recovery of expenditures.

## 5. Conclusions and discussion

Cultural activities are an important factor in the Icelandic economy. Their economic impact is often underestimated in economic statistics. The influence of culture in increasing the well-being of people is often not measured, perhaps not even measurable, in monetary terms, but is nevertheless of great effect. The value of a society is to a large extent underpinned by the depth of its cultural roots. Public authorities can successfully support cultural activities on the basis of their positive externalities and their economic impact.

Activities designed to increase the share of cultural activities within an economy lead to economic growth and higher living standards. The contribution of cultural activities to GDP is about 4% in Iceland, which is considerable in comparison with other industries. There are numerous enterprises within the cultural sector, most of them small and medium sized enterprises or micro-enterprises. Entrepreneurship is very important within the cultural sector.

Public expenditures on cultural activities have increased substantially in Iceland, both in nominal terms and as a share of GDP. Local government spends more than central government on cultural activities, and public expenditures cultural affairs are very high compared to other functions. Globalization offers new opportunities for cultural activities.

There are several ways of strengthening the role of SMEs and entrepreneurs within the cultural sector. Increased cultural activities by entrepreneurs can be achieved by strengthening the school system in the field of culture, especially fine arts. In some countries, public authorities have supported programs either by direct subsidies or through the tax system, e.g. by allowing tax reductions to enterprises which support cultural activities. Reforming the structure of public support, e.g. by the establishment of a ministry of culture, export driven funds and advice for entrepreneurs are examples of policies and programmes which can be implemented successfully. The creative industries are extensive in Iceland, and cultural activities form a part of these industries. Creative industries in Iceland account for approximately 23% of all jobs, up from 20% ten years ago and entrepreneurs are an important part of these creative industries.

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