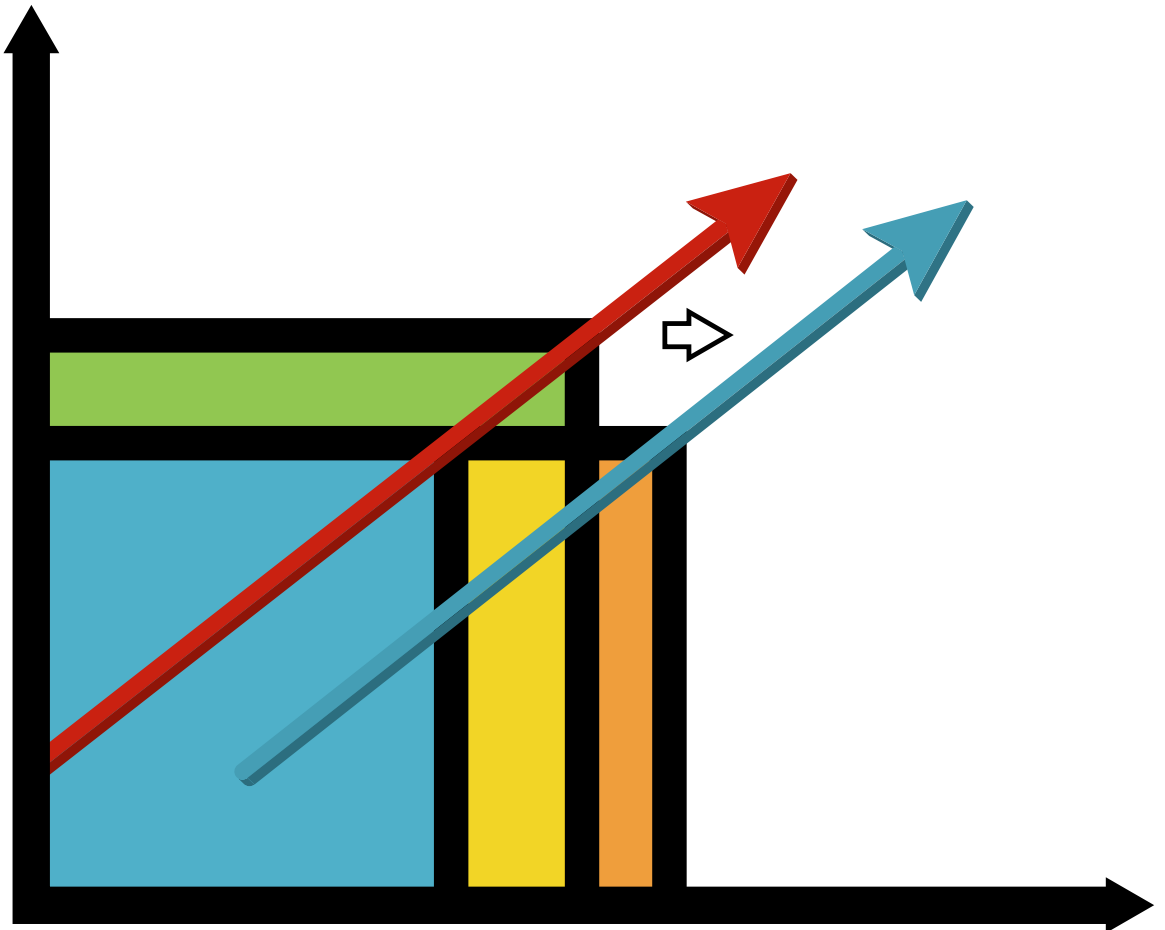


Ágúst Einarsson

# CULTURAL ECONOMICS



# Cultural Economics



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# **Cultural Economics**



**BIFRÖST UNIVERSITY**  
HÁSKÓLINN Á BIFRÖST

2016

**Cultural Economics**

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*To Kolbrún Ingólfssdóttir*



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# Preface

Culture is not only one of the most important elements of any society because of its intrinsic, aesthetic, unifying or other intangible values but it also generates a great deal of economic activity. This activity is among the subjects of study in cultural economics, and this book discusses the basics of cultural economics with the purpose of enhancing readers' understanding of the subject. The book should give readers not only a practical knowledge of the fundamentals of cultural economics, but also an understanding of the main principles that apply in economics in general, which are explained here in the context of their significance for culture and cultural activity.

The book is suitable for students of cultural management and cultural studies and for students of art, economics and business who are interested in obtaining an insight into this branch of economics. In addition, the book should be of interest to people in managerial positions at cultural institutions and in businesses operating in the cultural sector and to those interested in culture who work in the business sector, non-governmental organisations, public administration and politics.

In writing this book I have drawn to some extent on the text and content of some of my recent books, especially *Menningarhagfræði* ('Cultural Economics') (2012), of which this book is a partial translation and adaptation, and the *Economic Impact of the Motion Picture Industry: the Icelandic Model* (2014).

The general structure of the book is that the opening chapter discusses the definitions of culture, the origins of cultural economics, the concept of value – a fundamental concept in economics – creativity and the creative industries. The chapter also provides an account of the special position of culture in economics, some of the fundamental features of economics and opportunity cost. Finally, the chapter discusses the international classification of economic indicators relating to culture.

The second chapter deals with supply and demand in culture and explains the concepts of demand function, price elasticity, consumption and consumer behaviour. It also describes the working environment of business enterprises and factors of production, as well as the categorisation of production, cost and the general features of the cultural industries.

The third chapter discusses the role of government and cultural policy. It describes the forms of government support for culture and suggests reasons why such support is both necessary and beneficial. It also discusses the objectives and formulation of cultural policy and means of promoting cultural activities. The concept of cultural heritage is also discussed, as well as international public goods and creative areas or creative cities, in addition to the links between culture and development and international development assistance.

The fourth chapter deals with international trade and market matters, globalisation, market forms and market models. The chapter also describes the principal features of marketing and the useful life and income share of goods and models to analyse the market position of business firms.

The fifth and penultimate chapter deals with financial matters and management in the cultural industries and explains funding needs, financing and investment. The chapter also explains corporate structure, strategic planning and planning methods and the principal management methods.

Finally, the sixth and last chapter summarises the contents of the book and looks to the future. Sources and suggestions for further reading are cited in footnotes. At the back of the book is a register of all the illustrations and tables in the book, an index of names, an index of terms and a list of references.

Interspersed throughout the book are brief biographies of individuals who have been influential in culture and cultural economics. The selection of such individuals for inclusion is inevitably subjective, but I have tried to exercise some variety in my choices, including variety of time. However, figures of religious importance are not included, notwithstanding their undoubted influence on culture. The biographies are intended to break up the text of the book with bits of information about remarkable individuals with links to culture and/or economics, particularly from a historical viewpoint.

A number of individuals have assisted me in this work, and I would like to thank Axel Hall, Árni Pétursson, Fredrik Heinemann, Jón Trausti Harðarson, Njörður Sigurjónsson and Sólveig Einarsdóttir for their advice and help, and especially Jón Skaptason. My wife, Kolbrún Sigurbjörg Ingólfssdóttir, has as always, been my best advisor in writing works of this kind, and I would like to thank her especially and dedicate this work to her and our marriage of almost 45 years. Nevertheless, any deficiencies in this book are my own responsibility.

Reykjavík, January 2016

Ágúst Einarsson



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# 1. Introduction

‘Culture’ is an extremely broad concept with countless possible definitions. The anthropological definition, for instance, is that everything done by human beings falls under the classification of culture. The word ‘culture’, used in various forms in many languages, including English, German (*Kultur*) and Danish (*kultur*), is rooted in the Latin word *cultura*, meaning cultivation. The original meaning is cultivation of soil in agriculture, but the word eventually came to be used to denote activities undertaken by individuals in the context of their communities involving progress and the development of ideas and the framework of human society.

A concise definition of culture is, therefore, if not impossible at least difficult, but for the purposes of this book culture is understood as virtually all human conduct that is passed on from one generation to the next. Culture is not the prerogative of a single generation, but is embodied in, and shaped and adapted by, a succession of generations. Culture creates, describes, preserves and disseminates the thoughts, emotions and general fabric of human society through the production of cultural goods and services as varied as ideas, sports, arts, languages, religions and traditions. The concept of culture also includes not only the goods and services produced, but also all the work involved in the promotion and dissemination of those goods and services.

This book focuses in particular on cultural goods and services from an economic standpoint: that is, their creation and production, various factors that are common to the economics of culture and other factors that are unique to culture. Special attention is given to the participation of government in matters related to culture, for enormous resources are allocated by governments to cultural matters in addition to the resources contributed by businesses and private individuals.

Cultural products, or cultural goods and services, are manifestations of culture, but culture can also take the form of events, such as films screened, plays staged, ballets danced and concerts performed. Culture can also be viewed from the point of view of certain characteristics, in that that culture entails some sort of creation or transformation of the human environment. Culture also manifests itself in communication using signs or symbols, whether in language, music or other forms of expression. Moral and ethical criteria may be established as minimum requirements for an activity to be regarded as culture. Those requirements may relate to democratic principles, protection of minority rights and peaceful relations. The formation of such criteria in public discourse sets a certain framework for culture that relates to intellectual and artistic human behaviour, although its sources can differ from the behaviour that characterises the community as a whole. Because of its state of constant flux, culture is a dynamic process, changing continually in the course of time.

## 1.1 Origins of cultural economics

Humans have always engaged in culture, and in scientific studies the subject of culture has primarily been the domain of the liberal arts. However, discussion of culture in the social sciences, including economics, has increased in recent decades.<sup>1</sup> Through the ages numerous economists have involved themselves in artistic and cultural subjects. Adam Smith, known as the father of economics, wrote articles about music, dance and poetry, and John Maynard Keynes, one of the most prominent economists of the twentieth century, was a member of the literary group known as the Bloomsbury Group and a patron of the arts. Various other economists have also been artists concurrently with their work in their academic field. However, it is only in recent times that attention has been focused on the economic principles that govern the cultural sector of the economy.

Cultural economics, as a distinct area of study, came into existence in the 1960s. Seminal works on the subject include books by John Kenneth Galbraith and Lionel Robbins, which, among other things, discuss the role of government in subsidising the cost of museums.<sup>2</sup> In works by

<sup>1</sup> For a discussion of culture in the social sciences see, e.g., the writings of Crane (1994), Frey (2000), Heilbrun and Grey (2001), Edgar and Sedgwick (2002), Wasko (2005) and Throsby (2010).

<sup>2</sup> See Galbraith (1960) and Robbins (1963), and for a discussion of the history of cultural economics see, e.g., Towse (2003), Ginsburgh and Throsby (2008), McCain (2008) and De Jong (2009).

Baumol and Bowen the tools of economics were first applied systematically to the arts. Among other things, they suggested that the influence of technological progress might be weaker in the arts and that for this reason costs would fall less over time in this area than in other sectors and productivity would, therefore, increase less in the arts than elsewhere. For example, the performance of a piece by Mozart takes just about the same amount of time now as it did on the day it was composed, and the text of a play by Shakespeare, despite improvements in the last hundred years in achieving textual accuracy with sixteenth and seventeenth versions, will not be essentially altered for most viewers and readers of the plays: ‘To be or not to be’ will remain ‘To be or not to be’. And a quartet will always require four performers! Generalisations on this matter are inadvisable, but there is a large body of scholarly writings on this subject.<sup>3</sup>

The consumer’s valuation of culture is more complex and more subjective than the economist’s valuation. In culture, value is reflected, among other things, in the impression made on an individual. It is the work itself, and possibly people’s experience of the work, that creates value in their minds. The aesthetic value of works of art has always been a matter of dispute and discussion in a number of scientific and academic disciplines. Beauty is dependent on taste, and beauty is not the only source of value in aesthetics. Beauty can be said to manifest itself in three ways in a work of art: in the work itself, in the opinion of experts and in endurance over time. The opinions of experts, however, are rarely unanimous, or even similar or compatible. Nevertheless, well-known works of art are nearly always the work of artists who were known in their day, although there are, of course, exceptions, a famous case being the Dutch painter Vincent van Gogh, who is said to have sold only a single painting in his lifetime. Time is perhaps the best filter for art and often a good judge. However, time as such does not in itself bring about changes in the assessment of art; what does change is the institutions of society and their social environment, including popular taste.<sup>4</sup>

Numerous viewpoints could be expressed regarding the way in which people employ their leisure time. It should be borne in mind that leisure time – a prerequisite for the existence of the recreation and experience

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<sup>3</sup> See Baumol and Bowen (1966), and a fine discussion of Baumol and Bowen’s problems in Cowen (1996), Heilbrun (2003) and Ginsburgh and Throsby (2008).

<sup>4</sup> Examples of writings on aesthetics include Eco (2004), Hutter and Schusterman (2008) and Ginsburgh and Weyers (2008); these writings also cite a number of other insightful sources.



industries – is something that the general public did not possess in any abundance until the last two or three hundred years. In earlier ages normal people devoted most of their time to the task of making a living, and for the vast majority of people there was little time left over for any kind of recreation and relaxation, although the common notion that life in the past was all work and no play is probably a fallacy.

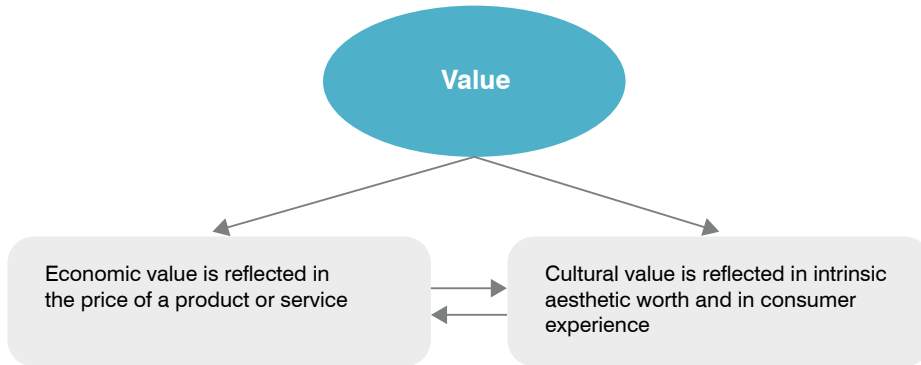
In any case, art has always accompanied humankind as an important aspect of culture. Much of what is now considered to be art was formerly a part of daily life and worship and a part of the basic culture of any community. Attitudes to art underwent profound changes in the eighteenth century in tandem with other transitions, such as the growth of the bourgeoisie, urbanisation, the industrial revolution and scientific progress. Other factors, such as the quest for profit, also had an effect and are useful for economic analysis.

**Aristotle** was born in 384 B.C. and died in 322 B.C. He was a student of the Greek philosopher Plato for a number of years, who in turn had been a student of Socrates. Aristotle was much more than a philosopher; he was an all-round scientist who analysed all manner of questions on nature, metaphysics, the human condition and life in general. He had a profound impact on culture and history down to the Renaissance in Europe in the fourteenth century. Some of Aristotle's works have survived, but most of them are lost and their existence can only be deduced through their impact on other scientists and thinkers. Aristotle was Alexander the Great's teacher and a pioneer in the field of logic, where he has had an impact lasting well into the modern age; his works are still required reading in a number of disciplines, including literature and the arts. Few people, if any, have had such a deep and pervasive influence on Western culture as Aristotle. Thomas Aquinas, one of the best known scholars of the Middle Ages, referred to Aristotle simply as 'the Philosopher'.

Cultural goods often consist in some form of narrative. A well-told story has always been an important aspect of human society and is much older even than writing, a fairly late development in human history. It makes no difference whether the narrative takes the form of spoken or written words, music, film, dance or painting; all these art forms have captured the imagination for a long time and some of them from time immemorial. But cultural goods and products are extremely diverse. Gambling, for instance, can be classified as recreation and experience and thereby as culture. Gambling is a legal form of recreation in many countries and casinos are in some cases even run by the government. Underlying all of this is production and industry, whether we call it the culture industry or the experience industry, and this industry involves extensive economic activity. The experience industry, often said to be the largest of all the industries, meets consumer demand for entertainment, recreation and experience.

## 1.2 Value in cultural economics

In order to assess price or value in culture, we need to base our judgment both on economic, or monetary, value and on cultural value, see Figure 1.1.



**Figure 1.1:** The concept of value in cultural economics

It is impossible to evaluate cultural goods or products exclusively on the basis of the traditional methods of economics, but looking at the concept of value from two viewpoints, the economic and the cultural, gives us a good framework for assessing the economic aspects of culture. The concept of value, a key concept in both economics and culture, forms a sort of bridge between them.<sup>5</sup>

In economics the value of goods and services is reflected in price, which in turn reflects the utility that individuals subjectively derive from the goods or services in question. Price determines the extent of distribution of goods in the marketplace and constitutes a link between consumers and producers. However, the value of cultural goods is also determined from another viewpoint: that of culture itself. It may be the sound of a musical work or the impression created by a certain composition of colours in a painting. Cultural value is manifested in a process that evaluates and re-evaluates and also defines itself. In culture, value is, therefore, an assessment of events or goods and services, which is also the case in economics. Discussion of value in economics, on the one hand, and value in culture, on the other hand, involves assessment, whether that assessment is financial, which is the norm in economics – and then with reference to price – or more extensive, as in the case of culture itself. A painting can

<sup>5</sup> For a discussion of the two approaches to the concept of value see, e.g., Throsby (2001) and Hutter and Throsby (2008b).

be of value to cultural history, and a pub or an inn in a village may have cultural value for the surrounding community far in excess of the cash turnover it generates. The inn may even be the chief centre of culture in a small community.

There can also be interplay between economic and cultural value, because an object of cultural value, such as the Louvre in Paris, may generate significant economic value in the form of tourist spending in France. By the same token, an object of economic value, such as the computer industry in Silicon Valley, California, can become a part of the culture of an area which is reflected in its school system and general social interaction.

It is traditional in the discussion of value in culture, in particular in the arts, to look at the artistic and the aesthetic and to highlight these factors, which are often subjective and reflect an individual's valuation of the work or event in question. Value in culture, for instance in a work of art, can derive from factors such as the aesthetic perception of the work or simply its origin, history or heritage.

Cultural value can also be inherent in an object as such or in an event. Observing a work of art or another object of culture is an experience that cannot be separated from the work itself. People would rather view the original of a painting than a photograph, even if the photograph reflects the painting precisely. When listening to music the setting, such as a concert hall, its atmosphere and acoustics, can in some cases have as great a significance for the audience as the music itself.<sup>6</sup>

Communications between people have been transformed in a variety of ways in recent years. Perhaps the most prominent of these changes are the influxes of blogs, social media, such as Facebook and Twitter, and sharing sites such as YouTube and Flickr, where people communicate and establish contacts in entirely new ways. The changes in the manifestations of culture have perhaps never been as extensive as in recent years.

Non-governmental organisations are another example of changed communications; these are movements of people, often focused on a single issue, which are a growing influence in modern society, including culture, although they may not have significant weight in the economy. This manifestation of changed relations between individuals has sometimes

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<sup>6</sup> For a discussion of experience in culture see, e.g., Krasilovsky and Shemel (2003), McCain (2008) and Sigurjónsson (2009).

had a significant impact on politics. Environmental organisations are examples of such movements.<sup>7</sup>

A characteristic influence on cultural affairs has been the price tag attached to cultural products, and the vulgar monetary element, as it is regarded in various quarters, seems to have sullied art, especially when terms like profit and yield enter the discussion. This is a misunderstanding, as it is unavoidable and, in fact beneficial, to give an economic value to things and events, and it makes no difference whether they are cultural or not. The reason is that people – or at least most of us – repeatedly have to consider cost in making economic decisions.

Shortly after the Second World War, Max Horkheimer and Theodor Adorno harshly criticised the cultural industry, saying that the commercialisation and industrialisation of art was a means used by capitalism to accumulate wealth and gain control over public needs. This criticism was expressed from a Marxist viewpoint, as Horkheimer and Adorno belonged to the Frankfurt School of philosophy and social theory. They viewed the concept of a cultural industry as a negative force. This criticism had great influence in the social sciences, although it has fallen into some disrepute in recent years.<sup>8</sup>

### 1.3 Creation in culture

Creativity is an important aspect of most branches of science, and this includes the social sciences. As regards culture, the maintenance and preservation of cultural goods, such as museums, art galleries and heritage sites, are important, but maintenance and preservation are separate issues, which are discussed elsewhere in this book. In economics, creativity is mostly referred to as an innovative concept and a driver of technological advances. Changes in technology are essential, and innovation is, of course, an important concept in economics. Because creation increases knowledge, it is a key concept in cultural economics. Culture and creativity are inseparable concepts, particularly in connection with the arts and artistic production, whether of books, films, music or other art forms. Creativity is the *sine qua non* of artistic endeavour.<sup>9</sup>

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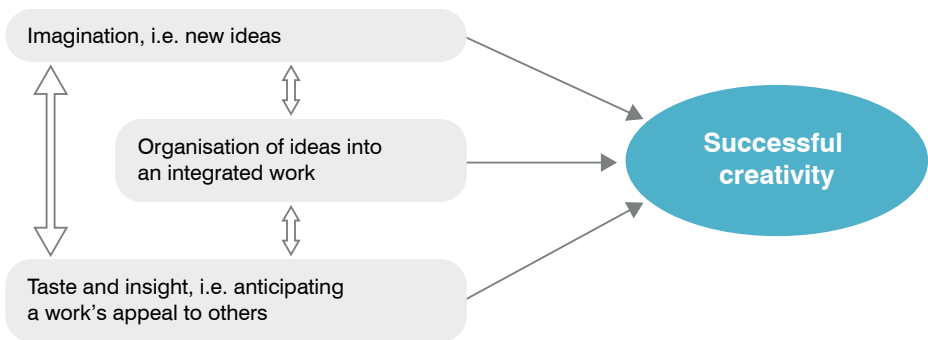
<sup>7</sup> A number of scientists have discussed non-governmental organisations, including, for example, Light (2008).

<sup>8</sup> For a discussion of the theories of the Frankfurt School see, e.g., Horkheimer and Adorno (2007).

<sup>9</sup> For a discussion creativity and innovation see, e.g., Baumol (2002).

Creation has something of a mysterious or, on occasion, even supernatural or divine quality. People blessed with a good singing voice are said to possess genius, an inspired talent that most other people lack. A child who is more creative than other children is referred to as a ‘*Wunderkind*’. Artistic geniuses in art are by no means commonplace, and no satisfactory explanations as to how artists came by their gifts and talents have gained widespread acceptance. Leonardo da Vinci, Pablo Picasso and William Shakespeare are on the lists of most art experts, and they have few equals. Likewise, lists of poets, composers of music, dramatists and novelists attain a similar unity. Perhaps it is possible to explain genius on the basis of inheritance and certain genetic combinations. In any event cultural economics is concerned more with conserving and supporting artistic excellence than with explaining its origins.

But creativity requires more than just inspiration, and it has been suggested that creativity involves three major traits, as shown in Figure 1.2.



**Figure 1.2:** Features of successful creativity

As Figure 1.2 illustrates, creation begins with imagination, which consists in coming up with new ideas. Secondly, there is the quality of being able to bring organisation to these ideas. It is not enough simply to have the ideas; they must be organised into an integrated whole. Thirdly, taste, which refers to the artists' ability to realise what portion of their work ought to be preserved and what needs to be put aside, or the insight of others to recognise the best of its kind, consists in the ability to appraise and develop a product of the imagination to the point where it becomes a work that appeals to others and possesses internal coherence. This can be complicated by the fact that artists are frequently ahead of their time, so that their genius is not appreciated until much later, when critics

and the general public catch up. The three factors also influence one another and interact, as illustrated in Figure 1.2 where the arrows point in both directions; in combination, these factors lead to creativity. Even though Figure 1.2 highlights the individual features of imagination, organisation and taste, there are other factors that also play an influential role, such as environmental factors and the surrounding community where the creative work is conducted. Seen from that broad perspective, creativity appears as a social system or process that is dependent upon the creator's surroundings.<sup>10</sup>

Although the term creativity is often applied in daily discourse to art and artists, it also has relevance for the creative industries in general, and, as in the world of art, creativity in the industries faces many and varied obstacles. The creator's environment can be an obstacle – we have already mentioned artists who are ahead of their time, and an entrepreneur may encounter difficulties gaining public appreciation of a new product or service – but the primary obstacle is normally the lack of capital. The definition of capital in economics is that it is the money used to pay for or fund resources; that is, resources which are used for production and are normally assets belonging to an undertaking or individual. Even where other obstacles exist, such as technological obstacles and lack of time, the lack of capital can easily lead to market forces taking precedence in the creative process. This precedence is reflected, for instance, in the fact that more popular music is published than classical music, simply because the market for popular music is so much larger. Shortage of capital, whether in the form of the income or revenue of an individual or a symphony orchestra, places severe restrictions on all creativity, just as in fact it imposes restrictions on various aspects of human life. One consequence of the scarcity of capital is that it can be difficult to survive on creativity alone: an artist will often engage

**David Attenborough** was born in Britain in 1926. He is a world-renowned wildlife broadcaster and ambassador *par excellence* of the British Broadcasting Corporation (BBC) in his field. Attenborough is meticulous, captures stunning images and describes extraordinary and complex matters in a clear and readily understandable manner. His educational television series *Life on Earth* has been shown worldwide. A naturalist by training, Attenborough began his career in radio and later became a versatile filmmaker. One of his works is a television series on climate change and animal life in the polar regions. David Attenborough is the recipient of numerous awards and honours and was knighted, becoming Sir David Attenborough, in 1985. He holds an impressive 29 honorary degrees from British universities, more than any other person. He has been assured immortality by having a number of newly discovered fossils named after him.

<sup>10</sup> A number of works have been written on creativity and its characteristics see, e.g., Sternberg (1999), Csikszentmihalyi (1999), Throsby (2001) and Towse (2010).

in more lines of work than artistic creation, and writers are frequently teachers or librarians, composers are often music teachers, and so on.

A work of art is a result of creation, and like other production it requires various kinds of input. One input can be genius, which engenders the product that will constitute the work of art, which incorporates value, both economic and cultural. Although it is not possible to obtain exclusive rights to an idea, creation begins with an idea, but a work of art is a combination of ideas, organisation and taste. When these factors are combined into an integrated whole, as shown in Figure 1.2, the end product may meet the conditions of intellectual property law and the work becomes the exclusive property of its creator and thereby acquires economic value.

Cultural products entail a moral right of ownership which is protected by intellectual property rights law. Intellectual property rights are vital for the cultural and creative industries and have, therefore, been given added weight in research into the creative industries.<sup>11</sup> It has become increasingly important to protect the rights of those who create works, as in the case of inventions and technical innovation.

Intellectual property rights constitute a temporary exclusive licence for the use of a product, method, material etc. subject to certain conditions; the award and protection of such rights have a long legislative history. A number of international agreements have been made concerning intellectual property rights in trade between countries, such as the Berne Convention, which provides for the protection of literary and artistic works. The Berne Convention dates from 1886 and uses the words 'literary and artistic works', thereby separating literature from the arts. This distinction illustrates the direction of the general discussion of intellectual property rights, which initially revolved mostly around works of literature with the result that this phrasing has remained in use globally, including in official texts of international agreements, and remains widely in use in national legislation around the world.

These rights are continually becoming wider and gaining greater weight in connection with intellectual property; they can be traded, as in the case of staging plays, where care has to be taken regarding copyright even in the case of old works, and they are durable: copyright expires

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<sup>11</sup> A number of scholars have discussed intellectual property rights in the context of cultural economics, including Burrows (1994), Hartley (2005), Varian (2005), Landes and Levine (2008) and Towse (2010); these works also contain numerous references to other writings.

seventy years from the time of death of an author, and copyright can be inherited, so that it is not only the artists but also their descendants who benefit.

In our time international intellectual property rights matters are the domain of the *World Intellectual Property Organisation* (WIPO), which is one of the agencies of the *United Nations* (UN). Agreements drawn up by the WIPO dating from 1996 on intellectual property and the performance, production or distribution of works of art, including distribution on the Internet, have a special interest for artists and other creative individuals. In addition to the WIPO agreements there are numerous local and regional rules on intellectual property rights.

Property rights are among the most important aspects of human society and a key to economic welfare. The ownership of an asset, whether a house, stocks, films or museums, needs to be made clear in order to permit use and disposal and possibilities for income generation or borrowing by pledging the asset as collateral. This basic principle of economics applies as much to creations as to other assets. In order to achieve success, creative individuals, artists, for instance, need to live in a community where they are assured of a fair return for their work and where it is assured that others will not use their work without paying for the use.

## 1.4 The creative industries

In the creative industries creation, as the name implies, is in the foreground. These industries rely for their existence on human capital, which represents the knowledge possessed by an individual or individuals that can be useful in the operation of a business enterprise, organisation or any other operation. Although the most important capacity of human capital in the creative industries may be knowledge, the knowledge needs to be supplemented by various other factors, such as versatility and tolerance. There is much, therefore, that is needed to enable creation to take place, such as various human characteristics and the environment in which the creation takes place.

The creative industries are an important factor of the economy, and they reflect a new vision of the subject of cultural economics. Studies of creativity and the creative industries were first conducted in the social sciences, psychology in particular, where the focus was primarily on creative individuals and on genius. Creation has been studied from the point of



view of personal development, family background, education and the social environment in which the creative work takes place.<sup>12</sup>

The environment in which people grow up can be a hugely influential factor. The external framework and organisation of a community, and the varying degrees of emphasis on culture, often decided by politicians, have influenced and deepened scholarly thought on the creative industries. Creativity consists in ideas that are generated, the order imposed on those ideas and their presentation, whether determined by an artist's tastes or the creative work of finding new markets or new business opportunities. This is reflected in the development of cultural economics: it began as the study of the economic aspects of art, but subsequently branched into the economics of culture, sometimes called 'cultural economics' and often referred to as the economics of the creative industries.

Creation often takes place in clusters, for instance in universities or other cultural environments. Some individuals need to work with others, for

instance in the production of a play, the performance of music or the filming of a movie. The creation of a work of art is the work of many, whether in its production or performance; individuals are brought together and their interaction can lead to innovation. It is, therefore, vital for creation and people involved in creation to have access to a fertile, encouraging and inspiring environment.

Universities are a typical favourable environment for creation and exchanges of views, whether within faculties, at conferences or through the production of scientific or scholarly articles. In a typical situation, a number of individuals will be working on the same subject and incrementally advancing the existing knowledge. Of course, an academic

**William Baumol** was born in the United States of America in 1922. He is a professor of economics at New York University and one of the best known economists in the world. He has taught at a number of universities and held a number of distinguished positions of trust. He is still doing research despite his age. Among other things, Baumol has conducted research on the labour market, the methodology of economic thinking and a number of other economic issues. His book, *Performing Arts – The Economic Dilemma*, written with W.G. Bowen and published in 1966, is regarded as having marked the birth of cultural economics. Other subjects addressed by Baumol include monetary theory, taxes and entrepreneurship, all fields in which he has been hugely influential. His prolific contribution to the study of economics include over five hundred peer-reviewed articles and a number of full-length books. Baumol has received a number of awards in the course of his career and has often been seen as a candidate for the Nobel Prize in economics.

<sup>12</sup> A great deal of scholarly work has been done on creativity and the creative industries in psychology, e.g. by Amabile (1983); in connection with art studies see, e.g., McNiff (1998), Candy and Edmonds (2002) and Sullivan (2010), and in connection with museums and galleries see Frey and Meier (2008). The environment of creative work has also been extensively discussed see, e.g., Caves (2002) and Potts *et al.* (2008).

environment is not a requirement for creativity. However, in most cases creation requires not only individuals, but groups of individuals and/or institutions, and it requires organisation. Universities, for instance, and symphony orchestras are typical institutions of this kind. A group engaging in creative work has to be sufficiently strong for ideas to develop and gain support. Just as land for cultivation needs to be arable, creativity requires fertile soil. You cannot grow corn in a desert. The environment is, therefore, an important element, and this will in many cases call for the involvement of government, which can assist in making possible an environment that is suitable for creative work.

Individuals also need their work to attract attention, since their creations have to extend beyond themselves. Creation can be a part of an individual's personal development, but a creation as a product also has to appeal to others. A work of art has to be staged, shown, read or otherwise 'consumed'. A technological innovation has to have a role in production and the economic and cultural value has to come into existence.

Even though cultural and creative production is in most cases much the same thing, not all culture falls within the boundaries of creativity. Examples of this include religion and religious affairs, which, as such, are culture, but not a part of the creative industries. Some scholars do not actually draw this distinction but focus instead on production of cultural goods that are assets or arise out of the assets of their creator; that is, goods that are protected by intellectual property rights. The distinction that is drawn between cultural industries and creative industries therefore rests on a point of view rather than on an essential difference. This means that museums and sports, while a part of culture, are not included in the creative industries. Another feature that should be emphasised is that art and creativity often revolt against prevailing views and opinions. Rebellions against, and radicalism in the face of, prevailing views are as old as art itself, and in some cases may explain the origin of some kinds of art. New ideas replace old ideas, which makes creativity a source of change, and on occasion a substitution cannot be made without some ruffling of feathers.

A business enterprise or institution operating in the creative industries could, for instance, be involved in the motion picture industry, whether this involves actual filmmaking, distribution or exhibiting films in theatres or airing them on television. These can be enterprises or institutions working on the production and distribution of music or in the sciences,

as in the case of research conducted in universities. They may also be involved in tourism, which is to a large extent based on creative thinking, as in the case of cultural heritage tours or cultural tourism in general.<sup>13</sup> There are numerous definitions of creative industries.

Firstly, the creative industries can include architecture, advertising, interactive computer games, software design and related services, arts and crafts, design, filmmaking, along with video compact disks, television and radio, the stage, fashion, music, publication and commerce in art and antiques.<sup>14</sup>

Secondly, we can also include research and the toy industry. The addition of research and the toy industry to the creative industries is explained by the fact that these additions fall within the scope of intellectual property rights and, as noted earlier, it is common for such rights to occupy a central position in studies of the creative industries.<sup>15</sup>

Thirdly, the creative industries are defined based on four major features: heritage, arts, media, and functional creations. Heritage is divided into two subcategories, that is to say traditional cultural expressions, such as arts and crafts, festivals and celebrations, and, on the other hand, cultural sites, such as archaeological sites, museums and libraries. Art is inspired by heritage, identity values and symbolic meaning. The arts are divided into visual arts as in the case of painting, sculpture, photography and antiques, and performing arts as in the case of live music, theatre, dance, opera, circus and puppetry. The media include publishing and printed media such as books, newspapers, magazines and other publications, as well as audio-visual products, such as film, television and other broadcasting. Functional creations are goods and services that have functional purposes, such as design, new media and creative services like architecture and advertising. This definition, created by the *United Nations Educational, Scientific and Cultural Organisation* (UNESCO) is likely to gain wide acceptance and prominence in the coming years.<sup>16</sup>

Fourthly, defining the creative industries looks at the production itself and includes among the creative industries those industries that

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<sup>13</sup> For a discussion of cultural tourism see, e.g., Hughes (2000) and Richards (2006).

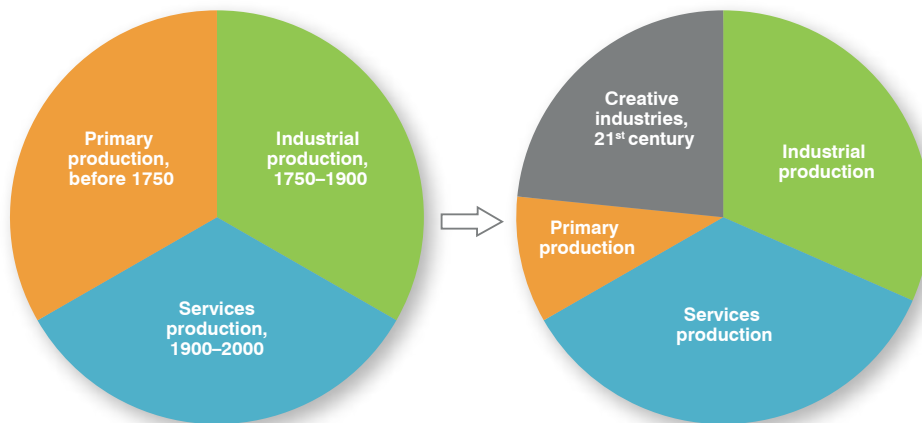
<sup>14</sup> The definition of thirteen industries as creative has its origins in the first decade of the present century see *Creative Industries Mapping Document 2001* (2001); this definition has been widely used.

<sup>15</sup> See Howkins (2004).

<sup>16</sup> This definition used by UNESCO, based on four principal aspects, can be found in *Creative Economy Report 2010. Creative Economy: A Feasible Development Option* (2010).

manufacture products and services of cultural and artistic value. This approach is narrowed here by using the term ‘cultural industry’. This industry covers everything pertaining to advertising and marketing, broadcasting, radio and television industries, film industries, the Internet industry, music industries, print and electronic publishing and video and computer games.<sup>17</sup>

Fifthly, the creative industries can be defined by looking at individuals and their jobs and professions. In economics, production in the economy has traditionally been divided into three categories: primary production, industrial production and service production.<sup>18</sup> This approach adds a new dimension, that is, a fourth category, namely the creative industries, where the creative class is defined as the individuals who work in the creative industries, as shown in Figure 1.3.<sup>19</sup>



**Figure 1.3:** The four dimensions of the economy

Primary production, mainly agriculture, fisheries and mining, was dominant in the world well into the second half of the eighteenth century. It was followed by the industrial revolution, which, with its harnessing of steam power and external energy, had a huge influence for the first time

<sup>17</sup> A discussion of the creative industries primarily from a cultural point of view can be found, e.g., in Hesmondhalgh (2002).

<sup>18</sup> The left side of Figure 1.3 shows the three earlier categories (primary production, industrial production, and service production) as equal in size. The right side of Figure 1.3, with the creative industries added, aims to depict the contemporary division of the Icelandic labour market.

<sup>19</sup> The scientist who has written most extensively about the creative class is Richard Florida; see Florida (2002) and Florida (2005).

in human society. The nineteenth century was dominated by industrial production, but was superseded by service production in the twentieth century. Primary production is now only a small part of the economic activity of most countries, as shown in the right side in Figure 1.3. It can be difficult to assess the role of culture in the economy, and care must be taken to avoid both over- and underestimation.<sup>20</sup> The creative industries may well be the principal industries of the twenty-first century, particularly in the developed countries. One of the principal reasons for this trend is that a constantly shrinking proportion of income is devoted to sustenance while more and more is devoted to recreation and experience.

The creative industries require creative thinking, but in different quantities, as is the case in all other industries. Uncertainty can be significant, both as regards supply and demand, in the cultural sector. It can be difficult to channel production in culture into predetermined courses, and it can also be difficult to predict consumers' tastes and changes therein. However, this description of uncertainty applies to a greater extent to some aspects of culture than others; for instance, it applies well to motion pictures, but not to religion, which also forms a part of culture.<sup>21</sup> The creative industries are like other sectors that are special in certain areas, but fundamentally they are no different from other sectors of the economy, notwithstanding the duality of economic and cultural value.

One of the most famous quotes in the discussion of the arts is from the screenwriter William Goldman, who responded to the question of predicting the success of films that 'nobody knows anything'. This assertion has proven remarkably accurate. It is impossible to predict the success of a film, although numerous attempts have been made to do so using a variety of statistical methods.<sup>22</sup> What is interesting regarding Goldman's quote is that he was himself an experienced screenwriter and wrote a number of excellent scripts and was thus extremely familiar with the industry and with techniques for creating successful products. Even so, he could not come up with a better answer than 'nobody knows anything'. But the fact is that his answer applies to virtually all the creative industries, since there is almost invariably significant uncertainty regarding the public acceptance of any new cultural product.

<sup>20</sup> For studies in this areas see, e.g., Florida (2004), Florida (2005) and Einarsson (2004).

<sup>21</sup> For a discussion of uncertainty and risk in the cultural sectors see, e.g., Pignataro (1994), Scott, W. R. (2006) and Seaman (2008).

<sup>22</sup> Goldman's comment is from Goldman (1983) and a summary of methods to try to predict the success for films can be read, e.g., in De Vany (2005).

## 1.5 The special position of culture in economics

Discussion of culture has changed – and increased – in recent decades, as evidenced by UNESCO reports.<sup>23</sup> Culture is now increasingly discussed in the context of economics. This change is the result of a number of factors, including the cultural policies of government authorities and economic changes brought about by globalisation.<sup>24</sup> Culture is about much more than art and cultural heritage, and culture often has an impact on other production. Increasing attempts are being made to understand the links between culture and other economic factors.

Culture has strong ties to history, and cultural economics attempts to measure individual cultural indicators, such as the number of people employed in cultural activities, the contribution of culture to gross domestic product, the generation of export revenues, and so on. Gross Domestic Product (GDP) is a measure of the value of the finished goods and services produced in a year in a country. GDP indicates the scale of the value available for distribution.

International trade in works of art and other cultural goods has always been extensive. Large gatherings, such as music and art festivals, are staged in numerous countries. They create significant value and attract tourists. In recent years exports in the creative industries worldwide have grown spectacularly.<sup>25</sup>

An important aspect of any economy is the rules that govern the business environment, whether established by businesses themselves or codified in laws or rules issued by government agencies. These rules and laws influence human behaviour and thereby decision-making. Among the subjects studied in cultural economics is the impact of different rules on supply and demand for cultural events or works of arts and other cultural goods. The studies focus on the regulations that apply in the respective environments of cultural institutions, for example in the case of theatres that operate in a competitive environment while subsidised by government.<sup>26</sup> These

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<sup>23</sup> Reports of this kind include the *World Culture Report: Cultural Diversity, Conflict and Pluralism (2000)* and *Recommendation concerning the Status of the Artist (1980)*.

<sup>24</sup> The changes resulting from globalisation in culture-related sectors have been the subject of extensive discussion; see, e.g., Peacock and Rizzo (1994), Storm (2003) and Obuljen (2006).

<sup>25</sup> Much has been written about the international trade in cultural goods and art festivals; see, e.g., Schulze (1999), Quinn (2005), Tohmo (2005), *Creative Economy Report 2010* and *Creative Economy: A Feasible Development Option (2010)*.

<sup>26</sup> For a discussion of theatres in competition see, e.g., Hansen (1997).

studies are to some extent the subject of the New Institutional Economics, one of the special fields of economics.<sup>27</sup> In addition to the regulatory environment, New Institutional Economics covers various other factors, such as social custom, intellectual property rights, transaction cost, organisation of resource utilisation and means of improving efficiency in the economy; that is, the ratio of resources to produced goods and the utilisation of resources in production. The tools used in the New Institutional Economics are well suited for use in analysing the cultural sector.

Special circumstances in culture and the arts have the effect that cultural economics is a separate field of the economic sciences. These special circumstances include the regulatory framework of culture and the arts and differences in consumer behaviour, that is from one country to another and one generation to the next. As regards the supply of art, a distinction is drawn between the artist and the framework, or institution, where the art is offered, such as a theatre or concert hall. 'Artist' is not a regulated professional title, even though artists will usually have a significant educational background.

The proverbial poverty of artists and its importance to fertility for the production of art are by now established features of the discourse on artistic production. This view was popular, especially in the romantic period in the nineteenth century, but it is far from being a universal rule. A number of artists, even in the Romantic Era, had decent, if not lavish, incomes. Artists in the employ of public figures such as kings or queens and the nobility, and public bodies, such as the church, included painters like Leonardo da Vinci, Peter Paul Rubens, Rembrandt Harmenszoon van Rijn and musicians such as Wolfgang Amadeus Mozart, Giuseppe Verdi, Ludwig van Beethoven and Richard Wagner; these were in many cases quite wealthy people in their time, at least for parts of their lives.<sup>28</sup>

The life and work of an artist, however, will often be characterised by financial circumstances that are sometimes worse than those of others with similar educational backgrounds, with the result that artists will often have other secondary – or primary – employment for sustenance. Artists' incomes are also frequently irregular with greater fluctuations

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<sup>27</sup> For a discussion of New Institutional Economics see, e.g., Eggertsson (1990), Jackson (1996), Stanfield (1999) and Gander and Riepke (2004).

<sup>28</sup> For a discussion of the financial circumstances of artists of the past see, e.g., Frey (1994) and Throsby (2010).



than those that are common in other walks of life.<sup>29</sup> However, artists will often be captivated by their work, which they may carry out for purposes other than hope of financial gain. An increase in pay for the secondary work which is unrelated to the artistic creation can, therefore, cause the artist to cut back on the workload in the secondary work in order to devote more time to artistic creation. This common reaction runs counter to the normal effect of a pay rise, where an individual may even want to work more when his or her work is appreciated more and the appreciation is expressed in greater remuneration. In fact, however, the work of an artist is often project-oriented and will not consist in a permanent job at an institution or business enterprise. Making greater use of part-time or temporary employees for individual projects rather than employing permanent staff reduces risk for a business enterprise. This situation is common in theatres, for instance, where an attempt is made to limit the number of permanently employed actors and rely more on actors who are appointed for a specific staging and then removed from the payroll when the piece is retired.

Economics uses the term ‘externalities’ to denote the impact that the production of goods or services has on a third party or society as a whole without any involvement of any kind by such third party in the production or business transaction. This impact is often the source of market failure, where the market does not supply goods and services in an economical quantity; that is, the failure consists in too much or too little production. In many cases the only solution to market failure may require government intervention.

Externalities can be positive or negative. An example of a negative externality could be pollution, which can result in cost, such as

<sup>29</sup> Of all modern writers, perhaps George Orwell best exemplifies the impoverished artistic craftsman toiling away in abject poverty; the supreme irony of his life is that had he lived, say, an additional thirty years (up to ca. 1980), the reality of his straitened circumstances would have been significantly modified by the publication of *Animal Farm* and *Ninety Eighty-Four*, whose combined sales to date number in the millions of copies. Indeed, initial sales of *Animal Farm* in the USA by 1950 had given Orwell his first financial security.

**Ludwig van Beethoven** was born in 1770, in Bonn, and died in 1827. He lived for most of his life in and near Vienna, Austria. Beethoven is one of the greatest composer of all times, with nine symphonies to his name and countless other compositions, including the German National Anthem. He lost his hearing in the later years of his life and gradually became totally deaf, but continued to compose music, including many of his greatest works. Beethoven lived for a while in the town of Baden near Vienna, where he composed a number of his works. The Ode to Joy (German *An die Freude*), which has become the Anthem of Europe, is a part of Beethoven's Ninth Symphony. Beethoven was an admirer of Napoleon, but when Napoleon's imperial ambitions became evident Beethoven was furious at what he saw as a betrayal of the ideals of the French Revolution and in his rage he struck out the dedication to Bonaparte on the title page of his Third Symphony.



damage to human health or the environment. This cost may have consequences for society as a whole, but little or none for the party causing the damage. In the economy individuals and businesses bear expenses and derive profit from business, which leads to efficiency. Negative externalities act as a sort of wedge in the economy which causes increased cost. An example of a positive externality could be education, which advances and improves society and increases productivity as a result of technological progress. The same applies to culture and cultural activities, since increased cultural activity, according to one school of thought, improves society and is, therefore, a positive externality for our lives as individuals and our relations with others. However, the positive externalities of culture comprise a variety of factors that are not easily measurable, such as well-being and happiness.

Cultural assets change in value from one period to another, between years, decades or even centuries. What was worthless at one time may become valuable at another, years, decades or centuries later, and thereby value is created. Johann Sebastian Bach composed his works a long time ago, but they still have a significant weight in the economy. His music is still performed live in concert halls, broadcast or published on disks and other media and are thereby repeated continually with new value created each time.

The economy is sometimes described as a living organism. We speak of the economy being 'weak' or 'sound' or 'healthy', and we speak of the economy 'recovering' or being 'revived'. The diction is akin to that of our discussions of individuals who are afflicted by or recovering from disease. As a matter of fact, it is not at all far-fetched to speak of the economy as a living organism: it changes, develops and has periods of ups and downs like a living being. The same is true of culture, which is also often described as a living organism. We speak of a 'living' culture and 'dying' or 'dead' culture. The culture of the Incas in South America is an example of a dead culture, while the culture of Hollywood is an example of a living one.<sup>30</sup>

One of the basic elements of human economic activity is the allocation of limited goods. There is not enough for everyone, and there are severe shortages of some goods, such as food, employment and education, for billions of people. The goods that are available therefore need to be

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<sup>30</sup> For a discussion of culture in connection with the life sciences and environment see, e.g., Barker (2003).

allocated in as efficient a manner as possible, whether in the case of natural resources, such as energy and fish stocks, or our own work product. The production of goods and services, that is, supply, meets demand in a world of shortage, where a choice is continually being made between a number of alternatives. The principal questions to be answered by economics are what should be produced, in what quantities and for whom. This question applies equally to cultural goods as to everything else that is produced in the world.

## 1.6 Basics of economics and opportunity cost

Economics, as a social science, deals with people, human society, the human need for economic goods and economic coexistence with others. While other branches of the social sciences may examine culture from a variety of viewpoints, cultural economics focuses on the connection between economics and culture and examines the various economic aspects of culture.

In their everyday lives people confront certain fundamentals of economics which have been expressed by scholars and on which there appears to be a largely general agreement.<sup>31</sup> The first fundamental involves the choice that people need to make regarding the use of the funds at their disposal; for example, if a sizeable portion of money is spent on clothes, a lesser amount will be available for the theatre. The second fundamental is that when something is done, something else is not done. A person who spends an hour watching a film cannot use that same hour to study cultural economics. This is known as opportunity cost, that is, the cost of missing the second best alternative to a certain course of action, for instance when a decision is made to manufacture one product rather than another. The third fundamental is the assumption that people behave rationally and adapt to changes. For instance, if the price of goods and services changes, attitudes to those goods and services will also change. The fourth fundamental is that trade benefits everyone. It cannot benefit an economy if individuals or nations isolate themselves. Trade between countries and the specialisation of individuals in areas where they excel will always benefit the commonweal. This is particularly important in the cultural industries, where ideas travel at great speed between countries and tension is created between cultures,

<sup>31</sup> For a discussion of these fundamental features of economics see, e.g., Mankiw and Taylor (2010).

with a resulting positive impact on creativity. The fifth fundamental is that markets are a good way to organise the economy. The 'market' is the venue where supply and demand meet, and price is determined in a process known as price mechanism. Experience has shown that this arrangement has been efficient. The sixth fundamental is that government can have a positive impact on the market through interventions, such as support for culture.

Economics attempts to decide and explain what goods are produced, their quantities and how and for whom they are manufactured. The decision is based to a significant extent on what is known as the price mechanism: price is set in the market and determined primarily by supply and demand. As a general rule, if the price of something rises, for example, the cost of a cultural tourist trip, the demand for participation will fall. The organiser of the trip, on the other hand, might well welcome the price hike and attempt to increase output and thereby the supply of cultural tourist trips.

Participants in the economy fall into three principal groups. On the one hand, there are companies that produce goods and services for others,

**Miguel de Cervantes** was born in 1547 and died in 1616, the same year as William Shakespeare. Cervantes was born into a poor family and among other things he earned a living as a soldier and a tax collector. His most famous work, *Don Quixote de la Mancha*, tells the story of a deluded *hidalgo*, or gentlemen, who goes out on a knightly quest with his companion, Sancho Panza. Their story is one of the landmarks of literature and is often referred to as the first modern novel. Its influence on literature spread far beyond the Spanish-speaking world and *Don Quixote* has been translated into virtually every modern language in the world. Although Cervantes achieved his greatest fame for the first part of *Don Quixote*, he also wrote a number of other works. People still talk about 'tilting at windmills', which is a phrase from *Don Quixote*, where the hero attacked a windmill under the delusion that it was a giant.

and, on the other hand, there are consumers, that is, individuals, families or households, who consume goods and services and contribute their work and other production factors at their disposal. The link between business enterprises and individuals is that individuals sell their work, receive their remuneration and then use this remuneration to buy company outputs. Enterprises produce, sell and use production factors, including human resources. The third important participant in the economy is the state or government. The interrelationship between these three participants is a special subject of study in economics, including cultural economics.

There is not enough food and energy available in the world for everyone. A choice needs to be made between various options, that is how resources and limited raw materials should be used. Choosing between options

entails a decision. Some goods and services are free, a classic example being the atmosphere; everyone can breathe the air without effort or cost. Air is necessary for life, but so is water, but water is a limited resource in the world and in some places so scarce that it is very expensive. It should be noted, though, that as a result of pollution in recent decades, clean air is no longer an unlimited free commodity.

Globalisation has brought about extensive economic, social and geopolitical changes. Firstly, globalisation has eliminated obstacles between countries as regards the movement of capital and labour; secondly, the marketplace for cultural goods is now the entire world; thirdly, the globalisation of communications has resulted in the free flow of cultural ideas throughout the world. As a result of globalisation new forms of expression have emerged, new forms of communication, and the exchange of experiences, ideas and goods is now continuous and relentless. Technological advances in communications and globalisation have led to a culture of innovation, risk, expectations and hope.<sup>32</sup> Technological advances have also led to more efficient management, marketing and effective trading.

In an economy all the participants will attempt to make the most of their respective situations and advantages and specialise in what they do best. Those who are better at producing goods or services in a particular area will have what is known as an absolute advantage. This benefit may result from better technology, special skills, availability of resources, better organisation of manufacturing and sales or stronger capital. However, it is not absolute advantage that makes a business thrive, but rather *comparative advantage*, and it, like other factors in economics, is measured on the basis of opportunity cost. This means that the party with the lower opportunity cost has a comparative advantage over another party. All production and trade are based on comparative advantage. All undertakings have their respective areas of specialisation in comparison with others, and this provides an advantage in business. This asset applies equally to the production of cultural goods and other goods, such as shoes or bread. Given that comparative advantage is a decisive factor in determining where goods or services are produced, it is important to promote the factors that can create comparative advantages in important industries.<sup>33</sup> All these concepts feature in Illustration 1.

<sup>32</sup> For a discussion of different types of culture see Castells (2002).

<sup>33</sup> For a discussion focusing on comparative advantage in economics see, e.g., classical textbooks such as Samuelson and Nordhaus (2005) and Krugman and Wells (2009).

### Illustration 1: Comparative advantage and opportunity cost

Comparative advantage is a perpetual theme in any economy and in economics. But what is a comparative advantage? It is best explained using an illustration.<sup>34</sup>

If the famous footballer Lionel Messi has some spare time one Monday morning, he can appear in an advertisement, which could earn him the sum of \$100,000. However, he can also use the time to mow the lawn, which is long overdue; this task would take three hours, or about the same time as filming the advertisement.

Sancho Panza is Messi's friend nearby, who is not affluent; he is offered an opportunity to work as a replacement cook at a nearby fish restaurant in Barcelona, which will earn him the sum of \$1,000, as Mr. Panza is an excellent cook. Mr. Panza can also mow lawns, and sometimes does, but he is not as good at it as Messi is, who is a trained athlete in much better shape than Mr. Panza. It would take Mr. Panza six hours to mow Mr. Messi's lawn.

In this illustration Lionel Messi can mow the lawn much faster than Sancho Panza, and he can also earn much more money than his neighbour doing other things. In the language of economics, this means that Lionel Messi enjoys an *absolute advantage*, both in generating income and in mowing lawns. However, it is not absolute advantage that forms the basis of trade. We need to look at what constitutes the two friends' sacrifices when they take on a temporary acting job in an advertisement, helping out in a restaurant or mowing Mr. Messi's lawn.

A basic task of economics is to answer the question of what is sacrificed when something is done, known as *opportunity cost*, which is the value of an option that is lost when another option is chosen. If Mr. Panza mows the lawn, he will sacrifice \$1,000, the sum that he could have earned at the restaurant. If Mr. Messi mows the lawn, he will sacrifice \$100,000, which he could have earned for the advertising gig. Since Mr. Panza's opportunity cost is lower, he enjoys a comparative advantage as regards mowing the lawn, even though his efforts cost him twice as much time as those of Mr. Messi.

The best option is, therefore, to arrange matters so that Mr. Messi accepts the acting assignment while Mr. Panza mows the lawn. Mr. Messi would have to pay Mr. Panza more than \$1,000, but he can well afford to do so, having earned an income of \$100,000. Mr. Panza would no doubt be quite happy with the sum of \$2,000 for his labour.

This little illustration illustrates absolute advantage, comparative advantage and the efficiency of trade, which is based on comparative advantage. And these are not recently discovered facts; the British economist and philosopher David Ricardo expressed these thoughts about 200 years ago, although it has often been difficult to persuade politicians to understand this fundamental feature of commerce and trade.

Worth particular mention in this context is the misconception that an economic sector and/or individual with inferior performance in all respects requires special protection from competition with others. This is false, as illustrated by Sancho Panza's story. It pays off for him to concentrate on things where he has a comparative advantage. This applies everywhere in the economy, as it is comparative advantage, and not absolute advantage, that determines efficient trade.

<sup>34</sup> The basic example of the athlete and the neighbour is taken from Mankiw and Taylor (2010).

The influence of culture is pervasive in most societies and affects all individuals, which is in fact the case with most economic factors. Culture is the driving force of a number of human undertakings. Many aspects of culture are well suited for explanation in the context of economics. However, culture is fraught with value judgments, which are personal and which change in the course of time, sometimes swiftly and radically.

Consumer behaviour is one of the principal factors of economics, where the individual is the focal point, even though the individual may be part of a larger whole, such as a household or a family. In assessing total consumer demand, all individuals in all sectors are taken into consideration. Since culture permeates society as a whole and its use is not limited to specific groups but society at large in one way or another, it shares some characteristics with the air in the atmosphere. Not every human need can be supplied on the basis of profit and not all supply can be assured by enforcing competition, and some needs cannot be supplied by business entities operating for profit. These characteristics of culture, and even just the scope of culture in and of itself, is sufficient justification for a government role in ensuring an adequate and desirable supply of cultural goods and services.

The scope of the culture industry alone is an important justification for government playing a role in establishing a cultural policy. Arts and other cultural activities are not the domain of a small group that requires government funds to survive; they are the foundation of extensive economic activity, including an extensive production of cultural goods which are sold around the world. Culture is, therefore, both a part of, and a prerequisite for, extensive economic activity in addition to its role in improving and enriching quality of life. There are, therefore, not only macroeconomic reasons but also microeconomic reasons that provide arguments in favour of government support in the culture industry.

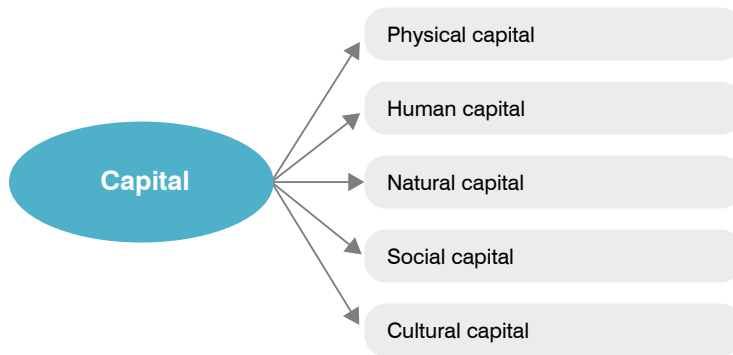
Economic impact reflects the aspirations of individuals, both for themselves personally and also for themselves as participants in a community. In economics the desires of individuals and their valuation of utility and expectations are in the foreground and determine demand. All these individuals are at the same time participants in society as a whole and participants in groups within that same society. The impact of culture in a community represents the combined impact of individuals and groups.

Changes in technology also cause changes in behaviour and thereby in supply and demand. For instance, there is now a new generation of

people who use cell phones, the Internet and digital media, not only to expand their cultural horizons, but also to turn from being passive consumers to become active participants in cultural and human exchanges.

## 1.7 Capital in culture

Capital, that is, the value of resources used in production, is categorised in a number of ways, as shown in Figure 1.4:



**Figure 1.4:** Categorisation of capital

Physical capital can consist in buildings and machinery, that is fixed assets. Physical capital also includes liquid assets, which are various catalysts used in the production of goods and services, in addition to current assets, which include cash, bank deposits and securities. Another category of resources is human capital, which includes the talent and experience of individuals. Human resources are becoming increasingly important in the economy and especially in the creative industries and, thereby, culture.

Natural resources refer to both renewable and non-renewable resources of nature. Renewable resources include, for instance, water and human creativity, while non-renewable resources include oil, coal and metals, which will be depleted in time. Fish is a renewable resource, given sensible utilisation, since fish stocks can be harvested year after year if the fishing is prudently regulated. The ecosystem, which maintains and replenishes natural resources, constitutes natural capital.

Social capital represents the value of the social system adopted by a community. Social capital is discussed in the context of trust, customs and

other aspects of human relations. Cultural capital is the value of the assets used in culture.

The classification of capital shown in Figure 1.4 illustrates the way in which the points of focus have shifted in the economic sciences. In the earliest stages capital was mostly physical capital, but in time the focus shifted to certain other factors such as human resources and their social framework, and the concepts of human capital and social capital gained a central position. The same has happened in culture and cultural capital. A concert hall, for instance, is cultural capital, but at the same time it is physical capital.

A balance sheet shows the total assets of a business undertaking; it is a list that shows, on the one hand, assets and, on the other hand, liabilities, the latter being the capital that has been used to fund the acquisition of assets. The difference between assets and liabilities is referred to as equity. A balance sheet shows the book value of a firm, for example, at the end of a year. An income statement, also known as a profit and loss account or statement of earnings, reflects a business's income and expenses. An income statement covers not merely one point in time but a period, frequently a year.

A service is provided over a period of time, as in the case of a concert or a play. Its production, and the formation of its value, takes a certain amount of time and generates income that is entered in the income statement. The building where a play is staged or a concert performed represents a cultural asset having a certain value that is entered in the balance sheet.

Cultural assets, such as plays, have both a cultural and an economic value. The economic value is reflected in the proceeds from the sale of tickets or the wages paid for the performance, while the cultural value is reflected in the audience's experience of the performance. To give another example, a painting's value in terms of the physical capital used to produce it is not significant. Its creation requires canvas, paint, brushes and a stretcher frame, none of which is expensive. However, a completed painting will have value, sometimes enormous value. In this case it is primarily the cultural input that creates the final value.

Both cultural resources and natural resources have deep roots in time, and they impose obligations both on the current generation and future generations, so it is not inappropriate to speak of a cultural ecosystem,



which supports cultural life and human society, just as the natural ecosystem sustains continuity in nature. The cultural ecosystem thus denotes both cultural life and cultural community.<sup>35</sup>

The linkage between cultural capital and natural capital, where the principal components are renewable and unrenewable resources, the ecosystem, air, water and the human genome, is important, since sustainability is relevant to cultural capital, as in the case of preserved cultural sites. The same applies to natural capital.<sup>36</sup>

We sometimes speak of assigning a price to priceless things in our discussion of natural capital. We say that something in nature is invaluable and that it is a necessary condition for all life. Water and air, for instance, are necessary conditions for life. This discourse can also be applied to cultural capital. We sometimes talk about a work of art as being ‘priceless’, about a priceless cultural heritage or priceless cultural sites. However, the term ‘priceless’ is not a useful term in economics, since economics deals with assigning a price to things, as in the case of insurance value.<sup>37</sup>

In discussions of natural capital the question often arises whether capital assets are interchangeable, for example, whether one resource, say, solar energy can be exchanged for another, say, coal, without disrupting the ecosystem. The same applies to cultural capital, for instance if a selection has to be made between branches of art. If capital is limited, which it usually is, a decision may need to be made whether to spend it on a theatre or a concert hall and which aspect of art and culture should be promoted at the expense of others. Opinion is divided, but the interchangeability of capital assets is common, as in cases where one source of energy replaces another (solar energy for coal).

## 1.8 Organising statistics in culture

Organising cultural statistics as clearly as possible is necessary because statistics provide the basis for all decision-making and comparison. Although there is some consistency in statistical organisation between countries, work is still in progress on improving registrations and listings

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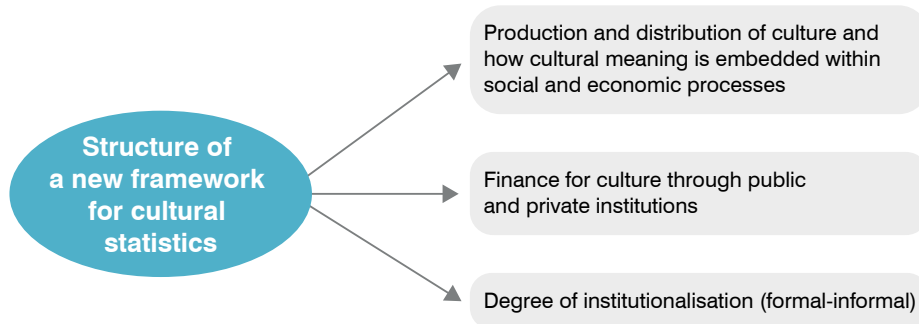
<sup>35</sup> For a discussion of the cultural ecosystem see, e.g., Benhamou and Peltier (2007).

<sup>36</sup> For a discussion of sustainability and cultural capital see, e.g., Gilmore *et al.* (2007) and Tisdell (2003).

<sup>37</sup> For a discussion of the priceless in capital see, e.g., Grampp (1989) and Heinzerling and Ackerman (2002).

and eliminating duplication. UNESCO's Institute for Statistics (UIS) has been working on a new framework for cultural statistics in recent years, which has now been completed in all major respects.<sup>38</sup>

The new framework incorporates a number of classification systems that are currently in use, such as ISIC (International Standard Industrial Classification) for cultural production activities, CPC (Central Product Classification) for cultural goods and services, ISCO (International Standard Classification of Occupations) for employment in culture, HS (Harmonised Commodity Description and Coding System) for international flows of cultural goods, and ICATUS (UN Trial International Classification of Activities for Time-Use Statistics) for cultural participation. The new framework<sup>39</sup> rests on three main factors, as shown in Figure 1.5.



**Figure 1.5:** Principal factors of a new framework for cultural statistics

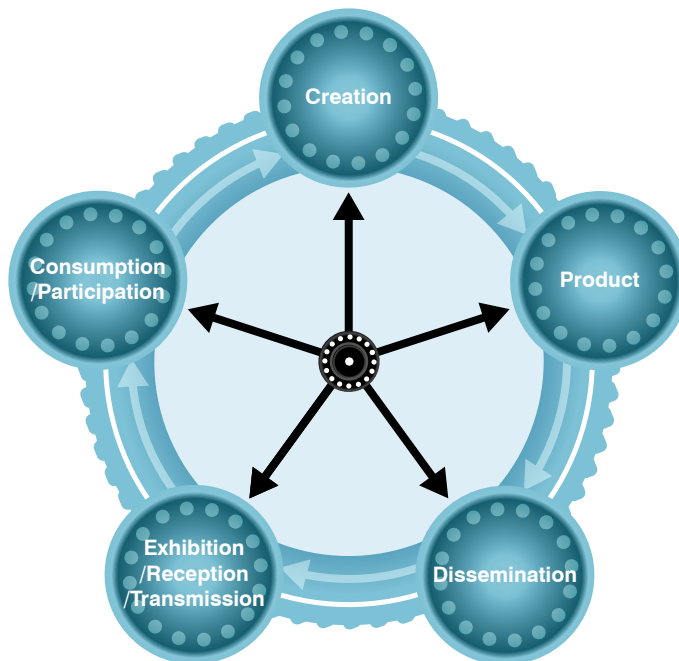
These principal factors, shown in Figure 1.5 above, have the main purpose of keeping accurate track of the production and distribution of culture and cultural goods and of taking into account how, and to what extent, culture is woven into the fabric of any economy. Secondly, the connection and interaction are taken into consideration of the other three principal factors in financing culture: (1) public funding, either through direct or indirect contributions, such as tax incentives; (2) private funding or the contributions deriving from the work of non-profit organisations; (3) the contribution made by business enterprises in the cultural sector, usually private business enterprises. The reason for this approach is that it is difficult to obtain precise statistical data on how

<sup>38</sup> For a discussion of cultural statistics see, e.g., *The 2009 UNESCO Framework for Cultural Statistics* (2009).

<sup>39</sup> For a detailed description of this new framework see *The 2009 UNESCO Framework for Cultural Statistics* (2009).

much the different forms of funding contribute, making precise analysis, and comparison across borders, difficult. Thirdly, an assessment is made of the extent of formal relations within culture, for example within businesses and institutions, and the informal and extensive cultural relations, which because they have no market price, necessitate an appraisal of their financial value.

The new framework includes individual areas that cover a certain cultural activity, such as the theatre, and those who are involved in its production, such as directors, actors and promoters. At the same time the framework must be flexible, that is adaptable to different regions or countries. This definition also incorporates aspects discussed earlier in connection with the creative industries, such as design and advertising, which are generally not categorised as culture. The concept of the culture cycle covers the creation, manufacture and distribution of culture, as shown in Figure 1.6.<sup>40</sup>

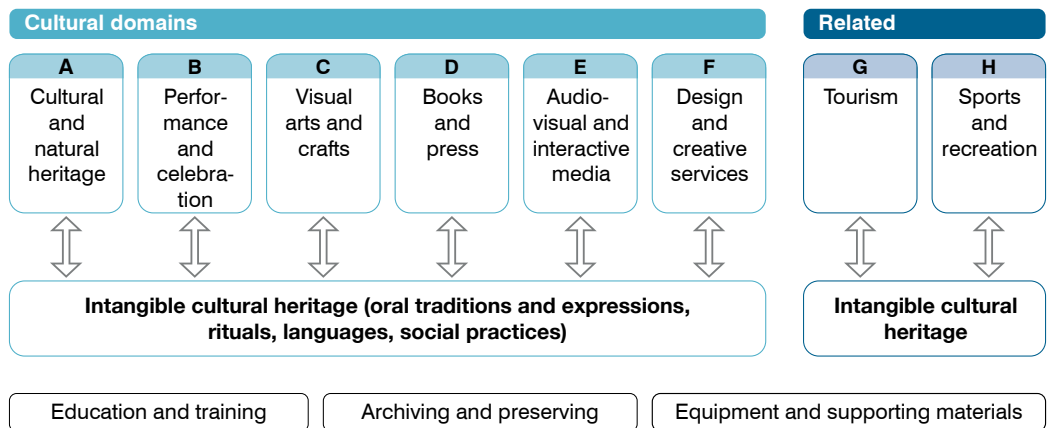


**Figure 1.6:** Culture cycle

<sup>40</sup> For a detailed discussion of the culture cycle see *The 2009 UNESCO Framework for Cultural Statistics* (2009).

The culture cycle has five stages, as shown in Figure 1.6. The first stage includes the people who are involved in creation, for example sculptors, writers and design companies, in addition to one-off producers of crafts and fine arts. The second stage covers production, such as television programmes and the tools needed for the production of culture, such as the manufacture of musical instruments and printing. The third stage consists of distribution, that is, of bringing the cultural goods or events to consumers and exhibitors. The fourth stage covers exhibition and refers, among other things, to places of consumption, as in the case of cinemas, theatres, opera houses, museums and cultural festivals. The fifth stage covers consumption and participation by consumers in cultural activities, such as watching television, listening to the radio, visiting museums, reading books and dancing. Various goods and services are delivered directly from the persons who produce them to consumers, including delivery through digital technology.

The culture cycle assumes interconnections across these activities and feedback, where consumption can inspire new creation. Individuals can also create and consume at the same time, as in the case of blogs or postings on Facebook or other social media. The culture cycle can apply to individual areas, where the entire process takes place, or it can extend to the entire world. The domains of the new classification scheme in statistics are shown in Figure 1.7.<sup>41</sup>



**Figure 1.7:** Framework for cultural statistics domains

<sup>41</sup> See *The 2009 UNESCO Framework for Cultural Statistics* (2009).

There are six cultural domains in the new classification scheme, in addition to two related domains, as shown in Figure 1.7, each of which has an interactive impact on cultural heritage. At the bottom of Figure 1.7 are three domains that extend across all the domains, that is, they are 'transversal': education and training, archiving and preserving, and equipment and supporting materials.

Domain A, Cultural and natural heritage, includes museums, archaeological and historical sites, cultural landscapes and natural heritage. This category includes buildings and monuments with a cultural reference. Cultural landscape represents the combined works of human beings and nature and expresses the long-standing relationship between people and their natural environment. Natural heritage encompasses geological formations and natural features that have scientific value and require preservation because of their natural beauty or other features. Collection and preservation in museums also fall into this category.

Domain B, Performance and celebration, includes the performing arts, music and stage performances, including festivals and fairs, and everyone who participates in the performance of arts of this kind, whether professionals or amateurs.

Domain C encompasses arts and crafts, including paintings, sculptures and photographs. Domain D, books and press, includes books, newspapers, magazines and printing in general, libraries, including electronic libraries, and book fairs.

Domain E, audio-visual and interactive media, includes radio and television broadcasting, including films, television shows and other visual material, as well as the social media. This domain includes both participation and passive reception, encompassing computer games and video games and their software, whether interactive or not.

Domain F, Design and creative services, includes fashion, graphic design, interior design, landscaping, advertisements and architectural services.

**Charles Chaplin** was born in Britain in 1889 and died in 1977. Chaplin was a pioneer in many fields. Not only a comedic actor and a director, Chaplin also wrote the script to every one of his own films. His numerous appearances in his role as a tramp have long since become classic in cinema history. Chaplin founded United Artists alongside other actors, a company which later became an empire, and he played an active role in protecting the interests of individuals employed in the film industry. Chaplin was a fierce opponent of the political extremism that gained momentum in Europe and eventually led to the Second World War. He produced *The Great Dictator* as a polemic against Nazism and became himself a victim of McCarthyism. Chaplin received numerous honours and was knighted in 1975.

The Intangible Cultural Heritage domain is defined as the practices, representations, expressions, knowledge, skills and their associated instruments, objects, artefacts and cultural space, that communities, groups and, in some cases, individuals recognise as part of their cultural heritage.

Education and training in this context does not include all education, but only education that concerns the dissemination of cultural values or cultural features, which is important for culture and cultural activities. Archiving and preserving include, among other things, the collection and classification of documents and the preservation of paintings. Equipment and supporting materials include the Internet, computers and information technology in general. Research is allocated to each respective domain.

Two related domains, Sports and Recreation and Tourism, are set apart from the domains since they are not as such regarded as cultural activities, although cultural tourism is regarded as constituting culture, as in the case of guided tours and tourist services, hospitality and accommodation. Sports include both professional and amateur sports, outdoors activities and physical training. Recreation also includes gambling, lotteries and various leisure activities, such as amusement parks and theme parks.

This new classification framework for economic statistics in culture has been adapted to the principal current systems, such as the ISIC (International Standard Industrial Classification), and it may be expected to gain increasing global recognition as earlier methods are incorporated, adapted and improved. The new framework also addresses the cultural domains holistically and focuses on consistency and context, which has not been done in as clear a manner until recently.



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## 2. Supply and demand

The fundamental features of an economy are markets that are characterised by supply and demand, two of the most fundamental concepts of economics. Supply is the quantity of products (such as books and CDs) and services (such as transportation) that firms are able and prepared to sell. Demand refers to the quantity of products and services that buyers are willing to pay for. What needs to be explained here are the forces that shape the demand for cultural goods and the mechanisms that underlie supply, or, simply put, how demand is met by supply. The market is the tool of trade and comprises the nexus where supply and demand meet. An equilibrium is achieved in a market when supply meets demand. In this section the principles of supply and demand in classical economic theory will first be examined and then how cultural goods respond to these principles will be explained. Simply put, do we choose how we spend our money on cultural goods in much the same way as we buy washing machines, lawn mowers, and coffee pots? Cultural goods are often subject to intellectual property rights and are often ‘experience products’; that is, their consumption consists in experiencing a certain pleasure, as in the case of listening to music in a concert hall or watching a play in a theatre.

### 2.1 Demand

#### 2.1.1 Demand function and price elasticity

There is a close relationship between the price of and demand for a product or service. Consumer demand is not determined by price alone, but also by the buyer’s income, the price of similar products, taste or expectations. Equation 2.1 shows a simple demand function, where demand (D) is a function of several factors.

**Equation 2.1:**  $D = f$  (product price, price of related products, advertisements, quality of product, expectations, taste)

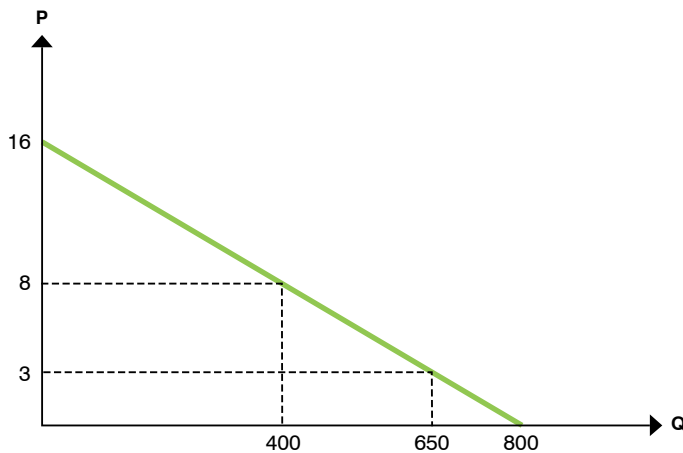


To a large extent demand is dependent on taste, an important factor in determining the use or usefulness of a product for consumers. Rational consumers have a use for their various purchases, but most people's acquisitions are dictated by budget constraints. Choices therefore have to be made. And it is not always just income that limits possibilities, but also time constraints, since most people lack the time to do everything they can afford.<sup>1</sup>

In economics, the demand function is often simplified by assuming that demand is dependent exclusively on product price (P) and that the impact of other factors is fixed. The demand function is then shown as follows, in Equation 2.2:

**Equation 2.2:**  $D = f(P)$

Equation 2.2 states that the quantity of goods in demand is dependent on price (P). This relationship is reflected in a model that is a simple and condensed depiction of reality. This model is used to explain the traditional factors that influence demand for cultural goods and is equally applicable to other goods and services. The more prices rise, the smaller the quantity in demand, and the lower the price the greater the quantity that consumers wish to buy. This context, called the law of demand, is shown in Figure 2.1.

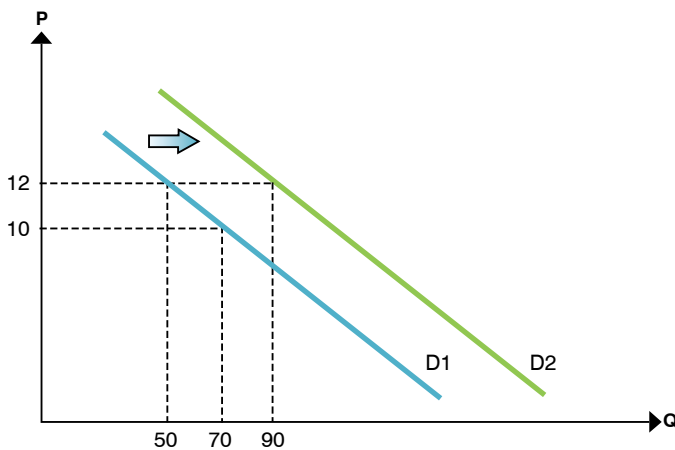


**Figure 2.1:** Demand curve

<sup>1</sup> Demand in the cultural sectors has been widely discussed, e.g. by Peacock and Rizzo (1994), Cowen (1996), Caves (2002), and Towse (2003).

In Figure 2.1 the quantity of products ( $Q$ ) is shown on the x-axis (the horizontal axis), while the price of products ( $P$ ) is shown on the y-axis (the vertical axis). The demand curve slopes to the right because if the price of a product falls, the quantity in demand increases. When the price is higher than \$16 per unit, there is no demand.<sup>2</sup> When the price is \$8 per unit, the quantity in demand is 400 units, and at the price of \$3 per unit, the quantity in demand is 650 units. Figure 2.1 assumes a linear connection between quantity and price. The lower the price of admission to cinemas, for instance, the greater the number of people queuing up to see the films. A deciding factor here, however, is what it costs to see or do other things, so that cultural goods are in constant competition with other goods at the same time as they compete with one another. Consumers choose what they want to do, including whether they wish to buy the goods on offer or not.

Figure 2.2 shows the demand curve, and changes in the curve, with  $Q$  denoting quantity and  $P$  denoting price. The price on the y-axis is the price to consumers.



**Figure 2.2:** The demand curve and its changes

A clear distinction has to be drawn between whether the movement is along the demand curve or whether the demand curve is shifted. If demand curve  $D1$  applies and the price is \$12 per unit, the goods in demand are 50 units. If the price falls to \$10 per unit, the goods in demand will be 70 units, all things being equal. This is movement along the demand curve.

<sup>2</sup> Prices are expressed in US dollars.

However, it is possible that other factors of demand besides price will change. In that case the demand curve shifts. If consumers' disposable income increases, then consumers will obviously have more money to spend and will be prepared to buy more for the same price. This creates a new demand curve, which is identified as D2 and lies to the right of the first curve. Figure 2.2 shows that when D2 applies, 90 units will be purchased if the price is \$12 per unit.

The demand curve can change in a number of ways. It can shift to the left with shrinking disposable income. It can rotate and become flatter, which means that consumers are more sensitive to price changes than before. There can be various reasons for such changes. Firstly, the demand curve can change as a result of changes in income. If disposable income increases, general demand will increase in the absence of other changes even if the price of goods remains unchanged. An increase in disposable income, therefore, has the effect that the demand curve shifts to the right, from D1 to D2 in Figure 2.2. This applies to what we call 'normal goods'. But there is another type of goods which are known as 'inferior goods'. These are goods that consumers will buy less of if income increases. To give an example, shoe repairs will decrease when income rises, since people will dispose of old shoes and buy new ones.

Secondly, changes in the demand curve result from a change in the price of a substitute good. Substitute goods are those that can replace other goods, like pens and pencils, labour and machinery, where each member of a pair can be substituted for the other member. In the case of two substitute goods, such as staged plays and motion pictures, if the price of admission to the theatre rises the demand for plays will fall, and consumers will go to the cinema instead. The demand for films would, therefore, increase even if the price of tickets to the cinema remained unchanged.

Thirdly, a change can occur in the price of complementary goods, that is, goods that is used together, such as pens and paper and bread and butter. If the price of opera admissions falls, the demand for them rises. This change has the side effect that the demand for opera programmes increases even though their price remains steady.

Fourthly, changes may occur in consumer expectations. If consumers believe that the price of goods will increase in the near future, the demand for them will increase before the occurrence of the price change. An announcement of a reduction in import duties on CDs will

have the effect that demand for them will fall sharply until the reduction has taken effect. The impending change shifts the demand curve to the left; that is, consumers will want to buy lesser quantities at their pre-reduction price.

Fifthly, a change in consumer tastes occasions a new demand. This alteration can happen quite suddenly, as when the demand for products such as clothing or a piece of music, which are subject to fashion trends, shifts. This moves the demand curve to the right or left, depending on the nature of the change in taste or fashion. This principle can be quite common in the cultural sector.

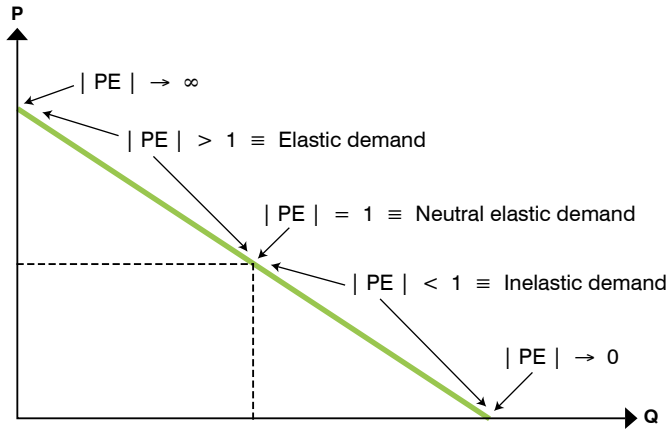
It is important to understand how the quantity in demand changes proportionally when prices change by a specific percentage, for example by 10%. Such changes are explained by using the concept of 'price elasticity of demand'. Price elasticity is a measure of the sensitivity of a market to proportional price changes; it has no unit of measure but describes the elasticity of the market. Price elasticity is defined as the proportional change that occurs in the quantity that is in demand if the price of a good changes by 1%. If the price of a good increases by 10% and the quantity demanded of the good falls by 20%, the elasticity of that good is equal to  $-20/10$ , or  $-2$ . By the same token, a reduction in price results in an increase in quantity. Although the numerical value of elasticity is normally negative, the minus sign is usually ignored. Elasticity differs depending on the nature of a good. Goods which are sensitive to price changes have an elastic demand. Conversely, if the quantity in demand changes only slightly when prices change, the demand is inelastic.

The elasticity of necessary goods is normally limited. People require a certain amount of milk, e.g., for children, almost regardless of cost. The demand for seats on passenger flights, however, can change radically with changes in price. Luxury goods are particularly elastic, although defining luxury goods can be problematic: a luxury item for one consumer may be daily fare for a more affluent consumer. Substitute goods are more

**Confucius** was born in 551 B.C. and died in 479 B.C. He was China's most famous thinker, together with Lao Tse, and his influence is still felt in the culture of this most populous nation of the world. Confucius died ten years before the birth of Socrates. His teachings became official government policy and a sort of set of moral precepts when the Chinese established an empire in 221 B.C., which stood for over two thousand years. The Chinese became a superpower long before any other nation. Confucius was rather conservative and a proponent of family loyalty and respect for elders. One of his precepts was „Do not do to others what you do not want done to yourself“. Confucius and his teachings had extensive influence on the culture of a number of countries in the Far East.

sensitive to price changes than other goods and may be termed elastic. The reason is that it is easy for consumers to refocus their demands on substitute goods.<sup>3</sup>

A correlation between price elasticity and the demand curve is shown in Figure 2.3:



**Figure 2.3:** Correlation between demand elasticity and the demand curve

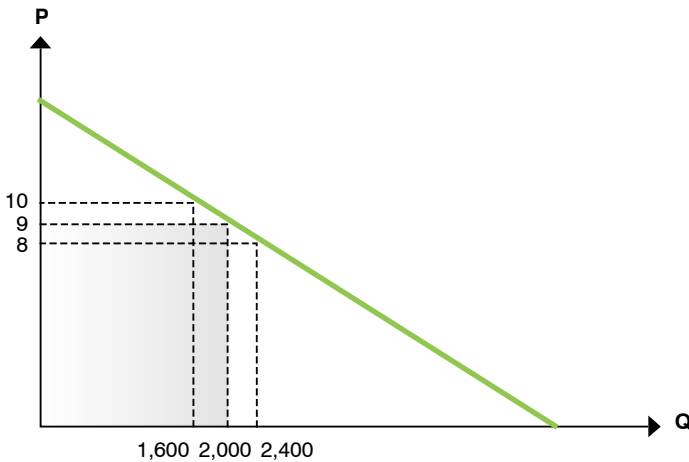
The numerical value of price elasticity is greatest at the highest price and then it falls, as shown in Figure 2.3. The numerical value of price elasticity is the figure ‘less than 1’ in the lower part of the demand curve, which means that the demand is less elastic.

Elasticity is an important tool for business enterprises and persons in economic management for understanding the impact of changes in circumstances. For instance, elasticity can be used to determine the effect of a 10% increase in the price of a book on the quantity demanded, or of the reduction in price by 5% on an increase in revenue of an art gallery. This relationship is indicated in the following illustration:

<sup>3</sup> There are also goods whose change in price has virtually no impact on the quantity demanded. This applies to goods used in small quantities (such as table salt), but which are nevertheless indispensable. Even though the price of table salt increases marginally (or even significantly), consumer demand scarcely changes. Because consumers buy table salt in small amounts, a very small part of their disposable income is spent on this commodity. Demand for goods of this kind is virtually inelastic and the numerical value of price elasticity is close to zero. This remark is added for the sake of completeness in discussing price elasticity and has little or no relevance to cultural goods.

### Illustration 2: Deciding the price of admission to a museum

The director of a museum finds himself in financial difficulties and considers raising the price of admission to generate increased revenue. He increases the price of admission from \$9 to \$10, but to his surprise the museum's revenue actually falls. He then contacts a cultural economist and asks him to explain this situation and provide expert advice regarding the price of admission. The cultural economist estimates the demand curve of the museum and plots it in a chart, as shown in Figure 2.4.



**Figure 2.4:** The demand curve of the museum in Illustration 2

If the price of admission is \$9 and the number of sold admissions is 2,000, as shown in Figure 2.4, where price (P) is shown on the y-axis, while quantity (Q) is shown on the x-axis, and the revenue of the museum is the price multiplied by the quantity, the revenue will be  $9 \cdot 2,000$ , or \$18,000. If the price is raised to \$10, the number of admissions sold falls to 1,600, as shown in Figure 2.4. This means that revenue becomes  $10 \cdot 1,600$ , or \$16,000, down by \$2,000 from the earlier revenue.

The cultural economist now explores what would happen if the museum director were to reduce the price from \$9 per admission to \$8. This would increase the number of visitors to 2,400, as shown in Figure 2.4. The revenue of the museum would then be  $8 \cdot 2,400$ , or \$19,200, up by \$1,200 from the original figure.

The cultural economist, therefore, advises the museum director to reduce the price instead of raising it, because the reduction will increase revenue. However, reducing the price applies only in the more elastic part of the demand curve, where the proportional reduction in price would increase the proportional quantity in excess of the proportional price reduction, thereby increasing revenue. In the inelastic part of the curve (that is, low on the curve in Figure 2.4 at a relatively low price) a proportional increase in price would reduce the proportional quantity less than the proportional increase in price, thereby increasing revenue. In such cases management needs to know how consumers will respond to changes in price; that is, it needs to know the elasticity of demand. Simply raising prices on the assumption that such a move will inevitably increase revenue is thus an ill-advised policy.

The concept of elasticity is used in economics not only to assess the effects of proportional price changes on proportional demand, but also for other purposes. Income elasticity, for instance, predicts how much demand will fall if the income of an individual decreases by 10%. Advertising elasticity measures how much demand will rise if advertising expenditures are increased by 1%.

Changes in the price of one good can affect the demand for other goods. This is expressed by using the concept of cross-price elasticity, which refers to the proportional change in quantity of one good (B) divided by the proportional change in price of the good (A) that caused the change. If the price of cinema admission (A) increases by 10% and the demand for theatre tickets (B) increases by 20%, the cross-price elasticity of goods A and B when the price of A changes is equal to  $20/10$ , or 2.

Cross-price elasticity is positive for substitute goods. If the price of any good A is reduced, the quantity demanded of the good A increases, and since the good B replaces good A, the demand for the good B is reduced. These are two negative changes, so that the cross-price elastic-

ity is in this case also positive. The extent of the cross-price elasticity reflects the strength of the link between substitute goods.

The opposite applies to complementary goods. If the price of CDs rises, this will of course reduce the demanded quantity of CDs, but since CDs and CD players are used together the demand for players will also fall. Cross-price elasticity is, therefore, negative for complementary goods. The extent of the impact of the cross-price elasticity will then depend on the extent to which the goods are used together.

It is important for business enterprises to understand cross-price elasticity, that is, the impact on their products when other firms change their prices, because business executives must grasp the notion in order to plan their pricing strategy. If a firm is operating in a market comprising a variety of substitute

**Leonardo da Vinci** was born in 1452 in Italy and died in 1519. An acclaimed genius, he is regarded as the greatest polymath of all times. He is one of the foremost painters of history and his portrait, the *Mona Lisa*, preserved in the Louvre in Paris, has been acclaimed for centuries. In fact, this applies in general to his paintings, such as *The Last Supper*, preserved in the Convent of Santa Maria delle Grazie, Milan. Da Vinci was also an inventor and many of his drawings have survived, showing outstanding creative power and vision. Da Vinci did a great deal of work for the Medici family of Florence and the Sforza family of Milan, families that governed their respective city states in great pomp. He was also a military advisor and designed a number of war machines, in addition to working for the Pope in Rome. Da Vinci spent his last years in the court of King Francis I of France, a fervent admirer of his genius.

goods, as is common in the cultural marketplace, knowledge of cross-price elasticity – which describes an enterprise’s competitive position in the marketplace – is absolutely essential. If cross-price elasticity is positive and relatively extensive, then a company needs to be cautious in its pricing strategy and sales in order to avoid losing business to competitors.

### 2.1.2 Consumption and consumer behaviour

Proverbially, we are what we eat, and our working and sleeping habits can also claim to be a partial measure of the person. But no one lives by bread alone – nor by grinding away at the coalface – and we all share a demand for entertainment, recreation and downtime, whether in the form of watching films, engaging in sports, attending the theatre, or listening to music. The use of leisure time is determined by individual choice, but whatever the choice, it is a fair bet that it will involve culture in one form or another, which means that as free time has increased, so has the consumption of culture.

The cultural industry, where cultural goods dominate, forms a part of the creative industry. A great deal more money is spent on culture than is usually thought. In 2011 U.S. households used an average of 8% of their total spending on culture and recreation. For comparison, about 9% of household spending was on transport, including the running costs of cars, and 6% on food and non-alcoholic beverages. The corresponding figures in the U.K. for the same period was 8% on culture and recreation, 10% on transport and 9% on food and non-alcoholic beverages. In the Nordic Countries at the same time, about 8% of household spending was on culture and recreation, 10% on transport and 9% on food and non-alcoholic beverages. Thus the proportions are similar for all these countries and show that spending on culture and recreation is significant in comparison with other categories of spending.<sup>4</sup> Consumption of culture differs, however, depending on income and age group. As income grows, often in line with increasing age up to a certain limit, increasing amounts are spent on culture, since the elderly will frequently have more time to enjoy culture.

In economics it is generally assumed that supply will be driven by consumer tastes and attitudes. Consumers decide what products they will buy. In the cultural industry, however, decisions on what gets produced often depend on the subjective opinion of the individual in charge of

<sup>4</sup> For further information on the division of household spending see UNdata (2014).



the production, and these decisions are grounded in the knowledge possessed by that person. The result is not always what the market wants, as countless stories of highly touted musical stage productions and high-budget movies attest. Among hard-headed businessmen, almost no investment is riskier than backing theatre productions.

In the performing arts, which include the theatre, dance, opera and classical music, the rule applies that the same aficionados will frequent the branch of arts that interests them the most. Of these four branches of the performing arts in the United Kingdom, the theatre attracts the greatest attendance, followed by classical music, opera and, finally, dance.<sup>5</sup>

In self-styled elite circles of the performing arts modern opera – especially when performed in the languages in which it was originally written – enjoys the reputation, perhaps not exclusively among opera buffs, as having great cultural value, but its low economic value suffers from a lack of demand, rarity of performances and scarcity of capital. On the other hand, a soap opera – the name itself betrays a bias against the genre – could by some be regarded as having little cultural value, while it may have significant economic value due to extensive viewing, significant sales and abundance of capital. This reflects the differences in individual attitudes, which play a significant role in culture.

High cultural value and extensive economic activity do not always go hand in hand. For some things there simply is not a great deal of demand, and this lack is reflected in small volumes of production and limited sales. However, regardless of sales an artistic work or product may have significant cultural value. Archaeological artefacts are one example. However, valuation of this kind differs from one society to the next, and the same yardstick cannot be used in all circumstances. It is not always possible to explain everything that concerns art. What, for instance, does red or blue in a painting signify, and does it matter? Such matters are impossible to explain in the abstract, and it is the picture as a whole that is observed and assessed in its cultural setting.

In economics, willingness to pay reflects the price that people are prepared to pay for goods and services. This assessment may be higher than the price that needs to be paid for a product. The difference between willingness to pay and price is referred to as ‘consumer surplus’. Consumer surplus also reflects the time that people determine as their own

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<sup>5</sup> For a discussion of this British survey of attendance of artistic events see Towse (2010).

time, which is used to enjoy a cultural event, such as a play, including attendant costs, for example what it costs for transport to and from the theatre. Willingness to pay can be measured by surveys to discover what people would be willing to pay for goods and services. Willingness to pay can also be clearly expressed at auctions, and it is also reflected in the price of admission, for example, to museums. In other cases, it can be more difficult to discover what people are prepared to pay for various elements of culture.<sup>6</sup>

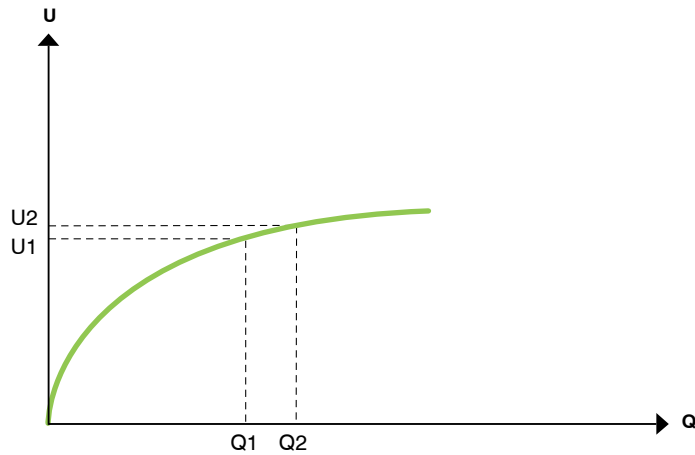
Willingness to pay is not always clear in the cultural sector, as people are often unsure what they are willing to pay for a product. This insecurity can result from a lack of the necessary knowledge or information about what they can expect to receive for money spent (is the play/film good or bad?), or from the conflicting information on offer ('Smith's performance has the greatest potential for improvement I have seen in many a year'/'Smith was truly born for this role'). Experienced theatregoers tend to rely on critics as to the plays they attend, whereas outside of large world cultural capitals (Paris, New York, Berlin), many moviegoers tend to respond mainly to the movie industry's advertising campaigns, especially those touting highly paid stars when they choose what movies to see. Indeed, one of the make-or-break financial aspects of the movie industry is how much revenue a movie generates in its first weekend of distribution, which cannot be much affected by critical reception and appears to be the direct result of energetic and hugely expensive advertising.<sup>7</sup>

In economics it is assumed that consumers want to maximise the utility that they derive from the products they buy. Consumer demand for a product will depend on its usability, and the more a consumer consumes of a product, the greater its utility, as shown in Figure 2.5.

<sup>6</sup> For a discussion of cultural consumption and willingness to pay see, e.g., Frey (1994) and Frey (2008).

<sup>7</sup> See, for e.g., Simonoff and Sparrow (2000).

**John Kenneth Galbraith** was born in 1908 in Canada and died in 2006. He was extremely influential in the public discourse on politics and economics. He was also one of the first to write about cultural economics. He was somewhat to the left of centre in his politics and published a number of books where, among other things, he criticised unchecked market capitalism. Galbraith was a professor at Harvard University and appointed by President John F. Kennedy as the U.S. ambassador to India. He subsequently returned to Harvard. He participated actively in American politics and was involved in a number of presidential elections as one of the chief advisors of presidential candidates of the Democratic Party. He exerted great influence on the American political discourse and for a time he was the best known economist in the world. Galbraith received a number of awards from the United States government and held honorary doctorates at a number of universities across the world.

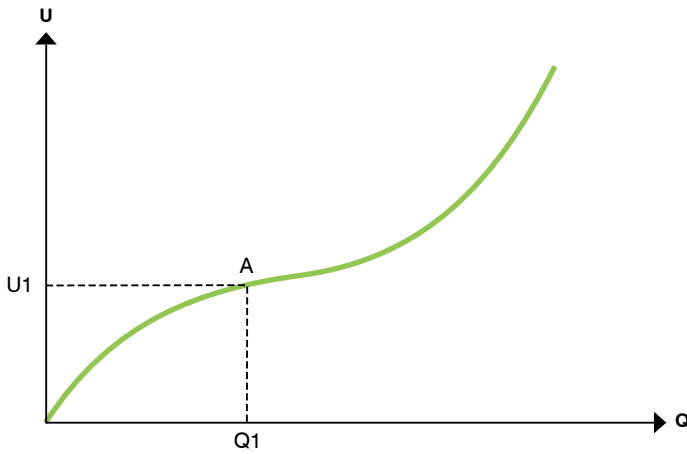


**Figure 2.5:** Traditional utility function

The norm in consumer utility is that as consumers own more of a specific good, their needs will gradually become satiated. Figure 2.5 shows that if there is an increase in quantity from  $Q1$  to  $Q2$  there will be a relatively small increase in utility, that is, from  $U1$  to  $U2$ . To give an example, people will not accumulate endless quantities of clothes.<sup>8</sup> However, this economic law need not apply universally with regard to cultural goods, for increased consumption of culture will often generate increased consumer interest in culture and thereby increased demand. A person who listens to music frequently will develop a more advanced taste for music and, as a result, will often want to listen to more music. Thus, demand is increased by increased consumption, which seems to violate an economic principle.<sup>9</sup> Figure 2.6 shows this relationship.

<sup>8</sup> Indeed, Imelda Marcos's legendary shoe collection (alleged to be 3,000 pairs), an obvious aberration of this economic law, was emblematic of the Marcos kleptocracy.

<sup>9</sup> How supply increases with increased consumption was initially suggested in Becker and Murphy (1988).



**Figure 2.6:** Relationship between quantity and utility in cultural consumption

Figure 2.6 shows that utility increases with increasing quantity, but the increase is reduced up to the quantity of  $Q_1$  and the utility  $U_1$ . This is known in economics as diminishing marginal utility. After the quantity  $Q_1$  utility increases significantly, this part of the chart depicts what is known as increasing marginal utility. After the quantity  $Q_1$  the consumer's taste has changed so that he or she now enjoys music or films, for instance, more after the increase, resulting in a desire to increase consumption. This change means that there is some sort of learning curve at work: increased knowledge and consumption beyond a certain quantity of goods and services increases demand still further.

Consumers choose between types of goods and services, and they determine their own needs for themselves. People have different tastes and different incomes, and these factors influence their behaviour. Consumers' desires can also change over time as a result of any number of influences, such as religion and tradition, which themselves are also elements of culture. The basic idea is that individuals will try to make the most of their possibilities in their own interest. All participants in the economy will attempt to bring about their own optimal results.

Consumers' desires are manifested in their evaluations. As in the case of cultural events, the assessment of the individual is dominant. In economics three assumptions are made regarding the tastes and behaviour of consumers, from which conclusions can be drawn. The first assumption is that consumers will know what they want if they have a choice between two or more options. This assumption means that it is understood that a

consumer has the option of choosing between two types of product and evaluating their respective utility.

The second assumption is that consumers will choose more over less; that is, they will prefer a greater quantity to a smaller quantity of goods. This claim seems obvious, but bearing it in mind significantly facilitates the extrapolation of various aspects of consumer behaviour in economics. The third assumption is that if product A is preferred to product B and product B is preferred to product C, then product A will be preferred to product C. This approach is used to establish an order of precedence for individuals. However, this does not always apply to cultural goods. If song A is preferred to song B, and song B is preferred to song C it is not certain at all that song A will be preferred to song C. A similar syllogism applies to paintings and other art. It is, therefore, not always possible to use the same basic models to explain behaviour in cultural economics and general economics.

The price or value of cultural goods is complex. It can be determined, for instance, by the accumulation of knowledge and experience, and valuation in the past or present can influence consumption in the future. To give an example, major old works of art have often been valued based on their history and their evaluation over the centuries. The price in the marketplace is, therefore, not sufficient, in and of itself, to ascertain the value of cultural goods. However, price is often the only measure available, and there are also those who believe that the market price is the only useful measure of the value of a work of art.<sup>10</sup>

## 2.2 Supply

### 2.2.1 Factors of production

We fulfil our needs through production, and production requires resources. In the case of a poem, for example, paper, pen and a fertile creative imagination would be the basic resources needed. Both goods and services are produced in the context of an economy. Goods can be preserved as inventory over longer or shorter period of times, as in the case of cars, food, beverages, and fashion items. Service, however, cannot be preserved, as the use or benefit of a service takes place as soon as it is provided, as in the case of a visit to a hairdresser, where the use takes

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<sup>10</sup> For a discussion of the market price as the only measure of the price of a work of art see, e.g., Robertson (2005) and Robertson and Chong (2008).

place during the time that the hairdresser styles or cuts the customer's hair. However, goods and services are often inextricably linked, as in the case of dinner at a restaurant, where the food constitutes goods, but the setting and presentation are service. Eating out is an experience, and at the same time it meets an individual's need for food; this combination constitutes the consumer's utility. All of these factors apply to cultural goods in the same way as to other forms of economic production.

Production is linked to technological, economic and organisational conditions. Technical problems in production relate to the technical possibilities of producing a certain good. If the objective of an undertaking is to maximise profit, then the factors of production need to be used as cheaply as possible if the selling price of the product is known. Organisation relating to matters such as rights of title to production factors or intellectual property rights in the case of the cultural industry is also an important element.

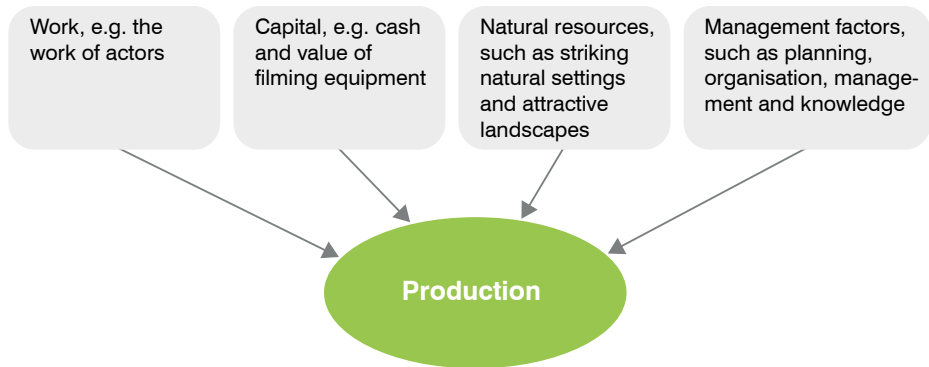
The connection between production and production factors is described using what is known as a production function, which shows what quantity of a product can be made using a certain quantity of production factors or resources. Changes in the production function can occur for a number of reasons. The number of performances of a play can be increased, films can be distributed in different ways or an entirely new and improved organisation can be introduced, for instance by adding shift work, with the obvious limitation that there are only twenty-four hours in a day.

If there are two production factors, there are two possible relationships between them. On the one hand, the production factors can replace one another. These are substitute factors of production. Examples could include labour and machines. Another possible relationship is that the factors may be necessary in a certain proportion; for example, one musical instrument and one musician. These are related factors of production.

Produced goods can be analysed from a number of viewpoints. They can be categorised by economic factors, the nature of their demand, social viewpoints and technological conditions, for instance whether a single unit is being produced, such as a building, or a product is being mass-produced, as in the case of CDs or books.

Sometimes production involves only a single type of goods, as in the case of an electric power station which produces only electricity. In other cases it may be possible to produce a number of products which may be closely related. A dairy, for instance, can produce milk in a number of forms, such as butter, yoghurt and cream. The common denominator in the production is milk in some form, which is the starting material for all the products.

There are four kinds of factors of production that are needed for the production of goods and services: work, capital, natural resources and management factors such as planning, organisation, management and knowledge, as shown in Figure 2.7, which uses the example of the production of a motion picture.



**Figure 2.7:** Links between factors of production and production

Filming a motion picture requires specialised work, such as the work of actors, directors and a film crew; it also requires capital to meet the costs of production; it will often require natural resources, such as picturesque landscapes and the sounds that accompany them; finally, the management factors of production are fundamental features of contemporary business operations. A plan is needed to indicate who is to do what, how and when. Proper organisation is needed in the business, and contemporary business management relies on specialised knowledge involving the movie industry: the best actors to be cast for the roles in the films to be produced, the best natural settings, the best casting companies, as well as the nuts and bolts of financing any business venture. Most other factors of production in the culture sector are similar to those illustrated in Figure 2.7 for the motion picture industry.

Supply is subject to principles similar to those governing demand. Supply is the quantity of goods produced by a firm and offered for sale and is subject to several factors, such as the price of the goods, the price of similar goods, technological advances and the price of resources. Technology and technological advances are a dominant factor in supply: if there is a technological advance that reduces price, this development will lead to increased supply, since the production costs accruing to a business will fall. If, on the other hand, the price of resources increases, supply will decrease as the cost of the business increases. If the cost of a product increases, it becomes less attractive to consumers than other products, and business firms will, therefore, tend to cut the quantity in supply. The price elasticity of supply describes the effect of potential price changes on the proportional change in the quantity in supply in a similar manner as that described previously in connection with the price elasticity of demand.

It is comparison with other goods and other options that decides the behaviour of consumers and business firms in the economy, as illustrated by the principle of opportunity cost. It is not the price itself of goods that dictates consumer demand or supply by firms, but the price in comparison with the price of other goods; that is, it is the relative price that determines the behaviour of participants in the economy. Also, the number of competitors has an impact on supply, not only because competition will drive prices down, but also for the simple reason that more goods will be produced, and market conditions in general, e.g. employment, wages, inflation, interest rates etc., will also have an effect.

The supply function describes supply as a function of factors of influence. Equation 2.3 shows a simple supply (S) function of product A.

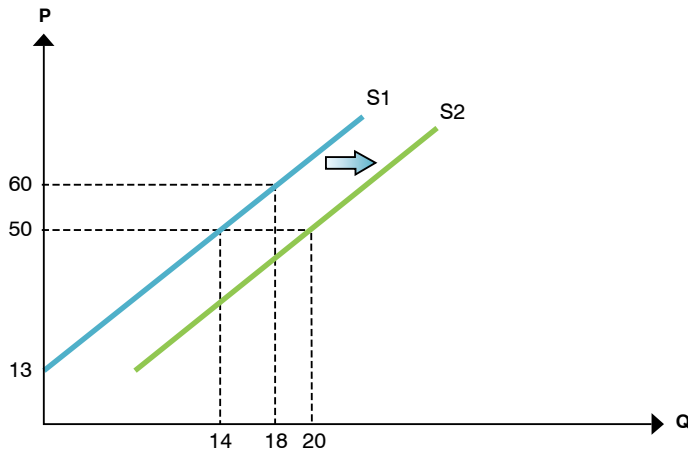
**Equation 2.3:**  $S = f$  (price of product A, price of related products, price of resources, technology, expectations)

Equation 2.3 is not exhaustive, and there are other factors that can affect supply. If all the factors of influence in Equation 2.3 are known and it is possible to assess their impact on supply, the function in Equation 2.3 describes possible changes. As in the case of demand, as discussed above, the presentation is simplified, and it is assumed that the influence of all factors other than the selling price are constant. In those circumstances supply as a function of selling price is shown in Equation 2.4.



**Equation 2.4:**  $S = f(P)$ 

The normal rule is that if the price increases, supply will increase, because a firm will expect greater profit at higher prices with increased sales. Figure 2.8 shows this correlation, where the supply curve of a business over a brief period is observed.



**Figure 2.8:** The supply curve and its changes

Figure 2.8 shows that if supply curve S1 applies and the price is \$50/unit, firms will offer the quantity of 14 units. If the price for some reason increases to \$60/unit, the supply will increase from 14 units to 18 units, all other things being equal. The reason is that with the price increase, the product will become relatively more expensive than other products and will, therefore, be more profitable than other products that the firm manufactures. This results in changes, so that the manufacturers of other products will now begin to produce and offer this relatively more profitable product in the place of other products, and current manufacturers will also increase their supply. This combination of changes constitutes the total impact. Although the number of firms may not change anything in their production and sales despite a price increase, the general effect of a price increase is that it will become more profitable to produce that product rather than others. A change in price results in a movement along the supply curve.

Figure 2.8 shows that if the price is lower than \$13/unit, there will be no supply. This zero supply reflects the principle that the price has to reach a certain minimum before the manufacture of a product and its

entry in the market become economically viable. Launching any product requires planning, which in turn entails costs, so that from a short-term perspective, fixed costs will accrue; a certain minimum price has to be reached for the supply of a product to be economically feasible.

And the supply curve can shift as a result of changed circumstances: factors of influence other than the price of the product change. Firstly, supply will normally increase as a result of decreasing production cost if the cost of resources falls. An increase in supply will have the effect that the supply curve shifts to the right, with the new supply curve at  $S_2$ , as shown in Figure 2.10. Assuming that supply curve  $S_2$  applies, the quantity of 20 units is offered if the price is \$50/unit. The decrease in price of resources has, therefore, had the effect of increasing supply, because the product in comparison with other products becomes cheaper to produce.

Secondly, the supply curve can shift as a result of changes in technology. A firm's supply is based, among other things, on technology. If a firm (or an industry as a whole) can take advantage of technological advances – for instance if a relatively inexpensive machine that reduces labour costs appears on the market – then production costs will decrease and the product will increase its profits. A prime example is the price of computers, which has fallen steadily in recent years and decades as a result of technological advances.

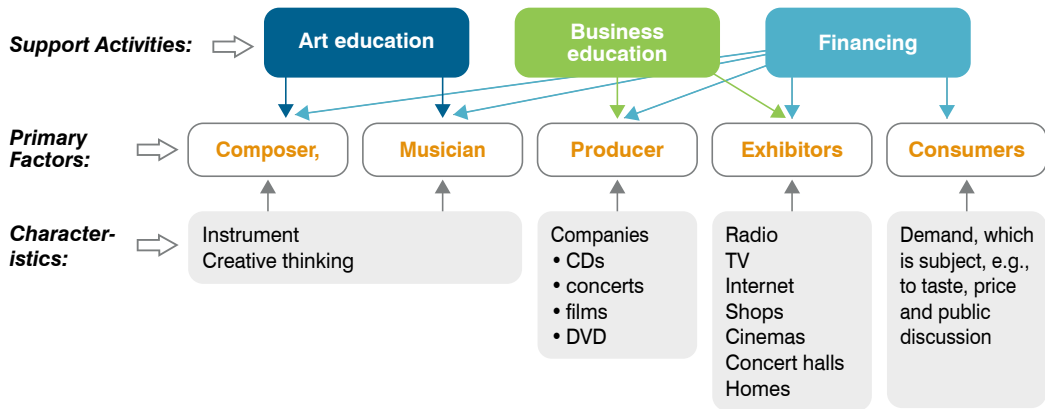
Thirdly, changes in expectations will affect supply. Just as in the case of demand, proposed changes, for instance in taxation, will have the effect of changing supply. Here time is a significant factor affecting expectations. In the very short term there is little that a firm can do to increase its supply. In the long term it may be possible to add production machinery. In the long term new companies can also gain footholds in a new sector of the economy while others may cease their operation. In the very short term supply will not change much but looking to the long term all factors can change and supply can thereby change significantly.

### **2.2.2** The value chain

The value chain in the production of cultural goods depicts a process of production, distribution and consumption, where value is added at each stage of the process. Creative thinking is one of the factors of production. The chain can be quite simple, as in the case of a busker playing a musical instrument in the street and collecting coins in a cap. At the other end could be the complex process of staging an opera, which eventually finds

its way to the Internet, where it is enjoyed by consumers (often without paying) after the music has been uploaded by legal or illegal means. The value chain in culture can, therefore, be varied and complex.

Value creation in the cultural industry takes place in several stages that can be illustrated in a chart of a value chain in the music industry that depicts its primary factors, characteristics and support activities, as shown in Figure 2.9.



**Figure 2.9:** The value chain in the music industry

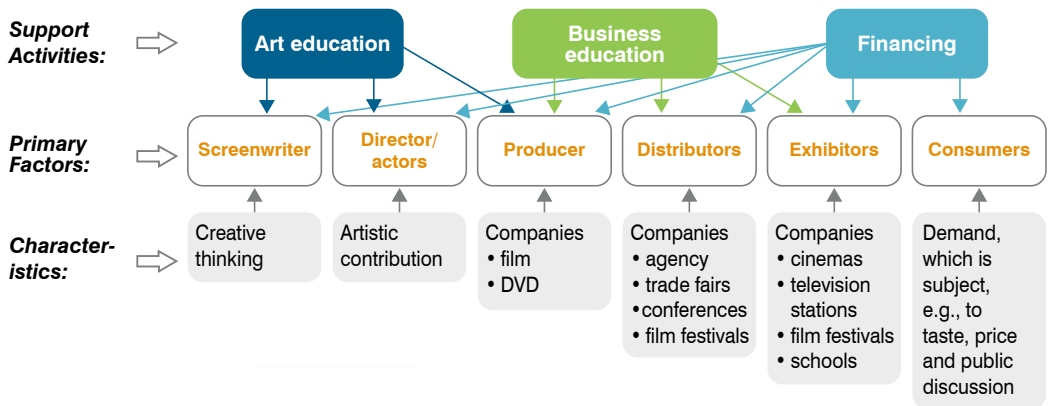
There are five primary factors: the first two are the composer who creates the music and the musician who plays it on an instrument (although the composer and musician may be, and often are, the same person). The two characteristics of these two factors are, on the one hand, a musical instrument and, on the other hand, creative thinking.

The third primary factor is the producer, who prepares a framework for the music; a feature of the producer is that he or she normally comprises a business enterprise, although there are exceptions to this. The performance of the music can take various forms, such as concerts, and involve various media, such as CDs and DVDs or other media suitable for distributing music. The fourth primary factor is the distributor, with the features of this factor being that the distribution may involve radio, television broadcasting, the Internet, shops, such as specialised music retail outlets, cinemas, concert halls of all sizes and types and even households and business premises, where much of the listening takes place.

The first four factors can, in fact, be the same person; it is not unusual, for instance, for composers to perform their own music, produce it,

market it and even distribute it, for instance over the Internet or through mail order sales. Finally, the fifth primary factor is the consumer, whose primary feature is demand, which is dependent on taste for music, the price that the consumer is willing to pay for the goods or services, and public discussion.

The three support activities in the value chain are shown at the top of Figure 2.9: art education, which applies principally to the first primary factors, that is, composers and musicians; business education, which applies principally to the next two primary factors, the producer and distributor; financing, which is linked to all the five primary factors, as capital in some form is indispensable at all stages. Figure 2.9 shows the parties involved in the creation of value, often working in close cooperation. In reality, success in the music industry principally requires talent, education and capital, each of which in almost all periods of history remains in short supply. Figure 2.10 shows, as an example, the value chain in the motion picture industry.<sup>11</sup>



**Figure 2.10:** The value chain in the motion picture industry

In Figure 2.10 there are six primary factors. The first is the screenwriter or screenwriting team that creates the script for the film. The characteristic of screenwriting is creative thinking, and it makes no difference whether the script is original or based on a novel or other work, as screenwriting is accompanied by a great deal of additional work done by others, including the musical score and illustrations used in the film, and this work needs to be planned in detail.

<sup>11</sup> See Einarsson 2014b.

The second primary factor consists of the director and actors; the characteristic of their work is creative contribution. This work is planned meticulously in order to save the time spent on filming, because each day of filming is extremely expensive. A complementary factor to these two primary factors is art education, as shown at the top of Figure 2.10, and financing, which is a fundamental factor and a condition for the making of any film and often the most difficult obstacle.

The third primary factor is the producer or producers, who bear the financial responsibility for the making of the film. A characteristic of this factor is that it is frequently a company established for the purposes of completing a single project, and the object produced is a film for exhibition or a video compact disk for sale to consumers. Usually, however, video compact disks are simply made following the completion of the film. The complementary factors here are art education, business education and financing.

**Johannes Gutenberg** was born in 1398 in Germany and died in 1468. He is best known for his innovations in printing; he developed a special alloy to cast moveable type which was then arranged in presses to produce printed sheets. He also invented a new and improved ink, all of which made printing both cheaper and more efficient than it had been before. The invention of printing is regarded as one of the most revolutionary events in human history, as before Gutenberg books had to be laboriously copied by hand. To give an example, over two thousand people were employed in transcribing books in Paris before the introduction of the new technology. Gutenberg's inventions transformed the world and made it much easier to disseminate knowledge around the world than before. Gutenberg printed a bible which was an acclaimed work of art and is known as the Gutenberg Bible. Gutenberg always had difficulty financing his inventions and spent much of his time on lengthy litigation. Nevertheless, he received some recognition for his life's work shortly before his death.

The fourth primary factor is distributors; their characteristics are that they are companies who distribute films as agencies and are in direct contact with cinema operators, or they distribute motion pictures at special motion picture trade fairs or film festivals. The complementary factors here are business education and financing.

The fifth primary factor is exhibitors; their characteristics are that they are companies or organisations which can be cinemas, television stations, computers or the closely related Internet, film festivals and schools. Schools are in fact prolific exhibitors of films, which are frequently used in teaching. The complementary factors here are business education and financing.

The sixth and last primary factor is consumers, whose characteristics are primarily demand for films, which is dependent, among other things, on taste, price and public discussion. The complementary factor here is financing, as consumers have to be able to afford the

price of admission to the film and also have the time at their disposal to attend the cinematic programme.

Figure 2.10 shows the parties who are involved in the creation of value, often working in close cooperation, as in the music industry. In reality, the essence is talent, education and capital to produce a film, that is, the same factors that were referred to as the *sine qua non* of success in the music industry; this factor applies to most productions in the culture industry.

The emphasis on education in Figure 2.10 indicates that a good education is a condition for success in the film industry, whether in the case of actors, directors, producers, distributors or exhibitors. Marketing is also one of the principal factors in the work of producers, distributors and exhibitors, even though marketing is not specifically noted in Figure 2.10, since marketing is included in business education.

There are great similarities in the value chains of the music industry and the motion picture industry, as shown in figures 2.9 and 2.10. The complementary factors are the same, that is, education in art and business and, finally, financing. Creative thinking is the characteristic of the first level or first levels of the primary factors, and demand depends on the same three factors, taste, price and public discussion.

The value chain takes different forms in different sectors; the original primary factors were transport to plant, the production process, transport from plant, marketing, sales and service. The complementary factors were infrastructure, human resource management, technological development and procurement of production factors. This presentation is geared to traditional factory production and service provision rather than to the specialised motion picture industry, which is used as an example here.<sup>12</sup>

There are various aspects of the production of cultural goods that differ from those of other productions. Some goods, such as paintings, cannot be duplicated – or at least a reproduction will not have the same value, monetary or otherwise, as the original, while in the case of other goods, such as books or films, reproductions will have the same value as the original, at least in terms of content. Although the value chain in figures 2.9 and 2.10 is shown as a linear process, this is not always the

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<sup>12</sup> A great deal has been written on the value chain in the industries. Reference is made here to Porter (1980), Porter (1990) and Hearn *et al.* (2007).

case in cultural production, since links can be interactive, thereby forming a sort of network of relationships and influences. Value chains have changed in the cultural sector in recent years as technology and other factors have effected profound changes for participants in the music industry, and the changes have affected consumers everywhere in the creative industries. It must be assumed that technological progress will continue and be even more extensive and rapid in the future than in recent years and decades.

### 2.2.3 Cost

Cost in financial accounting, or bookkeeping, includes the assessment of use or wear of assets, such as theatres or concert halls, through depreciation. To give an example of depreciation, if a vehicle costing \$100,000 is written off over a period of five years the sum of \$20,000 is entered as expense in the accounts for each of the five years.

Costs are normally divided into fixed costs and variable costs. Variable costs are the costs that change depending on volume of production. Fixed costs, which include, for example, depreciation, rental cost, and interest on initial borrowings, do not change with changes in production quantities. In the short term, nearly all costs are fixed, while in the long term all costs are variable. In economics, the principal focus is on costs that affect decision-making. For example, the cost and time of rehearsing in the performing arts can be significant, and the terms of employment can determine whether this cost is fixed or variable.

With respect to cultural products wage costs are the predominant production costs and can be either variable or fixed. However, there are various other costs. For example, running an opera house is extremely expensive, involving, as it does, large buildings with huge operating costs and large staffs involved in staging works and various other functions, such as maintenance. In order to spread this cost to a greater number of parties and art forms, operas, ballets and even plays are often staged in the same premises.

Transaction costs, the expenses entailed in participating in a market, can provide protection for incumbent domestic companies, since a firm that operates in a domestic market will possess certain knowledge that a foreign firm does not always possess and, therefore, often has to pay for. Transaction costs can include, for example, the cost of legal assistance and the cost of translating cultural sales material.

Firms will usually produce a number of products from a number of production factors. The price of the products and the production factors and the production function need to be known to make it possible to estimate the most feasible production. Costs will change if the price of production factors changes. Increased use will mean increased demand and increased price. Technological progress can also occur with the result that the price of production factors decreases. This change will result in greater use of those factors. The simplest approach is to assume a certain price for production factors at the outset and fixed production coefficients and calculate the costs per unit for products; this approach is frequently used in business operations.

Competition forces businesses to attempt to achieve the lowest possible average cost of their production. It is by no means certain that the efficiency of a firm will increase with its size. There are limits to economies of scale. In a firm whose grasp exceeds its reach, managers can lose their bearings in handling the business day to day and be unable to respond to changed circumstances that a smaller firm might easily accomplish. Although no overall generalisations are possible in this regard, a small business normally has lower production costs per unit than a large business.

It is important in business operations to have a clear view of cost and to explore the differences between various cost factors. This is an aspect of a firm's strategy. In this context the management factors of production, such as planning, organisation, management and knowledge, make a significant difference. All of this results from the fact that firms in an open market are normally in competition with each other, as is often the case in the culture industry. In order to succeed, opportunities need to be utilised to the greatest possible extent.

Production costs will often fall when more units are produced, and this is known as internal economies of scale. In addition, people learn their craft in the course of time, and as they become more skilled at what they do, the average cost per manufactured unit goes down.

It can surprise no one that technology is of significant importance in the culture industry. The new world of the computer, the digital world and the Internet as a distribution channel for information and culture, has brought about profound changes. Technological innovation has probably never been as rapid and extensive in the cultural sector as in the last decade. However, technological changes have often occurred before in



history, as in the case of printing, when in the fifteenth century Johannes Gutenberg invented the method of creating movable type using a special metal alloy. This method enabled him to print books much faster and more cheaply than any previous method<sup>13</sup> and caused a cultural revolution of enormous importance and lasting effect. Motion picture technology, which emerged near the close of the nineteenth century, has had a spectacular impact on the creation of art and dissemination of culture, information and knowledge, as did the subsequent emergence of television. Knowledge of technology and its possibilities is, therefore, of enormous significance. Research has shown that technological advance accompanies increases in productivity in the production of cultural goods.<sup>14</sup>

The reasons for such increases can be divided into four factors.<sup>15</sup> Firstly, advances have been made as regards the size of theatres and stages and improved amplification of sound. Tens of thousands of people can now attend the same concert because of larger venues, which in some cases can even be enormous sports stadiums with seating capacities approaching 100,000 spectators. Sound can now be amplified to the point where it can be heard even in such a huge venue. Secondly, reproduction has led to increased output and increased revenue. Audio disks and books are released in huge runs around the world, and ideas travel instantaneously from one computer to another across all borders. This trend has greatly increased the consumption of cultural goods. Thirdly, costs can be reduced through cheaper settings. Much has happened in this regard, for example, in the theatre. Plays dating from the eighteenth and nineteenth century can now be staged in a much simpler manner than they were staged originally. Costumes, for instance, are much simpler to make now than they used to be, which not only results in a new vision of the works in question, but also in cheaper production. Fourthly, government and private business contributions, as well as individual donors to culture and cultural activities, have increased significantly in recent decades. This influx of capital has helped to alleviate the financial problems of cultural institutions.

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<sup>13</sup> For a discussion of technological innovation in the print industry see, e.g., Broddason (2005).

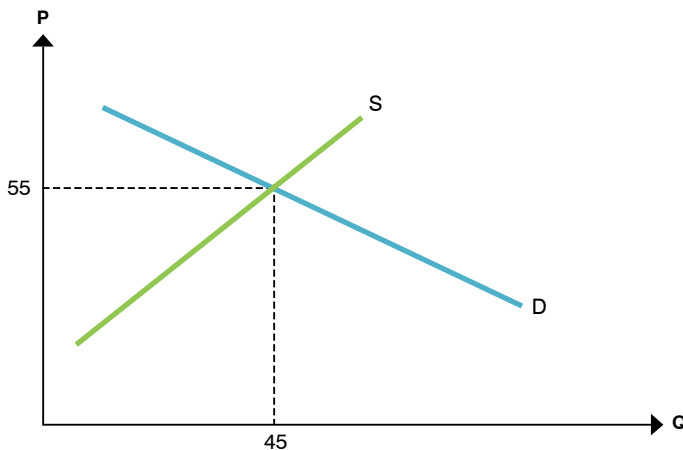
<sup>14</sup> An equally interesting subject is the resistance to technological change. For example, many graphic designers refused to learn computer technology and suffered drastic financial penalties as a result.

<sup>15</sup> For a discussion of increased productivity in cultural production see, e.g., Cowen (1996) and Throsby (2010).

As regards artistic creation, not all the creators involved have full employment in its primary factors, as discussed earlier. The total number of actors is no indication of how many people are actually employed in a theatre company. A number of artists, such as authors and musicians, are also self-employed. Artists have always existed in great numbers, because artistic creation is such an important element of human life. Finding an outlet for artistic expression is also essential to many people even though not everyone can make a living in creative activities, and the chances of success are in fact quite small. Only a very small number are still remembered from the past, and most have not survived the test of time.

### 2.2.4 Supply and demand in equilibrium

Supply and demand meet in an equilibrium, as shown in Figure 2.11.



**Figure 2.11:** Excess demand and equilibrium

Figure 2.11 shows an equilibrium at the price of \$55/unit and the quantity 45 units. Where supply and demand come together circumstances are formed which determine and shape price and market activity. A market can be a geographical location or place, such as an art gallery, or it may be as ephemeral as an Internet site, as in the case of video on demand. Where there is an imbalance, the market will attempt to find the price equilibrium where supply and demand match. In a free market, system imbalances, that is to say excess demand or excess supply, will only last for a brief period, as an adaptation will follow in the wake of price changes. This important fact is known as the law of supply and demand, and it applies to cultural goods as much as it does to any

other goods. However, once an equilibrium has been reached, it can be disrupted through a variety of events and circumstances. This assumes a market where price formation is free, which is by no means the case in all markets or all countries.<sup>16</sup>

Although the law of supply and demand applies to the cultural industries when cultural goods and events are placed on the market and traded, it functions somewhat differently from the way it works with less complicated goods, such as shoes or other apparel, where a need is identified (or created) and then satisfied. To give an example, not all the plays put on the programme of a local theatre are a response to public demand, either real or projected; some plays are kept on the books simply because a stock of local actors have proven durable in the past playing roles that found favour with the theatregoers; others are staged to support local playwrights who without support from the local theatre would have no support at all. The supply of art, therefore, needs to take account of a wider context.

If the supply of art is excessive, for instance if a theatre is attracting small audiences, there can be a number of reasons, such as a poor selection of plays, a poor company of actors or poor casting, inadequate marketing, strong competition from other, more popular, theatres or from other cultural recreation. One solution is to close down the theatre. Another is for the management of the theatre to reduce costs. A third is to adapt to changed conditions, such as by appointing a new manager or director or by launching a marketing campaign or improving the company of actors or changing the selection of plays. A fourth is to obtain funding elsewhere, for example, from a private or public source.

Digital distribution, including dissemination on the Internet, has become more common than before and now applies not only to music and visual material, but to books, magazines and newspapers. Graphic and digital presentation of cultural material and artefacts has become common, both in museums and on the Internet. Technological advances of this kind have shortened production times, reduced costs of production and distribution and facilitated access to cultural goods.<sup>17</sup>

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<sup>16</sup> It is worth noting that the supply of art and culture can also be restricted for political reasons. In human history, books, plays and music have frequently been banned or even destroyed for a number of reasons that are not part of economic laws. For a discussion of government intervention in the supply of cultural goods see, e.g., Rossuck (1997).

<sup>17</sup> For a discussion of the increased and changed presentation of material on the Internet see, e.g. Baumol (2008), Geber (2006) and Bernstein (2007).

There is a market for natural resources and capital which seeks an equilibrium of supply and demand. Factors of production are closely related. A factor that is plentiful will have a low price, while a factor which is scarce will have a high price. This means that if the quantity on offer of a factor of production decreases the price of that factor increases; to give an example, if there is a reduction in the number of trained actors, for instance if acting schools reduce their admission numbers, qualified actors will be paid more for their services. If a company has difficulties obtaining capital for its operation, for instance if government economic policy entails high interest rates that makes raising capital expensive and difficult, the policy will have the effect of reducing production and as a result the demand for labour will decline.

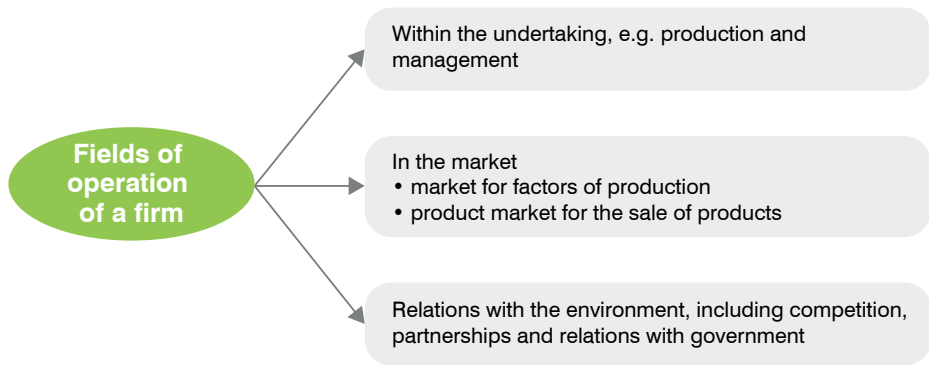
Producers of cultural goods are usually driven by the hope of profit, and they are almost always in stiff competition with other producers who produce similar products or offer alternative options for recreation and experience. Survival, therefore, requires a strategy, and one such strategy is to use celebrities that are known to attract attention. In the cultural sector well-known stars are well paid for their services. This applies to such diverse sectors as spectator sports, motion pictures and the music industry. Even when stars in these sectors are paid huge wages, this can be cost-effective because the demand is so high and the individual stars are so few in comparison with the total number people involved in a production, whether the product is a motion picture or a football game. Consumers want to see the best, and if those wishes can be met, it is worthwhile to pay high salaries to the best people.

This ‘superstar phenomenon’ which is reflected in the exorbitant salaries paid to stars, rests on the logical assumption that people want to see the most famous, and, therefore, presumably the best. Also, it is possible to make a product, which could be a motion picture or a football game, using a technology that enables large numbers of customers to enjoy the product without excessive cost. Hundreds of millions of people can watch a football game featuring superstars Lionel Messi or Cristiano Ronaldo in a live television broadcast. Motion pictures featuring big stars such as Meryl Streep or Tom Hanks can be shown all across the world to millions of viewers in movie theatres and can subsequently be published in huge numbers on DVDs or shown to a wider audience on television. In the cultural sector, in mass production as in the case of book publishing, CD releases and motion picture production, the cost of producing a single additional unit, such as one additional copy of a book, CD or DVD

is relatively low, which increases profit still further. Significant income can also be derived from ancillary activities in connection with cultural events or cultural goods, for example, restaurant services or sales of reproductions and souvenirs in museums, sales of programmes at art exhibitions or sales of sweets in cinemas.

### 2.2.5 A Business firm's fields of operation

Business firms have three fields of operation, as shown in Figure 2.12.



**Figure 2.12:** Fields of operation of an undertaking

A firm's fields of operation cover, firstly, what happens within the firm itself, for example, production and management, as shown in Figure 2.12. This could be a film producer who produces films under the banner of a separate company, or a cinema that needs to be managed.

Secondly, a firm operates in the marketplace. There are two markets involved: the market for factors of production, such as labour and raw material, and a market for goods and services, where the products are sold. For example, a theatre manager needs to hire actors for roles in a play, which he finds in a specialised labour market. Then the play needs to be staged and admissions sold; this is the market for goods and services.

Thirdly, a firm's field of operation covers the firm's environment, that is, cooperation or competition with other companies and relations with government entities, involving regulatory disclosures to a statistical bureau or tax authorities. This applies to all firms, whether they are involved in the cultural sector or any other production.

## 2.2.6 Classification of goods and services

Goods and services are divided into four categories, as shown in Table 2.1.

		Rivals in use, i.e. the use by one reduces usefulness to others	
		Yes	No
<b>Others can be excluded from use</b>	Yes	Private goods - foodstuff - motion pictures	Natural monopolies - subscription television - fire departments
	No	Common resources - national parks - fish stocks	Public goods - national defence - traffic lights

**Table 2.1:** Classification of goods and services by use and impact on others

As shown in Table 2.1, the first category comprises what is known as private goods. This category covers most goods and services. Their characteristic is that others can be excluded from enjoying the goods, and the use by one reduces the use by another. Some examples are food and theatre attendance. You can't have many people eating the same slice of bread. Anyone can see a play in a theatre, but they have to pay for the admission. A person who does not go to the theatre and does not pay admission has no use of the play. The fact that the use by one limits the use by other is clear, as two people cannot occupy the same seat. This results in competition for use.

The second category comprises goods and services that are classified as natural monopolies. This means that others can be excluded from enjoying the goods, but the use by one does not reduce the use by another. An example of this is subscription television. Anyone can buy a subscription to the station, but not without payment. However, the addition of one subscriber to the station has no impact on other subscribers.

The third category is common resources. Others cannot be excluded from using the goods, and the use by one does not entail a reduction in use by another. An example could be vulnerable tourist attractions. Sites of natural beauty can suffer if the crowds of tourists grow too large. Access by tourists to vulnerable places is, therefore, often restricted. There is a phrase in economics, the 'tragedy of the commons' that refers to the spoilage or depletion of shared resources, as in the in the case of fish stocks which are not carefully managed.<sup>18</sup>

<sup>18</sup> For a discussion of excessive exploitation of resources see, e.g., Coase (1990) and Winter (2008).

The fourth category is public goods. In this category others cannot be excluded from use, and the use by one will not curtail the use by another. Examples could include national defence and traffic lights. Everyone benefits from national defence, if there is any such defence in place. Everyone has the use of traffic lights when they arrive at an intersection. Even if one person benefits from national defence or traffic lights, this has no effect on the benefit to others.

Common goods are usually provided by government, as it is often difficult to collect charges for use by individual parties. The influence of public goods is significant in culture, where government can support production. Closely linked to common goods is the 'free rider problem', which arises when people use goods or services without paying for them. Free riding is never acceptable to a private trader who produces the goods and services, for the trader carries the cost of the production. The result is market failure, as the free market will not supply such goods and services in an economical quantity.

Primary research is an example of a public good. When the results of the research are disclosed to the public, it becomes a public good, available to anyone without payment. A mathematician's discovery of a new formula becomes a public good as soon as it is published. This does not apply to patentable discoveries, such as technical inventions, since the use of intellectual property rights is subject to certain rules, but scientific progress normally becomes public property once it is disclosed. This is one of the principal reasons that government supports primary research with funding, in the knowledge that the research will eventually bring benefits to all society.

In culture, goods are often private goods which are traded in markets. These may be plays, art exhibitions or other cultural events or works of art. In most cases a fee is paid for admission to the event or exhibition. In the case of public goods or common goods, however, there is no obvious price, and this is often the case with public goods. Archaeological sites are examples of common goods: they belong to everyone and are accessible to anyone but have no specific market price.

Cultural goods are a mixture of private goods and public goods. Governments supply public goods, such as cultural goods, in a sufficient quantity by funding their production, at least in part, through taxes. A painting by Vincent van Gogh is an example of a good which can be a mixture of private and public goods. A painting by van Gogh can be

private property, since if a museum owns a painting by van Gogh and sells it to another museum the painting becomes private property with a buyer and seller and a buying and selling price. However, the painting also has historical value and is in that regard a public good. In this sense, the painting will be placed on display in the first museum and/or the second so that as many people as possible can enjoy it, as it appeals to the public and to professionals in a number of ways. Of course, the public can be excluded from seeing the painting, but this is rare, and the fact that someone else observes the painting does not detract from our own enjoyment of observing it.

### 2.3 The cultural industries

Economics addresses issues such as demand, production, consumption, distribution and sales. The same general principles will apply in the case of cultural goods as in the case of other goods. In fact, this concept can be turned around, and we can talk about corporate culture. The culture of the industries is characterised by certain attitudes which are long-standing in deep-rooted industries.<sup>19</sup>

Distinctions in the cultural industries are not always clear. The print industry, which forms a part of the cultural industries, is an example. A great deal of material is printed, such as books, magazines, newspapers, musical scores etc. However, a great deal of other material is also printed which hardly pertains to culture, such as instructions with household devices and similar written material. What is true of other industries applies also to culture: it is not always possible to draw a line between their segments.

The quantity of goods in the cultural industry is measurable: the number of admissions sold to a theatre, the income from the release of a CD or the print run of a book. However, this is not simple in the case of resources such as labour, since many of the people who work in the cultural industries are also employed elsewhere. An electrician may work in a theatre, and thereby in the cultural industry, but the same person may also be an electrician in a car repair shop, an activity unrelated to the cultural industry. So work can be performed in different places and areas; however, these are marginal examples. Normally, it will be quite

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<sup>19</sup> For a discussion of organisational culture see, e.g., Schultz (2004).



clear whether a firm is engaged in the cultural and creative industries and what tasks form a part of these industries.

The cultural industry has gone through profound changes in the last thirty years. Companies have grown, they have expanded into a greater number of areas, and their turnovers have increased significantly. Globalisation entails cultural products being sold across national borders, and progress in telecommunications and computer technology has been rapid over the same period. Government policy has also changed, and is now increasingly shaped in a global context. Consumer tastes have also become more complex, and the extent of promotion of cultural products is much greater than ever before. The number of small and medium-sized enterprises (SMEs) in the cultural industry has grown markedly, but in reality most companies in any sector of the economy are small and medium-sized enterprises.<sup>20</sup>

The definition of small and medium-sized enterprises differs between countries and in some countries companies with over a hundred, or even five hundred, employees are classified as SMEs. In the *European Union* (EU) an enterprise with fewer than ten employees would normally be classified as a microenterprise, an enterprise with ten to fifty employees would be a small enterprise, while an enterprise with fifty to two hundred and fifty employees would be a medium-sized enterprise. Also, the EU will also take account of the turnovers or balance sheets of undertakings.<sup>21</sup>

One difference between the production of cultural goods and goods in more traditional manufacturing industries, such as the automotive or food industries, is that in these industries once the manufacturing process has started, changes in the goods are more difficult to make. In the cultural industry this can be easier, for instance in cases where a film, its actors or plot are altered even in the course of the production process.

Goods or products in the cultural industries are based, among other things, on the creative work of artists, and they are intended to enhance usability or the well-being of consumers. These products have a variety of characteristics. There is great uncertainty regarding their value, as it is difficult to predict the popularity or success of an individual product

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<sup>20</sup> For a discussion of small and medium-sized enterprises in the cultural industry see, e.g., Caves (2002) and Hesmondhalgh (2002).

<sup>21</sup> For the *European Union* (EU) definition of small and medium-sized enterprises see *The activities of the (EU) for small and medium-sized enterprises (SMEs)* (2005).

or service. The products are also many and varied, but in spite of an almost endless variety the number of products that achieve significant popularity is invariably small. However, those that succeed can achieve almost boundless distribution and popularity. Many products are sold shortly after their production, but will have a short life cycle and make a brief appearance in the market. It can be a very expensive proposition to make the first product, but replicating it often adds little to the original cost, as in the case of books, films and music, where reproduction is cheap once the product has been made.

The creative force of producing cultural goods will originally derive from the work of artists, whether working alone or as part of a group. Employment in art is in demand, even though not all artists earn a comfortable living; in fact, this line of employment is characterised by an inequality of income. Only a very few artists can have very high incomes, but the attraction of joining their ranks is great. Artists often need to make sacrifices to engage in their creative work, but they do so because the work gives them great pleasure. The same applies to scientists.

One of the consequences of creative work in the cultural sector is a risk of conflict between the person engaged in the creative work and other participants in the work. For this reason the relationship between the individual participants in the process of creating cultural goods is normally clearly defined, often through highly detailed contracts between the artists and the producers and also with those who undertake the distribution and marketing. Contracting with creative artists can be a complex process and requires a great deal of precision. One of the reasons that no loose ends will normally be left in such matters is that conflicts can easily come up, such as artistic conflict or conflicts regarding the development of certain ideas, and such conflicts can quickly lead to increased cost.<sup>22</sup>

These are classic power struggles. They are common throughout the economy, but the reason that they can become so prominent in the creative industries is that the production is often linked to an artist's self-perception. The artist, or the creative contributor, believes that he or she is investing a part of himself or herself into the product, often an important and very personal part of himself, and, therefore, wants to influence the work to its very end, which in many cases is neither feasible nor possible.

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<sup>22</sup> For a discussion of contracting with artists see, e.g., Caves (2002), Alper and Wassal (2008), Scott, W. R. (2006) and Lampel *et al.* (2006).

A classic problem in the creative industries is the conflict between independence and control. Creative work, especially artistic work, requires a great deal of freedom, since otherwise the work is unlikely to succeed to the extent needed to arouse public interest. On the other hand, all production needs to be properly channelled with an overview of costs and through control and intervention by professional management.

The trick in the production of cultural goods, where the initiative of the individual needs to be manifested, is to recognise this special feature and the latitude that needs to be granted in the process. In such circumstances a good manager will tap from his or her creative employees all that they have to offer and all that can be transformed into a saleable product. If a manager goes too far in channelling creative thinking into precise work processes and into the precise organisation that often characterises industrial production, this effort can cause the creative energy to evaporate and the work to amount to nothing. The only thing that has been achieved is that creative thinking has been forced into a rigid system. Flexibility is essential to the creative industries, and particularly in the industries which are characterised by significant uncertainty and risk.

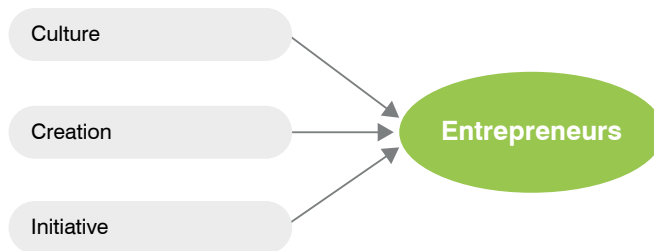
An important factor that relates to the creative and cultural industries is the new digital technology that is widely used in dissemination, particularly over the Internet. The emergence of this technology has enabled rapid communication of knowledge, and it has also resulted in spillovers, that is to say positive externalities resulting from the dissemination of knowledge. This spillover caused, or enabled, by the Internet, computers and contemporary information technology in general has also led to the formation of clusters, or concentrations of knowledge and work, as in the case of film producers in Hollywood, theatres in London or fashion designers in Paris.<sup>23</sup> In this kind of an environment knowledge flows more freely and rapidly between individuals and enterprises. This results in external economies of scale, an improvement in productivity that emerges when people come together and technical advances result from their interaction.

Strong companies can become centres of economic activity for entire regions and attract other business activities. An example of a group formation of this kind in the United States is the cluster of knowledge companies in Silicon Valley near San Francisco. Concentrations of this kind

<sup>23</sup> For a discussion of clusters see, e.g., Porter (2000) and Scott, A (2005).

can lead to reduced average costs of production, which is an advantage in the global competition. In this way external economies of scale can lead to internal economies of scale.<sup>24</sup>

Figure 2.13 shows a model that illustrates the three fundamental concepts of entrepreneurship: culture, creativity and initiative. A combination of these three factors can lead to the emergence of an entrepreneur.



**Figure 2.13:** Entrepreneurs

Culture, creativity and initiative are factors of production for individuals who are entrepreneurs and often work in clusters. Entrepreneurs are important participants in the economy, as they are the ones who visualise, launch and run enterprises in all sectors, including the creative industries and the cultural sector. Much production in the cultural sector and the creative industries has the form of technically advanced industrial production, which is just as subject to the principles of increased productivity as any other industry that does not have creativity as a fundamental factor.

Traditional industrial production studies apply to the culture industry as much as they apply to other industries as regards organisation, implementation of strategy and performance. Organisation applies, among other things, to the situation of a number of producers and consumers, product mix and conditions for market entry and exit. The implementation of strategy concerns price formation and decisions on production quantity, marketing and competition. Performance relates to the effectiveness of undertakings in meeting demand with regard to quality, cost and price. This thinking applies to the culture industries and in the creative industries in general.

<sup>24</sup> For a discussion of internal and external economies of scale see, e.g., Hall *et al.* (2002).

Research has shown that growth in production and work in the creative industries has increased significantly in recent years, and more than in other industries. The reason for this growth can be traced to increased demand for cultural goods, which in turn requires greater supply, which has been greatly facilitated by the new digital technology. Technology and human resources are, therefore, the driving force of economic growth. The creative industries form a sort of network, where the connections between producers and consumers are extremely varied. Economic growth in this area can be traced, among other things, to increased production per capita, that is increased productivity, or to increased consumption of cultural goods since, as mentioned earlier, consumption of cultural goods tends to increase with increased consumption. Cultural capital has also increased, which contributes to economic growth.<sup>25</sup>

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<sup>25</sup> For a discussion of growth in the creative industries and cultural capital see, e.g., Florida (2005) and Cheng (2006).

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### 3. Role of government and cultural policy

Attitudes to culture have changed in recent years. For one thing, today there is in general more discussion about, and appreciation of, cultural matters in society from various economic perspectives, such as micro-economic perspectives, regional development perspectives, cultural education perspectives and many, many more. More attention is now being given to analysing the impact of economic factors on various matters that relate to culture, cultural goods, cultural industries and cultural policy. The results of such analysis are then often mustered in support of arguments for public backing of culture, which will often exert significant influence on public political discourse and thereby influence government behaviour. A second reason for changes in attitudes to culture is that increased demands are being made for widespread public access to various institutions that used to belong exclusively to the privileged classes, for children's education to be expanded and made more varied, and for cultural institutions to take greater account of changed and more multicultural societies.

A third reason relates to increased government participation in cultural affairs. Public service represents a large factor of the economy, and the extent of public service is measured and evaluated in a number of ways. The success of public expenditures on cultural matters can be assessed, for instance, in terms of the number of people visiting museums. However, this attitude is open to the criticism that too much emphasis is placed on the economic aspects of culture at the risk of losing sight of the fundamental point that the nature and principal purpose of culture lie in its importance for the advancement and co-existence of individuals. Does culture make individuals and society at large somehow better off? Plenty of people who claim to know about these things seem to think so, and it behooves us for this reason alone to direct our thoughts in this chapter at this notion.

Thus, it is hard to argue that attendance numbers express the real value of visiting a museum or attending a concert – as if culture were an experience that people can be exposed to in order to derive its benefits, the more exposure the better – and it is, in part, this kind of attitude that downgrades the cultural value of such institutions.<sup>1</sup> As a matter of fact, attitudes to cultural matters and the role of government are constantly developing in the public and academic discourse, but it differs from one country to the next. Governments in most countries exert great efforts in their support of culture, but public cultural policies vary from one country to another and so do the arguments underlying the policies.<sup>2</sup>

### 3.1 Government support for culture

The focus of government involvement in the culture industry and/or creative industries can be either economic or cultural. Economically, the focus can be on support for small and medium-sized enterprises, the creation of a favourable infrastructure and support for innovation, for example through research, market support, education and training. The cultural focus would be on general governmental support for cultural activities. It is important to recognise the importance of the fundamental factors of culture for the economy. For example, this importance could manifest itself in the public discussion of media ownership, since the media are a powerful tool that can be used to broadcast an entire nation's self-perception; if the interests of business are properly heeded, this important element cannot be ignored.<sup>3</sup>

A number of arguments can be proposed in favour of government support for culture, many of which are based on purely economic viewpoints. These arguments can be divided into seven categories, as shown in Table 3.1, along with keywords for each one.

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<sup>1</sup> A visit to the Monterey Bay Aquarium is an experience heartily to be recommended. On offer in the large tanks are a wealth of sea plant life and many sea animals frolicking about that can also be seen offshore on the Monterey Peninsula; but be warned, admission for adults is currently \$39.95. In contrast, the American Museum of Natural History in New York City is \$22. It is highly unlikely that the price of admission to a museum is an index of the cultural importance of the exhibits on display. On this financial scale, the Smithsonian Institution is hardly worth a cup of coffee in the cafeteria, since admission is free, but anyone who has spent even a few hours in the complex knows how unreliable the price factor in judging a museum really is.

<sup>2</sup> For a discussion of attitudes to cultural matters and the role of government see, e.g., Bradford and Gary (2000), Lewis and Miller (2003), Holden (2004), Throsby (2010), Chong (2010) and Valtýsson (2011).

<sup>3</sup> For a discussion of media ownership see, e.g., Corn-Revere and Carveth (2004) and Galloway and Dunlop (2007).

Categories	Keywords
Economics	Merit goods, externalities, comparative advantages, demand, market failures, creative industries
Politics	Origin, equal access, preservation, cultural policy, cultural scale
Employment	Connection of industries, foreign filmmaking companies
Regional affairs	Rural areas, use of regional fixed assets
Education	Schools, clusters and cluster effects
Geography	Tourist promotion as a public good, tourist industry
State finances	Foreign currency revenue, taxes, returns

**Table 3.1:** Arguments in favour of government support for culture

These keywords, and by no means are all of them listed above, will be discussed later. However, a few words here on ‘politics’ (in the left hand column above), which is often a bone of contention, as well as the question of what form such support should take. Various arguments will be proposed here to support the notion that government support for culture is beneficial, especially because of the positive externalities involved, but at the same time it should be noted that many of these arguments are controversial and fall within the domain of normative economics.

Governmental support of culture and the production of cultural goods is, although often controversial, beneficial in many respects. One area where support is beneficial is the subsidy of merit goods, which in economics are defined as goods and services in the economy that are considered to be desirable and beneficial to a community, even though they cannot necessarily be measured in terms of monetary value. Goods and services of this kind are not always in such demand that the market alone is able to provide an adequate supply, and so governments are often called on for their support. Health care is one kind of merit good, especially public campaigns to vaccinate large numbers of people. Symphony orchestras are another example of merit goods, because they involve high operating costs and their music seldom enjoys mass appeal. However, many people would agree that society would be poorer without symphony orchestras, which is why most governments contribute public funds in support of such operations. It must be kept in mind, however, that any support of a specific activity of this kind, for example through financial contributions, will always occur at the expense of support for something else or at the expense of reducing public expenditure by lowering taxes. Merit goods are often regarded as having positive externalities when the amount of information reaching potential beneficiaries is sufficient to create a demand for the goods.



Culture and cultural activities enrich human society and many aspects of culture, such as the production of educational audio-visual material, lead to improved education and increased productivity in various spheres of the economy. Governments, that is to say public authorities, thus often support various elements of culture, such as filmmaking and radio, for the purpose of making cultural material accessible to the public, both because of its positive externalities and also in response to market failure, since the benefits of cultural events may be greater than consumer demand might appear to indicate.

Many believe that the culture of a community has intrinsic value and that, therefore, it should be made accessible to everyone. Equal access to culture is in itself important to any community, and it falls to government to ensure such equality of access, whether for genders, classes, income groups, regions or generations. The preservation of culture is not often a profitable activity as measured by how much value it generates, and so the task is left to government.

In the United States the tradition has been continued, which began in Europe, where aristocrats, kings and popes were patrons of the arts. In modern times, this role is left to the wealthy, who often enjoy tax privileges for their trouble, while public expenditure towards such ends is moderate. In Japan there is little public support for the performing arts, while in mainland Europe, particularly in Scandinavia, much of the cultural sector is supported by the government. In Britain, however, there is a richer tradition for allowing the market powers to exert a significant influence on cultural activities.<sup>4</sup>

The production of art and culture entails significant fixed costs, where economical pricing would not be viable without government support. However, over time public subsidies for cultural activities may lead to discrimination, where deep-rooted institutions are given priority, making it difficult for new participants to gain a foothold. Government policy on support and subsidies, therefore, needs to be constantly re-evaluated.<sup>5</sup>

There are times when government seeks to persuade the public to adopt a 'correct' attitude when the public, in the opinion of government, is not showing the required positive attitude to art and culture and does not generate adequate demand. In such circumstances government will

<sup>4</sup> For a discussion of the details of carrying out cultural policy see, e.g., Towse (1994), Netzer (2008), Van der Ploeg (2008), Champarnaud *et al.* (2008) and Towse (2010).

<sup>5</sup> For a discussion of government support policy see, e.g., Grampp (1989).

define its role as ensuring that the supply is adequate and taking measures to encourage demand, for instance through low admission fees to museums and various other measures. While this may be perceived as a sort of ‘paternalism’, it is not an uncommon attitude among governmental policymakers. However, the public may in fact be quite interested in culture and cultural events, in which case government will seek to meet these needs by promoting the supply of such events. Finally, public authorities may offer grants in the culture sector simply because there are powerful interest groups in culture, such as associations of artists, and government may yield to the demands of these groups.

Table 3.2 shows the labour force participation in the cultural sector in 15 countries in Europe in 2009.<sup>6</sup>

Rank	Country	Share (%) of employment in cultural sectors in 2009	Rank	Country	Share (%) of employment in cultural sectors in 2009
1	Iceland	3.2	10	Slovenia	2.0
2	Norway	2.6	11	Lithuania	2.0
3	Sweden	2.3	12	Croatia	1.8
4	Latvia	2.3	13	Hungary	1.8
5	Denmark	2.3	14	Estonia	1.7
6	Finland	2.3	15	Malta	1.7
7	Germany	2.2	16	Czech Republic	1.7
8	United Kingdom	2.1	17	France	1.7
9	Netherlands	2.0	18	EU-average	1.7

**Table 3.2:** Share of culture in labour force participation in seventeen European countries in 2009

As can be seen in Table 3.2, which shows the labour force participation in Europe in the cultural sector, Iceland tops the list with 3.2% of the labour force employed in the cultural sector. Other Nordic countries range between 2.3% (Denmark and Finland) and 2.6% (Norway). The average of the 27 countries of the EU is 1.7%, as shown in Table 3.2. As the table shows, the cultural industries have significant economic weight in many countries, and in addition it should be noted that cross-border collaboration, as in the production of music and motion pictures, is common, often with successful results and increased economic activity.

<sup>6</sup> For a discussion of labour force participation in the cultural sector in Europe see *Cultural Statistics* (2011).

Encouraging the production of culture can also be an important aspect of regional policy, that is, as a vehicle to strengthen economic diversity in rural areas. In the context of regional policy a great deal of effort may be put into promoting culture and various aspects of rural social infrastructure. When clusters form in small communities, they can, as mentioned earlier, contribute to the formation of stronger business firms possessing extensive knowledge and external economies of scale.

One of the principal tasks of government is to provide citizens with access to a good education.<sup>7</sup> Quality education improves human society in a variety of ways, and it also improves productivity in the economy; governments in many regions of the world would do well to contribute more to education.

Many countries spend a great deal of effort on promoting themselves and creating for themselves a positive image, not only to strengthen their respective national identities, but to encourage tourism, contribute to global trade and strengthen their exports. Promotions of countries also serve to disseminate culture, and this is an area where government has a role to play.

Modern tourist promotion relies principally on visual material, such as films, television programmes and websites; this is a radical change from the tourist promotion of a few decades ago, which was carried out almost exclusively through printed material. The avenues for promotion are now more varied than ever before. Tourist promotion, as a mainspring of the tourist industry, has become a public good with a number of parties benefiting from the work of a few people. In many cases this activity raises the classic problem of the free rider that was previously discussed in relation to public goods. Nevertheless, governments are usually quite willing to strengthen tourist infrastructure, and the promotion of countries as tourist destinations has a positive effect not only on cultural tourism, but also on other exports because knowledge of trading partners always benefits participants in business.<sup>8</sup>

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<sup>7</sup> For a discussion of the economic importance of education see, e.g., Samuelson and Nordhaus (2005) and Lynggaard (2008).

<sup>8</sup> For a discussion of tourism and its benefits see, e.g., Dwyer *et al.* (2004).

## 3.2 The objectives of a cultural policy

Increasing international attention has been devoted to culture in recent years and decades. The international organisations that have focused their attention on culture include UN, in particular UNESCO, OECD and EU.

A cultural policy has been established by UNESCO with five principal objectives. The first is that cultural policy should be a key feature of developmental planning in individual communities. Many of the countries of the world are in a phase of rapid development and since culture plays an important role, cultural policy should be adapted to this trend. The second objective is that cultural policy should encourage creativity and public participation in cultural life. The third objective is that cultural policy should reinforce the cultural industry and take account of the economic aspects of culture and preserve the heritage of culture. Human history includes numerous examples of heritage or distinctive features of culture that have been lost but would have been worth preserving. The fourth objective is that cultural policy should strengthen and preserve cultural diversity. This goal is a clear reference to the importance of culture to small communities. Artistic, cultural and creative work often involves some form of depiction of social or national identity and is, therefore, an important aspect of the cultural policy of any nation. This has particular relevance for countries with small populations, who will often place great emphasis on their identity. The same applies to ensuring cultural diversity. The fifth objective is that in the implementation of cultural policy more assets and human resources should be allocated to cultural affairs.

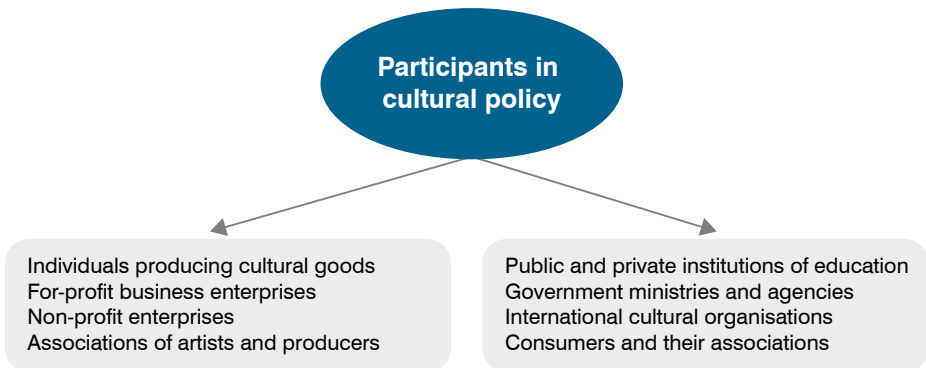
Most governments are pursuing these objectives in one way or another. The assumption underlying these five objectives is that culture has an important economic impact.

There are various obstacles to the implementation of a cultural policy, including a lack of information and statistical data. Making data comparable between countries can be fraught with difficulties. Nevertheless, statistics bureaux, at least in the wealthier countries, are gradually doing a better job of compiling cultural information. Cultural policy is evaluated by using the criterion of maximising welfare in society; as in the case of other sectors, the method used in culture is often contingent valuation methodology, which attempts to gather information by surveying

willingness to pay. Government will sometimes establish precise targets to be met with their contributions to culture, in particular the arts, and then measure the results of the contributions.

The artistic targets of a cultural policy are, first, that the culture produced should be of high quality in the judgment of knowledgeable persons. The second target involves progress and innovation, in the anticipation that new products will be created. This is not unlike the case of public support for scientific research. The third target is that the products created must be accessible to the maximum possible number of people in the interests of non-discrimination. Equality is measured in economics on the basis of distribution of income, that is, the way in which income is distributed among citizens, but equality is also an important aspect of culture and cultural policy.<sup>9</sup>

It is important in the context of artistic and cultural goals to ensure stability and continuity in artistic perspectives and artistic creation, which relates to both past and future generations. Cultural heritage and cultural perspectives need to be passed on to young people to enhance their understanding of the characteristic features of their culture and enable them to improve their quality of life. The participants in the production of cultural products and cultural policy can be divided into eight groups, as shown in Figure 3.1.<sup>10</sup>



**Figure 3.1:** Participants in cultural policy

<sup>9</sup> For a discussion of the objectives of cultural policy see, e.g., Myerscough (1988), *Draft Action Plan on Cultural Policies for Development* (1998), Noonan (2003), Eriksen and Sørheim (2005), Towse (2010) and *Compendium of Cultural Policies and Trends in Europe* (2015).

<sup>10</sup> For a discussion of participants in cultural policy see, e.g., Throsby (2010).

Participants in cultural policy are the individuals who produce cultural goods, including artists and everyone who is involved in artistic production, for instance, all the people involved in staging an opera. Enterprises that produce cultural goods for profit are participants in the cultural policy. These are commonly small and medium-sized enterprises. These enterprises, like other business firms, operate in a competitive market, but are cultural in the sense that the goods they produce are cultural goods and their management, therefore, must be based upon an informed understanding of the cultural environment to succeed.

Enterprises and organisations that produce cultural goods for purposes other than profit are also participants in the cultural policy. These are often voluntary organisations, such as choirs and amateur theatre companies. The same applies to public cultural institutions, such as art museums, libraries, concert halls, radio stations and educational institutions, whether operated by public or private entities, as in the case of various art academies. Such undertakings and organisations often have the corporate form of private non-profit institutions. Associations of artists and producers, like associations of undertakings in the cultural sector, are also participants in cultural policy. Government ministries and their cultural agencies are participants in the cultural policy, as well as international cultural organisations such as UNESCO, and consumers and their associations, since virtually all consumers partake of cultural goods to some extent.

A cultural policy should address the significance of culture for the nation where the policy is pursued, and a cultural policy should also address human rights, such as equality and freedom or other personal freedoms, since cultural matters are an important aspect of human rights, such as freedom of speech, opinion and religion. Culture and human rights are, therefore, closely connected in any cultural policy.

Cultural policy has an impact on trade, for cultural goods are not only important goods in any domestic market, but increasingly in international markets. Education in cultural matters, such as art education, and even basic education at the primary, secondary and university level, is a significant factor in cultural policy.<sup>11</sup>

One concept that has connections with culture is sustainability, which refers to the use of natural resources so as to meet the needs of the

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<sup>11</sup> For a discussion of education on culture see, e.g., Bresler (2007) and Bamford (2009).

present without prejudicing the opportunities for future generations to meet their needs. This is a serious commitment. It permits current generations to do what they want as long as they do not jeopardise the rights of future generations. This concept has become central in all discussions of the environment, but it is now also used in a much wider context than when it was first introduced.<sup>12</sup> The link of sustainability with culture is primarily rooted in the quest for ensuring cultural diversity so that certain elements of culture which are worth preserving are not lost and thereby made unavailable to coming generations.

Culture, the heritage of past generations, is a tool for peace. The more extensive the public knowledge of the culture and cultural trends of other nations, the greater the understanding of different circumstances and the less the likelihood of armed aggression against other people. Religion is a part of culture, and notwithstanding the frequent use of religion as justification for aggression most religions feature human kindness and charity as central elements that contribute to peaceful relations among individuals; ideologies of this kind are particularly appropriate in the current world situation.<sup>13</sup>

### 3.3 Planning a cultural policy

Public institutions play an important role in preserving culture and cultural heritage through education, conservation of knowledge and promotion of cultural heritage. The traditional method of policymaking in public administration is to establish an objective, prepare a strategy and then measure the success of the strategy. This can be done in six steps: establishing objectives, empowering the people who need the authority to achieve the objectives, co-ordinating the strategy between the individual levels of administration, selecting the tools that are best suited for the achievement of the established objectives, implementing the strategy with measurable results, and, finally, monitoring and evaluating the success of the strategy and using feedback to ensure its future success, as shown in Figure 3.2.

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<sup>12</sup> For a discussion of the concept of sustainability see *Our Common Future* (1987), where the concept was first introduced in a report known as the *Brundtland Report*.

<sup>13</sup> For a discussion of the role of culture in peaceful cohabitation see, e.g., Huntington (1996) and Rushton (2003).



**Figure 3.2:** Formulation of cultural policy

The activities of public authorities have a number of goals; for instance, they will want to ensure stability, full employment, balance of trade, a high level of welfare and control over market failures. These objectives are often mutually exclusive. Market failure is caused when a market cannot by itself resolve all the problems relating to supply, demand and price formation. This is clearly the case with public goods, which constitute much of art and culture, since public goods entail a benefit which is often unachievable without public support. The special position of public goods provides important grounds for the argument that government has an important role to play in cultural matters, as discussed earlier. Cultural heritage can have positive externalities, ranging from the mere pleasure of knowing that the heritage is in place and has been made readily available to its beneficial economic impact on tourism.

Goods and services can be transformed from private goods to public goods, as in the case of music that is distributed illegally on the Internet without payment to the composer or performer. This theft composes a scenario where public authorities must intervene, because new technology has transformed normal business practices to the disadvantage of stakeholders whose income depends on the inviolability of their intellectual property rights.



Efficiency is one of the principal goals of government, but since efficiency may be hampered if there is insufficient competition in a market dominated by a few firms – or in extreme cases by just one – governments in most countries are on guard against oligopolies and monopolies; one of the functions of competition authorities is to prevent mergers of firms when there is a risk of a monopoly that will dominate the market, eliminate competition, and impose higher prices on consumers. In addition to efficiency, equality is an important factor of public policymaking and most governments work on the assumption that equal rights should be secured, to the highest degree possible, among the diverse groups and individuals that form a community.

Economic growth is another general objective of government, and since in recent years the cultural sector has grown faster than the traditional economic sectors, growth has become a more important part of government policy. Culture and the creative industries in general also have an impact on other sectors of the economy, for instance the tourist branch, because cultural activities, especially in large urban centres such

as London and New York, attract tourists in enormous numbers who spend their money on a wide range of goods and services, all of which translates into enormous economic benefits for the host community.

Yet another government objective is full employment, and, as in the case of economic growth, employment in the cultural industry has grown faster than in other sectors.<sup>14</sup> The contribution of human labour in the cultural sector is extensive in comparison with other factors of production, making it a labour-intensive sector with a high contribution of human resources, often resulting in less need for physical capital in comparison to other industries. This circumstance makes investment in this sector in many ways attractive, which is yet another reason for government to include culture in its economic planning.

**Homer**, the great Greek epic poet, is believed to have lived in the 7<sup>th</sup> or 8<sup>th</sup> century B.C. He is said to have been the creator of the *Iliad* and the *Odyssey*. The former is an account of the rage of Achilles, Greece's greatest hero, in the siege of Troy in Asia Minor. The *Odyssey* is the tale of the trials and long journey home of Odysseus, one of the Greek generals in the Trojan War. The events are believed to have been set in the 12<sup>th</sup> century B.C. Both epics were narrated and sung in a long oral tradition before being written down. These works are the foundation of classical studies and Greek mythology and have had a profound impact on literature and the arts for centuries. Since little is known about Homer there are some who doubt that he even existed and believe that the two epics are the works of many poets. This has been a matter of dispute between scholars for a long time. The epics have been translated into most of the world's languages and are read in schools to this day.

<sup>14</sup> For a discussion of the growth of the cultural industry see, e.g., Bustamante (2004) and Wiesand and Söndermann (2005).

In addition, jobs in the cultural industry are often more satisfying for individuals than in many other sectors of the job market, notwithstanding the fact that many such jobs are ranged along the bottom of the wage scale.

In most countries cultural goods are both exported and imported. Some countries export much more than they import, as in the case of the United States, where the export of motion pictures, television programmes and music is vast. Although reliable statistical information is normally available for the export/import of goods, matters are more complicated in various service industries, such as in the case of payments for copyrights, which are normally not itemised separately in statistics. However, trade in cultural goods and products of the creative industries between countries has increased significantly in recent years, and there is little indication that this increase will cease.<sup>15</sup>

### 3.4 Means of enhancing cultural activity

One important factor in the production of cultural goods and in cultural policy is direct public support. It should be noted that the arm's length principle dictates that politicians should not be the parties who decide on the allocation of grants; those decisions are left to professionals in the field. Another method is to use some sort of peer review, where applications for cultural grants or for support of cultural production are scrutinised by peers; this method is widely used, for instance in deciding what contributions are published in academic journals, delivered at academic conferences and allocated to university research programmes.<sup>16</sup>

Direct support is assessed on the basis of objectives, methods and governance. Objectives refer to the need to consider the quality of cultural production and the access of the public to culture. Methods of public support refer, among other things, to the level at which the support is to be provided: for example, specifically for the artist's creative work itself after it is done and dusted; or in general cultural education in the hope that artists capable of producing cultural works will emerge as the result of a natural process; the construction of facilities for creative work or

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<sup>15</sup> For a discussion of the international trade in cultural goods see, e.g., Colbert *et al.* (2008) and *Creative Economy Report 2010. Creative Economy: A Feasible Development Option* (2010).

<sup>16</sup> For a discussion of the arm's length principle see, e.g., Ginsburgh and Throsby (2008) and Towse (2010).

for the staging of artistic events, such as concert halls and theatres. Support of cultural production is developed through subsidies and selling admissions to cultural events at a reduced price to enable the consumers themselves to use their limited financial resources in a manner of their own choice. This last method empowers consumers to create a demand for the cultural product instead of leaving matters to producers to create their own supply in the hope that producer taste will match consumer taste and result in the creation of a market that enjoys a certain degree of equilibrium.

Governance entails, among other things, privatisation in the cultural sector, for instance in the case of museums and concert halls, and is not as straightforward a matter as privatising banks, public transport providers or communications companies. Nevertheless, private enterprise can exist within the framework of a public system, as in the case of tendering of refreshment services in a museum or concert hall.

Support from the private sector can consist in sponsorship of events, where the sponsor is rewarded with an opportunity to advertise a product or brand. As a matter of fact, however, a sponsor's generosity may sometimes be subject to confidentiality for various reasons, in which case the sponsor receives no publicity and does not link the support granted to any individual, company or brand.

A public cultural policy need not in all cases be left in the hands of government. Associations of individuals can accomplish a great deal without direct government involvement. Non-governmental organisations play important roles, as in the case of choirs and amateur theatre companies. A public policy can, therefore, achieve a great deal of success by empowering such organisations, for example by means of allocations of funds.

The *Road Map for Arts Education*, issued by UNESCO addresses arts education, linking arts, education and community, by no means a simple task. This ideology is based on certain assumptions, such as that art and artistic creation are a prerequisite for quality of life. Most communities, if not all, want people to be able to engage in artistic creation. According to the *Road Map* art is a human right, even though this is not universally recognised; arts education should occupy a central position and it should be compulsory in the educational system. However, this is not always easy to achieve. If arts education is increased and the time available for teaching in general is limited, this means that something else has to give way and that can easily lead to disputes.

Art and culture provide opportunities for good living conditions resulting from the demand for cultural goods, their production and marketing. The argument for education in the arts is, therefore, much stronger than it was relatively recently, because most people are more aware of the pleasures associated with the arts and the benefits they provide than they were even a few decades or so ago.

### 3.5 Cultural heritage

Cultural heritage takes various forms. It can take the form of historic buildings, but also time-honoured traditions, customs or values. Financial activity in connection with cultural heritage can be extensive, for instance in the running of museums. Cultural heritage is the equivalent of cultural assets or cultural resources, and this heritage requires special treatment. It often needs to be reconstituted, as in the case of buildings or paintings. It is often overlooked that much of culture has been lost, and sometimes its preservation is a matter of chance or luck or the efforts of a few individuals.

Cultural heritage consists, firstly, of buildings or other immovable objects, such as monuments of various kinds. Secondly, there is moveable heritage, which includes works of art, books or other transportable objects. Thirdly, there is intangible heritage, such as music, tradition, language or other knowledge which is considered to possess cultural value. This intangible heritage is not only culture in itself, but also a source of culture.

Heritage, as a part of cultural capital, can reflect a fixed quantity, such as a historic building, or a flow, such as the operation of that same building, if it is a museum or attraction of some kind. Categorising heritage as capital brings into play the concepts of economics, such as investment, depreciation and yield, which can then be used to ascribe value. Yet again the dualism of economic value and cultural value proves its worth. A building, in and of itself, will always have some economic value. Constructing the building has its cost, but this can be augmented by a cultural element, and this increases the total value of the building.<sup>17</sup> Illustration 3 describes many of the concepts used in this chapter.

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<sup>17</sup> For a discussion of cultural heritage see, e.g., Rizzo and Throsby (2008), Peacock and Rizzo (2008), Throsby (2010) and Towse (2010).

### Illustration 3: Public initiative in cultural matters

Governments have often involved themselves in measures to reinforce the culture of their nations or cities. Among such measures are constructions of monuments, a long standing tradition in human history. The Greeks decorated their cities with splendid works of art that influenced artistic creation and art studies for centuries. The Romans continued on the same path, as evidenced by the historical monuments in Rome and elsewhere in the Roman Empire.

The Roman emperors not only built aqueducts and roads, which are still in use to this day, two thousand years after their construction; they also built stupefying monuments such as the Colosseum in Rome, which seated fifty thousand spectators. The Colosseum was a feat of engineering, but it also had a political purpose: it was the stage of huge games designed to gain the approval of the masses for power figures who otherwise might have been less popular. *Panem et circenses*, 'bread and games', was one of the mottos of the Roman emperors, reflecting their conviction that government figures had a responsibility to provide their citizens with food and entertainment through games. These were cultural events of the time, even though people often lost their lives in the course of the entertainment.

It was not only emperors who decorated their cities and supported art and culture, but also the church and various secular leaders. One of the best known patrons of the arts was the Renaissance leader Lorenzo de Medici, who was known as 'the Magnificent'; he and his family basically ruled Florence and what has been called the Florentine Republic in their time. De Medici contributed to the education of a number of artists, including Sandro Botticelli, Michelangelo Buonarroti and Leonardo da Vinci. His generosity, and that of his family, was renowned and is often taken as an example of what wealthy individuals can do in support of their environment. The same has happened elsewhere, as in the case of the United States of America, where moguls and wealthy families contribute vast sums in support of museums and art in general. An example is the Rockefeller family, which accumulated enormous wealth in the oil business and contributed a great deal of money to cultural matters. Sometimes these gifts are given humbly, and sometimes for self-aggrandisement.

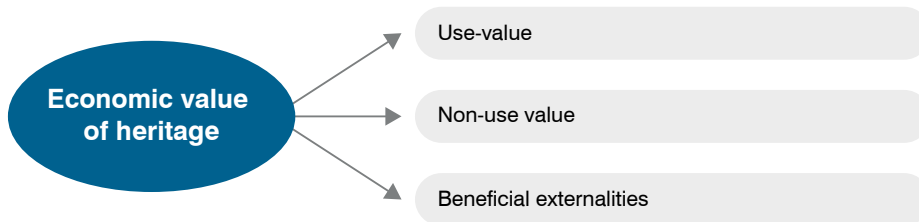
There are times when statesmen have reshaped entire cities, as in the case of Paris in the second half of the nineteenth century, when Napoleon III had Georges-Eugène Haussmann, Prefect of the Seine Department, design new buildings and streets in Paris and completely transform the city plan with the purpose, among other things, of broadening streets and reducing the risk of damage in case of fire. Many of the great avenues of Paris extend from the Arc de Triomphe, a fifty metre high monument celebrating France's military victories and housing beneath its vaults the tomb of the unknown soldier. This is the largest 'triumphal arch' in the world, and one of the principal sites of the city of Paris. A direct line of sight was drawn from the Louvre to the Arc de Triomphe. When a new Arch, one hundred and ten metres in height, was raised in La Defence, a district of Paris, a monument to humanity and its ideals, it was ensured that the plan should maintain the line of sight undisrupted.

Paris in many ways has the appearance of a metropolis, and it has been a constant ambition of French government figures to preserve the city's beauty. Recent presidents of France have not spared their efforts. For example, Georges Pompidou, President of France in 1969 to 1974, headed the construction of an avant-garde museum in Paris commonly referred to as the Pompidou Museum. The construction of the museum was hotly disputed and some of its critics said that it resembled an oil refinery;

nevertheless, it has gained the acceptance of Parisians, who are familiar with the feeling that it takes time to get used to new cultural assets. François Mitterrand, President of France from 1981 to 1995, had an annex built to the Louvre, including the large and famous glass pyramid; this was also disputed, but most people are now of the opinion that the enlargement proved a successful merger of the old and new to create an artistic whole.

In evaluating heritage, cost-benefit analysis, widely used in economic assessments, can be a useful tool. As regards culture, an assessment is made of the cost of preservation of heritage and the benefit of the preservation. All the costs of the preservation are then deducted. The increase in benefit must then exceed the increase in cost, but the benefit must be stated both in terms of cultural and economic value. Account needs to be taken of when the benefits accrue, that is, the present value of the benefit must be calculated by discounting future payments and the value of past payments must be adjusted to the present.

Cost benefit analysis can thus be used to calculate the benefit and cost of any individual decision or action. If several options are available and capital is limited, then cost benefit analysis can help to set priorities. For example, a conclusion could be reached as to which heritage should be the first to be preserved. In order to help in reaching a just decision, the benefit of cultural heritage can be divided into three categories, as shown in Figure 3.3.



**Figure 3.3:** The benefit of heritage

Value or benefit from the use of heritage, known as ‘use value’, can accrue, for example, when visitors arrive to view the heritage in question, for instance in a museum, and this entails economic activity. Value can also be derived from non-use, that is to say from not utilising the heritage. In such cases the value is assessed that does not directly relate to use, which we call ‘existence value’. Existence value is the term used when people want something to be preserved even if they have no intention of viewing it themselves, or where people wish to preserve something

for the benefit of future generations. An example could be the Angkor Wat temple complex in Kampuchea; most people are unlikely to have the opportunity to visit the site, but even so people generally would not want the world to be without it. There are many who want to have the possibility open for themselves, their children or future generations – or they simply want the heritage to exist as a remarkable witness to human endeavour.

The benefit of heritage can also result from externalities. Past heritage is often visible and tangible, as in the case of old buildings, such as churches, monuments, amphitheatres and statuaries, and such heritage can often be a foundation of contemporary culture without use of any kind associated with it. The economic value of heritage is created, however, with use of some kind. If we take as an example the city of Rome, which as a whole is a single living heritage, the city itself has cultural value. But economic value is created when the city is visited by tourists who stroll through the city's streets and partake of the ancient monuments. A price can now be put on their enjoyment, and we then have an example of a positive externality.

A heritage site need not be ancient or archaeological in nature. One example of a heritage site is the iconic Sidney Opera House, which qualifies as a member of the category as a result of its architecture, use and history; perhaps of equal importance, it has become a universally recognised symbol of Australia. And even though the Sidney Opera House is merely just over forty years old, it is listed as a UNESCO World Heritage Site.

Disputes are common between government authorities and the owners or possessors of heritage sites. It is not uncommon, for instance, for the aristocracy in the United Kingdom to own castles and mansions which are either archaeological or heritage sites; this prestigious classification means, however, that their alteration or use is restricted. Their owners may then feel that the encumbrances imposed by government are unjustifiably onerous.

In economics an instrument to resolve such disputes in the form of the Coase theorem has gradually emerged. The Coase theorem describes the economic efficiency of private party solutions. According to the theorem, if contracting entails no significant cost, that is, if the transaction cost of a particular contract is small, a private individual can resolve a problem posed by externalities by contract, thereby promoting the most

efficient use of the factors of production, in which case the intervention of public authorities is not needed.

A general example of the Coase theorem in action is one that involves a dispute between two neighbours, Jack and Jill: Jill's incessantly barking dog keeps Jack awake at night; they might be able to agree that Jill should get rid of the dog if Jack places a greater value on his sleep than the benefit that Jill places on owning the dog. If Jill values her ownership of the dog at five hundred dollars, and Jack values his discomfort at seven hundred dollars, then Jack could pay Jill six hundred dollars to get rid of the dog. On the other hand, if Jill values her dog ownership at a thousand dollars there can be no agreement, since Jack is loath to offer more than seven hundred dollars, and he will simply have to get used to sleepless nights. Oddly, it might seem, it makes no difference who is right in the eyes of the law. If Jill has the right to own a dog even if it barks, Jack could pay her to get rid of the dog if he values his discomfort as greater than her purported benefit. However, if Jack has the right to peace and quiet at night, then Jill can pay Jack for allowing her to keep the dog. For instance, if she values her benefit at a thousand dollars and Jack values his discomfort at seven hundred dollars, then she could pay Jack something like eight hundred dollars to keep the dog.<sup>18</sup>

The idea underlying the Coase theorem is that both parties should evaluate in economic terms the position that they represent and explore whether grounds for an economic agreement exist. Even though externalities can lead to market failure government is not always capable of resolving such problems. In many cases, individuals themselves can resolve the problem. Sometimes problems are resolved through codes of ethics, for instances by cultivating considerate behaviour. Transaction cost, that is to say the cost of establishing contracts, is a significant part of cost in the economy. If this cost is excessive, it will not pay to enter into a contract.

When government responds to negative externalities, two courses are available: on the one hand, powers of legislation or regulation can be employed; and on the other hand, it may be possible to seek market solutions by means of various taxes, such as pollution taxes, to give an example. Environmental issues can often be resolved using the methods of economics, because clean air and clean water are goods, just like other goods, and the price of goods is determined by supply and demand.

<sup>18</sup> For a discussion of the Coase theorem see Coase (1990) and, e.g., Mankiw and Taylor (2010).



Market solutions ensure efficient use of the factors of production, whether these factors are labour, fish, clean air, environment or creativity.

As regards policy on moveable heritage, such as paintings and sculpture, other viewpoints may apply than those that apply to stationary objects, such as buildings and the like. Paintings and sculpture have often been acquired by private individuals who enjoy them alone, lend them for public exhibition or, even worse, refuse to put them out on loan or grant public access to them at all. Such selfish acquisitiveness can also apply to antiques, which may be in demand among collectors, who often locate and obtain them on their own with no thought of making them available to the public or making provisions for their preservation. Formerly, all sorts of treasure hunts were carried out in an attempt to discover archaeological artefacts or hidden treasures that in addition to their cultural value have vast monetary worth. As a result it is now a criminal offence in many countries, and subject to severe penalties, to transport archaeological objects, often illegally acquired, across national borders.

Government policy regarding museums can be seen as a part of cultural policy, since the role of museums is mainly to collect and exhibit articles of art and archaeology; however, most museums own a far greater number

of objects than it is possible to exhibit, as part of their role of promoting education and research in the fields in which they specialise. Museums are, therefore, an important element of culture, particularly those that feature the archaeological finds of ages almost lost to the backward reach of history. A great deal of economic activity takes place in cultural museums, which often employ a large number of people. Because of the nature of museums, government has a particularly important role to play regarding their existence and operation.

As described earlier in the context of private consumption, the increase in the benefit of consumption will grow when a certain minimum level of consumption is reached. Since increased cultural consumption brings benefits, it is a matter of importance for

**John Maynard Keynes** was born in Britain in 1889 and died in 1946. He has often been called the greatest economist of the twentieth century. He worked both as a scholar and in the public sector as an advisor. Keynes criticised the economic impact of the peace treaties that followed World War I. His best known book is *The General Theory of Employment, Interest and Money*, which appeared in 1936. Among other things, the book highlighted the importance of vigorous state intervention in the economy to avert economic crises and promote full employment. Keynes played an important role in the establishment of the International Monetary Fund and the World Bank. He was a good fund raiser, he taught primarily at Cambridge University and was known for his one-liners. On the phrase „in the long run“, a common phrase in economics, he said: „In the long run we are all dead“.

government to promote the achievement of this minimum level. Such consumption can be achieved, for instance, by charging no admission fees to museums, a common arrangement in the United Kingdom. In fact, this is not a new policy, since in the United Kingdom, beginning in the nineteenth century, admission to museums was free as a part of government policy at the time to bring the arts to the masses.

The revolution in electronic and digital form and presentation has resulted in an increase in the preservation of artefacts and in the number and variety of exhibitions. Access to museums through the Internet and visual presentations have also increased public interest in this area of culture, and this trend will no doubt increase still further in the future; this access has the characteristics of public goods. The use of multimedia technology has, therefore, been one of the most important aspects of the work of today's cultural managers.

A great deal of international work is done in matters of heritage in the world, in particular by UNESCO, which maintains an annually updated World Heritage List that dates from 1972, with effect from 1977. UNESCO is also responsible for the Convention for the Safeguarding of the Intangible Cultural Heritage of 2003, which, among other things, focuses on oral traditions, including the preservation of languages, primarily those that are in acute danger of extinction. This effort is comparable to the efforts to protect animal species which are perceived as being in danger of extinction. The principle of sustainability also applies here. If animal species, languages or customs become extinct, then those cultural assets will no longer be available to future generations, and the disappearance of these cultural artefacts will constitute an enormous loss not to be computed in economic terms alone.<sup>19</sup>

UNESCO's World Heritage List includes seventy-nine cultural sites, 197 natural sites and thirty-one sites which are both cultural and natural sites. A total of 160 countries have sites on the UNESCO Heritage List of 981 sites.<sup>20</sup> Almost all the countries of Western Europe have more than one site on the list and many have several, as do the United States of America and several other countries.

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<sup>19</sup> For further information on the preservation and registration of heritage see, e.g., the *Convention Concerning the Protection of the World Cultural and Natural Heritage* (1972), the *Convention for the Safeguarding of the Intangible Cultural Heritage* (2003), Smith and Akagawa (2009), and *Cultural Statistics* (2011).

<sup>20</sup> For information on the registration of sites in international lists see *Cultural Statistics* (2011) and the *World Heritage List* (2015).

### 3.6 Global public goods and creative areas

Public goods can be discussed in an international context as, firstly, global public goods whose main characteristic is their accessibility. This means that culture, as a global public good, must by definition be available to all, or at least most, people in the communities in question. Cultural events in the past were often the exclusive domain of the privileged few, the upper classes and nobility, but this is incompatible with the requirements of modern society. Secondly, culture as a global good must extend to more than a limited number of countries to have the required international dimension. Thirdly, culture as a global good must meet the requirements of current generations without prejudicing the possibilities for future generations to meet their needs, which again highlights the applicability of sustainability as a concept in the context of culture.<sup>21</sup>

It is important to understand how culture influences the lives of people in urban settings, since cities are the melting pots of culture. Art and cultural events are enormously influential factors of city life and in fact contribute to the existence and development of cities. Single cultural buildings or festivals can generate extensive economic activity; some examples are the Guggenheim Museum in Bilbao, the Taj Mahal in Agra in India, the Great Wall of China or the music festivals of Salzburg or Bayreuth. The cultural industry and the creative industries thrive in cities, with each drawing strength from the other.<sup>22</sup>

Urban areas fall into various categories; they can be towns, cities, counties or even states or provinces. Urban area refers to a geographically defined unit where two factors exert the greatest influence as regards culture: the cultural infrastructure, and the fertility of the environment for cultural industries. Cultural infrastructure refers to capital, including human capital and cultural capital, tangible and intangible.

Public policy in this regard is often focused on increasing available capital and resources and renewing older assets or putting them to new use. This maintains a continuous creation of value. Living conditions relate, among other things, to transportation, education, services and other infrastructure, in addition to intangibles, such as a sense of community and atmosphere in general. Culture is often the foundation of human

<sup>21</sup> For a discussion of global public goods see, e.g., Kaul *et al.* (1999) and Held (2004).

<sup>22</sup> For a discussion of culture and cities see, e.g., Landry (2000), Bailey *et al.* (2004) and Throsby (2010).

society, particularly in small locations where culture can be a mainstay of the economy.

As regards creativity, it is possible to speak of creative regions and creative cities, just as it is possible to speak of creative industries. Theories along these lines have given rise to controversy, but creative work in cities is something that cannot be ignored, and some places are more active in this regard than others.<sup>23</sup> In creative areas knowledge is aggregated and similar activities are mutually supportive.

Discussions of creative cities focus, among other things, on changes in the economy, since factory manufacturing in urban areas is now much less widespread than it used to be. Labour of this kind has migrated to rural areas, or even abroad from western countries to countries in Asia, where the cost of land and labour is lower. Value production in cities is, therefore, more in the line of creativity and in the production of cultural assets. UNESCO and the EU have established a network of creative cities to enable them to share their experiences with others and thereby achieve greater efficiency.<sup>24</sup>

The role of architecture is important in this context, and the Sidney Opera House, mentioned earlier, and the Guggenheim Museum in Bilbao illustrate how single architectural masterpieces have achieved an emblematic status of the cities in which they are located. These architectural works also have an extensive economic impact and create both tangible and intangible value, for instance by becoming landmarks that attract tourists: old buildings can gain a new purpose, as in the case of the Tate Modern in London, which used to house a power station, or the Musée d'Orsay in Paris, which was originally a railway station.<sup>25</sup>

Cultural policymaking in cities, for instance to increase the weight of the creative and cultural sectors, can be divided into a number of elements, which include ensuring a sound infrastructure, providing access to investment capital (in particular for small and medium-sized enterprises), creating a favourable social framework and atmosphere, promoting empowerment in decision-making and supporting core activities in

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<sup>23</sup> For a discussion of the creative class see Florida (2005), Rausch and Negrey (2006), Markusen (2006) and Florida (2008).

<sup>24</sup> For a discussion of creative cities and the cultural cities of Europe see, e.g., Landry (2000), Richards and Wilson (2004), Throsby (2010) and *Cultural Statistics* (2011).

<sup>25</sup> For discussions of cultural buildings see, e.g., Plaza (2000), Drew and Browell (2002), *History of Tate. Tate Modern* (2015) and *A view of cities. Orsay Museum (Musée d'Orsay)* (2015).

artistic creation. These elements can be measured in order to gauge the success of different policies and the effect of financial allocations in support of creative and cultural activities.

Culture, as an important element of the economy, is given much more attention now than before. There are several reasons for this, including the great diversity in economic development in individual countries and profound changes in the human environment, which are, not least, a result of cultural influence. The present is a remarkable period in human history, where changes are more rapid than ever, diversity is prominent and international development is swift. All of human society is in a flux, partly because of improved transportation and partly because of the improved communications technology of the Internet. Science has also made enormous progress, with the result that the models used for analyses of all kinds have become more and more precise.<sup>26</sup>

Human behaviour has become increasingly diverse and it has also changed markedly in the course of only a few decades. The experience industry, a direct product of culture and a part of the cultural industry, has become extremely large and is constantly growing. People have more and more time to engage in activities other than working and sleeping. Work itself has also become more diverse, and in many cases the line between work and recreation has become increasingly unclear. Vast numbers of people are now employed doing what they most enjoy. This applies equally to artists and scientists in universities and professional athletes.

### 3.7 Culture and development

Culture has greater significance now than ever before, because for most people freedom of activity has increased. A profound change has occurred in this regard in the last hundred years or so. At the dawn of the twentieth century the world population was 1,600,000,000 people, but in 2015 that population had grown to 7,600,000,000, up by 5,600,000,000 people in only 114 years. The growth in population is projected at about two billion people over the next thirty years.<sup>27</sup> This growth will occur almost exclusively in the developing countries and will make all

<sup>26</sup> For a discussion of changes in cultural economics see, e.g., Appadurai (1996), Björkegren (1996), Bendixen (2010), Barker (2003) and Baumol (2008).

<sup>27</sup> For information on population growth in the world see, e.g., *Current World Population* (2015).

historical comparisons almost meaningless. The framework of culture is now totally different from the framework of 250 years ago when economics as a social science came into existence.

One widespread problem in the developing countries is known as the 'brain drain', the movement of educated people away from poorer countries to richer countries to improve their own standards of living. As a result, poorer countries are losing the ability to develop cultural policies that benefit themselves. Thus, an international perspective in cultural policymaking is much more important now than it was in the past. Cultural policymaking is now a key element in general policymaking for society and in development affairs. It is impossible to separate the concept of development from the concept of culture.

The importance of culture in development aid is a significant theme in the discussion of development. There are three major viewpoints regarding the way in which development aid can be administered in the most efficient manner. Firstly, it is important to consider whether globalisation could pose a risk to cultural diversity. National cultures are far more vulnerable than ever before as a result of globalisation, and this can pose a risk to cultural diversity. Things may be lost that must not be lost.<sup>28</sup>

Secondly, it is important to solve the problems of developing countries using tailored measures. It must be kept in mind that of the seven billion people or more on the Earth almost one billion suffer hunger and malnutrition, nearly all of them in developing countries.<sup>29</sup>

Thirdly, in relation to culture in the context of development aid, there is the recognition in cultural groups and cultural areas that their sense of identity and self-esteem must be preserved. In order to strengthen people

**Wolfgang Amadeus Mozart** was born in 1756 and died in 1791, only thirty-five years of age. In his brief lifetime he composed over 600 works and he is considered one of the foremost composers of all time. Mozart was a *Wunderkind* and had begun composing music at the early age of five. He worked in the service of emperors and noblemen and for a time accumulated some wealth, but he never achieved a state of financial security for a variety of reasons, including an expensive lifestyle and gambling debts. Mozart was a colourful personality of chaotic character. His musical creations range from cantatas to operas and chamber music to symphonies including the Austrian national anthem. A great deal has been written about Mozart, and his life and work has been the subject of books and films, but his image has been created and recreated so many times since his death that these are not always historically accurate sources of information.

<sup>28</sup> For a discussion of the importance of culture in development aid, there see, e.g., Sen (1990), Kapur (2002) and Barrowclough and Kozul-Wright (2008).

<sup>29</sup> For a discussion of malnutrition in the world see, e.g., *Hunger Stats* (2015).

mentally, improve their self-esteem and create a sense of identity, there is hardly a better route than to focus on the culture of groups and regions. It is essential to highlight what is of significant importance and what enables people to survive and to bond in perpetuity.

A number of international organisations work worldwide on development projects, such as the World Bank and the International Monetary Fund. Their policy is to look at culture and cultural perspectives as an opportunity to assist poor communities. Culture should be a venue for new opportunities, and regional development can be encouraged by means of dedicated assistance relating to culture and cultural events. The discussions currently in progress in the World Trade Organisation to reduce barriers to trade are the most important discussions of development aid that have been held for decades.<sup>30</sup>

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<sup>30</sup> For a discussion of development aid and culture see, e.g., Woods (2000) and *Understanding the WTO: Developing countries* (2015).

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## 4. International trade and markets

International influence is nothing new in culture, because all cultures have always been influenced by other cultures. What is new in the contemporary picture is that individual national and ethnic cultures are under much greater pressure and threat than ever before of being subsumed by dominant foreign cultures. Cultural influences come from all directions, and they are much stronger than at any other time in history. A key feature of globalisation is the pace of its influence on cultural diversity and the ability of smaller states, in particular the poorest ones, to resist. In bygone eras communities had time to adapt to external influences because such influences moved from country to country at a more leisurely pace. Now the spread of influence resembles the force of a tsunami rather than the pace of a camel caravan, and there is much less time, for better or worse, to react to or resist such influence.

International trade in cultural goods is growing, including trade in goods such as works of art, films, television programmes and music. Artists travel from country to country in an international labour market, and cultural goods are traded, as in the case of touring musicians and repertory companies. Museums exchange artworks in international cultural exchanges, and international cultural tourism is a large and growing industry.

Art markets have been studied extensively, the principal reason being that art auctions have a long history, and data that extend far into the past are a present feature of the market. Art markets and culture markets are similar to other markets, with the difference that the former are more subject to taste and fashion than, for instance, a commodity exchange.<sup>1</sup>

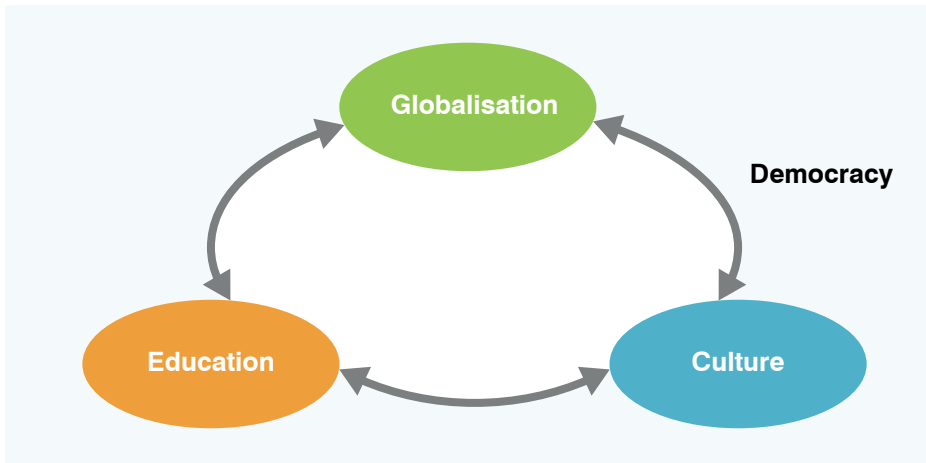
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<sup>1</sup> For a discussion of international trade in cultural goods see, e.g., Montias (1982), Hughes (2000) and Acheson and Maule (2008).



## 4.1 Globalisation

Culture, as a heritage from past generations, and education, are the key to progress in today's technologically advanced societies and a prerequisite for the efficient use of factors of production. Figure 4.1. shows certain key concepts, that is, education, culture, globalisation and democracy, that are of fundamental importance for countries in their quest for improved living conditions. These key concepts are also of fundamental importance for a diversified and efficient community.



**Figure 4.1:** Model of key concepts for national standards of living

Figure 4.1 shows globalisation, education and culture influencing and interacting with one another, embedded in democracy to illustrate the fact that relations between countries are constantly deepening and the number of countries included in the relationship is constantly growing. Globalisation characterises the framework of modern communities more than most other things. The communities that are most characterised by extensive cultural activity, flourishing and diversified education and strong globalisation are generally democracies, and the living standards of those countries are among the best in the world. It should be noted that even though democracy is acknowledged by most people as the best form of government, not many countries in the world can boast of a democracy that has been in place for many decades.<sup>2</sup>

<sup>2</sup> For a discussion of globalisation see, e.g., Huntington (1984), Salvatore (2011) and Payne (2012).

Figure 4.1. illustrates the framework of the countries that enjoy the best economic welfare, and it therefore seems logical that the developing countries should perhaps aspire to this form of government. The unequal distribution of wealth in the world is a challenge to be addressed in cultural economics, because the solutions consist in making use of limited factors of production in an efficient manner, ensuring equality among citizens and organising the economy so as to take account of the cultural trends in each community.

However, a number of social scientists maintain that globalisation consists primarily in spreading western values.<sup>3</sup> This spread applies first and foremost to the international cultural industry in films, music and television. It can be argued that the culture that now flows across the world reflects the national cultures of individual countries only in a very limited manner and is rooted primarily in the culture arising out of the English speaking world, particularly the United States of America.

English is the language of globalisation, trade and science and long ago replaced Latin, the *lingua franca* of earlier times. There may have been a number of languages in trade and international relations well into the last century that enjoyed this status, but it is now English that occupies the position of supremacy. This makes the spread of Anglo-Saxon culture even easier than it might otherwise be, as can be readily ascertained by looking at the television programming in most countries.

The globalisation of culture has deep historic roots. International relations have always existed, but they are more pervasive in our times than at any other time in history. The trends since the mid-eighteenth century, the period of the industrial revolution, have primarily emanated from the countries of Western Europe and the United States of America. These countries have also fought for dominance, most prominently in two world wars that were waged in the twentieth century. However, it should be noted that some academics believe that globalisation will lead to a kind of tribalism within demarcated areas where an attitude of ‘everyone for himself’ will prevail.<sup>4</sup> Perhaps we are already observing this trend in progress, when fundamentalist religious values have now become more prominent than they were just a few decades ago, and extremism has gained ground in a number of regions of the world.

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<sup>3</sup> As an example of this viewpoint see Altvater and Mahnkopf (2007).

<sup>4</sup> For a discussion of the impact of globalisation on regional cohesion see, e.g., Kaul *et al.* (1999).

Advances in cultural activity have often been circumscribed by country borders, although it can be argued that cities such as Venice, Florence, New York, Paris and Vienna have sometimes had greater importance by themselves than the countries in which they are located – in any case borders in Europe were constantly shifting throughout the nineteenth and twentieth centuries. When different cultural worlds meet, rapid progress is often the result, as in the case of the United States in the eighteenth and nineteenth centuries. Human history is in many ways the story of relations between cultures.

International relations are often necessary for cultural advances, as in the case of the Greek cultural heritage for the countries of Europe, Northern Africa and the Near and Middle Eastern countries. Much the same thing happened when Arabic culture had a deep and lasting impact on Spain and other southern European countries. Technological advances have also brought about profound changes. Electricity and its harnessing is probably the most important discovery made in the last two hundred and fifty years. Electricity and external energy are among the revolutionary forces of recent centuries that have shaped today's environment, particularly from an economic standpoint.

The spread of the Internet in our times is taking place even faster than the spread of electricity after its discovery. From 1922 to 1947 the number of households with access to electricity in the United States increased from 40% to 80% – that is, it took a quarter century to spread to 80% of households. From 1999 to 2012 the number of households with access to the Internet in the United States increased from 40% to 80% – it took the Internet only thirteen years to spread to 80% of households.<sup>5</sup>

It is not always clear whether technical progress originates in the United States, Japan, Germany or other technologically advanced countries, but this is not really relevant. Many modern corporations know no borders and operate in a number of countries. The economy no longer recognises the old national borders in the same way as before.

The system that is responsible for the dissemination of culture is closely related to various organisations, whether in the case of written or spoken material, television or radio broadcasting or the Internet, which is a powerful distribution network of culture and information. In many countries the state controls a part of the dissemination of culture by funding and

<sup>5</sup> For a discussion of the spread of electricity and the Internet see Bowden and Offer (1994) and *Internet Use Over Time* (2015).

operating radio or television broadcasting. Often it is the private sector that is responsible for the production and distribution of cultural goods, as in the case of film and music. In fact, private initiative and private enterprise are prominent in the cultural industry.<sup>6</sup>

Culture has gained, but sometimes also suffered, from foreign influence, and we need to ask ourselves whether globalisation poses a risk to cultural diversity. The reason that globalisation has gained such enormous importance so quickly is, more than anything else, economic. The efficiency and improvements in living conditions that result from globalisation have come about because globalisation offers a number of advantages – a larger market, to mention just one. Transaction cost is also lower than before globalisation, and knowledge is disseminated much faster around the world than before. Globalisation can bring opportunities because it increases knowledge of different societies, which can promote peace.

Whether all these ‘advantages’ are in fact beneficial may be disputed, but it is clear that larger markets, greater speed and lower transaction cost have a direct impact on improving living conditions. Still, there are also those who worry about globalisation, saying that it has a negative impact on the environment and that it entails only the freedom of capital, which flows across the world without restrictions and with no concern for the environment or nature in general.

Economic growth, which is a measure of the annual increase in domestic product, or value creation, differs greatly from one region to another and from one country to another. Although the industrialised countries are characterised by high domestic product, not only in volume but also per capita, their economic growth may not be any greater than in many developing countries. Economic growth is an important measure of the strength of an economy, but in fact history has shown that countries with strong economic growth will not necessarily maintain their advantage. Nor is it axiomatic that poor countries must be forever mired in poor living conditions and low domestic product. One of the principal explanations of differing economic growth is difference in productivity or efficiency.

Access to enormous natural resources is not a condition for strong economic growth or high standards of living. Japan is a good example of a country with limited access to natural resources but a high standard of

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<sup>6</sup> For a discussion of the distribution of culture see, e.g., Held and McGrew (2003) and Ingimundarson *et al.* (2004).

living. Denmark, which ranks second on the world prosperity index, has scarcely any natural resources at all but benefits from an abundance of human resources, advanced technology, knowledge and skills. The Danes buy their supplies from all over the world and transform them into valuable goods (such as design furniture and dairy products, to name just two export goods), which enables them to produce huge value per capita. Human resources are in fact one of the most important factors of production in a contemporary society. With the increasing use of technology and the ongoing process of transformation to a knowledge society, the creation of value depends more and more on information and the processing of information and knowledge. This single factor of production has, therefore, become much more important in recent decades than before. Culture creates human resources and it creates comparative advantages, which means that culture contributes to economic growth.

International trade has been characterised in recent years by a significant growth in trade and services, changed communications, reformed rules of international trade and the seemingly endless potential of the Internet. The extensive internationalisation of cultural goods has raised fears in some quarters that their culture may be drowned in the relentless tide. This issue has, therefore, received a great deal of attention in a number of international venues and organisations, such as the World Trade Organisation.<sup>7</sup> The question has been raised whether special rules should be applied to cultural goods in order to enable nations and countries to protect their own cultures from imported culture. However, this is inconsistent with the fundamental principles of international free trade, which maximises economic benefits; these arguments are, therefore, in direct opposition to one another.

There are arguments for and against the special treatment of cultural goods. Among the pro arguments is the contention that cultural goods have value that transcends mere economic value and that traditional markets do not properly reflect that value. In addition, cultural goods are central to the self-perception and national identities of individual countries and, therefore, need to be protected for the public benefit. Strong domestic cultural production is important for cultural diversity, which could be put at risk by cheap imports, which often enjoy their price advantages to combat competition, and for this reason a close eye has to be kept on world trade in cultural goods to prevent an unfair

<sup>7</sup> For information on the discussions in the World Trade Organization see, e.g., *Understanding the WTO: Developing countries* (2015).

advantage, one that is not market-oriented. Finally, the cultural industry is often weak, especially at the outset, and should, therefore, enjoy some protection in its developmental phase. There are also some arguments against special treatment for cultural goods, the principal argument being that special protection will result in market distortion and lead to inefficiency. It is also frequently mentioned that the drive for protection is highly tendentious, originating among market participants who are out to protect themselves and their own interests rather than their respective cultures. Finally, it is argued that protection entails restrictions on individual freedom of choice and that free trade in cultural goods increases cultural diversity.

In 2005 UNESCO drew up a convention to promote cultural diversity, which took effect in 2007.<sup>8</sup> The Convention addresses the importance of ensuring cultural diversity, with special emphasis on protecting culture that is at risk. In reality, this is primarily a protective reaction against the strong American media companies, in particular the broadcasting media, motion picture industry and television programming. The Convention provides for protection, but contains no provisions on the details of the arrangements of such protection.<sup>9</sup> It addresses measures in the event of threats to local culture, for instance if cultural diversity is at risk, but such measures are sometimes controversial, since domestic producers, as mentioned above, are often merely protecting their own special interests. However, there can be real danger, for example if a language is under threat in a small language area as a result of unrestricted imports of foreign-language material. Protection can also be justified if a domestic market is simply too weak to support domestic undertakings in competition with large foreign corporations. Nevertheless, despite all these efforts, international trade in culture is largely unrestricted.

One of the features of globalisation is the increase in tourism, which has become an important economic sector in many countries, and culture is a key factor in this growing economic importance. Tourism can be divided into two main streams. On the one hand there is a large group of tourists who invest in cheap transport, cheap lodging and relatively simple recreation. Examples include travels to sun resorts, as in the case of northern Europeans who crowd the beaches of Portugal and Spain and other countries on the Mediterranean and enjoy cut-rate (all inclusive)

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<sup>8</sup> For further information see the *Convention on the Protection and Promotion of the Diversity of Cultural Expressions* (2005).

<sup>9</sup> For a discussion of government protection in the culture sector see, e.g., Graber (2006).

hotel packages. On the other hand there is cultural tourism, which is an expensive service for comparatively few individuals with carefully planned offerings of cultural events or natural sites.

The tourist industry is a low-pay industry in most parts of the world. Jobs connected with the tourist industry in hotels and restaurants consist in the provision of basic service which is necessary but does not require specialised labour and is cheap by its very nature. It is, therefore, important to examine tourism from a different perspective, such as the perspective of culture, in order to generate additional income.

Culture can be of great significance for a place or for a city, and this influence can be divided into several factors. Firstly, cultural buildings can become icons for a place or city, like the Eiffel Tower in Paris, Big Ben in London, the Kremlin in Moscow and the Forbidden City in Beijing. These are the landmarks of their cities, and they have their origin in creativity. Secondly, cultural areas are often located in cities, as in the case of the West Bank of the Seine, which has played an important role in the cultural life of France, and the centre of Copenhagen, which is in many ways a melting pot of culture. Thirdly, exhibitions and facilities for exhibition can play a prominent role in the image of an area or a city, as in the case of the Metropolitan Opera in New York or La Scala in Milan. Fourthly, a certain area can be a crucible of creation, as in the case of Greenwich Village in New York and Soho in London, where cultural events of all kinds are a feature of daily life. The economic impact of these cultural landmarks is that they generate income. Tourists buy works of art and souvenirs, and they create a market for hotel operations and restaurants that are frequented not only by tourists but by the domestic population as well.

Cultural exchanges between countries can be extensive even if they do not entail significant economic activity. These exchanges may take the form of markets featuring artists working through agents or agencies, as in the case of opera singers travelling between opera houses and performing in the roles that they have chosen to master. Contracts of this kind are often made many years in advance. Artists have always toured in this way from country to country, theatre companies and orchestras being examples, and something similar happens in the case of motion pictures, which are often produced in cooperation between two or more countries.<sup>10</sup>

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<sup>10</sup> For further information on artists' tours and touring contracts see, e.g., Radbourne (2008) and Towse (2010).

Relations of this kind represent an aspect of government policy designed to exert influence in the world, and cultural exchanges are now often the preferred option over the exhibitions of military might in the ostentatious parades that characterised the past. Cultural relations are often also a precursor of trade, so that government policy of this kind is rooted in strong pragmatic economic arguments. Cultural relations are, therefore, a part of the foreign policy of most countries.<sup>11</sup> One of the positive externalities of these relations lies in combating population growth, which has been extraordinary in the last century. The question has often been raised whether the earth's natural resources will restrict economic growth and further population growth.<sup>12</sup> The reasons that restricted economic growth has not become the problem that so many have feared are advances in technology, especially in agriculture, and greater efficiency in the use of natural resources.

Cultural exchanges have been a part of human history since ancient times and continue to exert their influence. However, as political hardliners and religious fundamentalists are gaining ground in the world, the ethical principles of culture, such as charity, can become signposts to lead us out of the problematic state of current relations in a world of surging populations, growing hunger and unacceptable living conditions. Increased cultural relations could, therefore, help to take humanity forward

## 4.2 The efficiency of global trade

The goods produced in the cultural industry are traded in global markets. The impact of global trade is made clear if we compare in a basic model demand, supply, price in equilibrium and world market price before and after international trade. If the world price of a good is higher than the domestic price before the start of international trade, the producing country will become an exporter of the good and the domestic price will gravitate toward the world price.

On the other hand, if the world price is lower than the domestic price before international trade begins, it is advantageous for the country involved to become an importer. This is a manifestation of comparative

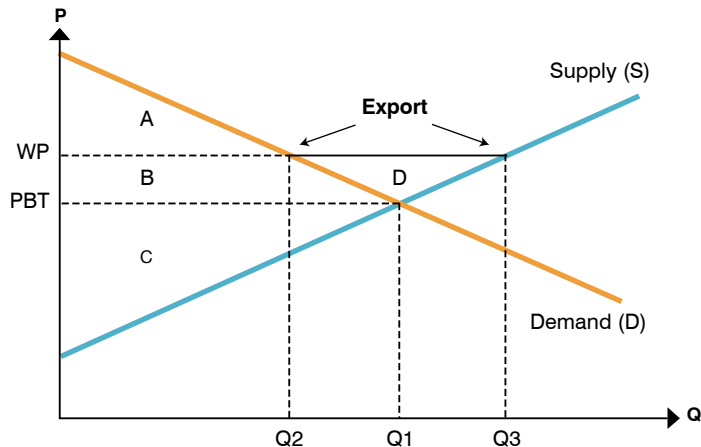
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<sup>11</sup> For a discussion of culture and foreign policy see, e.g., Whitfield (1996), Yúdice (2003) and Nye (2004).

<sup>12</sup> An example of this line of discussion can be found in Auty (2001).



advantage. If the price of goods is lower in one country than elsewhere in the world, then that country will enjoy a comparative advantage and export the goods. Figure 4.2 illustrates the situation when the world price (WP) is higher than the domestic price before trade (PBT).

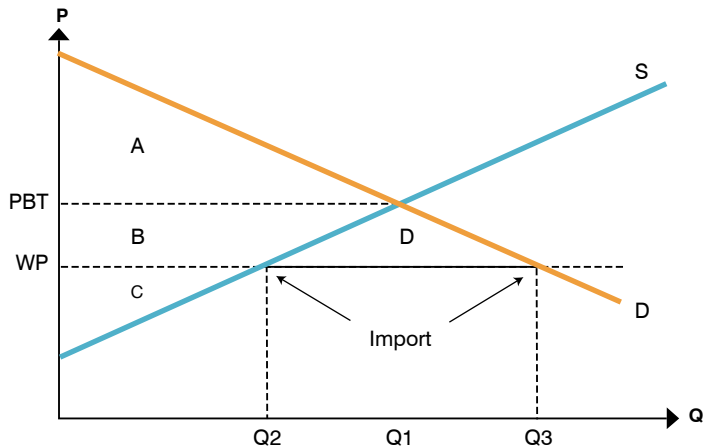


**Figure 4.2:** Export

In Figure 4.2 the domestic price adapts to the world price; that is, excess supply is reached, which is countered by export. The price becomes higher in the domestic market, which means a reduction in the quantity available to domestic consumers. The consumer surplus for domestic consumers falls, while the producer surplus for domestic producers increases. However, the producer surplus increases more than the loss of consumer surplus. When a country becomes an exporter of a good, this results in increased benefits from that trade.

Figure 4.2 shows a triangle delimited by A+B consumer surplus before international trade begins, and the producer surplus is a triangle delimited by area C. After trade begins, consumer surplus becomes a triangle delimited by area A and the producer surplus becomes a triangle delimited by area B+C+D, which means that international trade will increase the benefit of the trade by a triangle delimited by area D.

Figure 4.3 illustrates the situation when the world price is lower than the domestic price before the beginning of international trade.



**Figure 4.3:** Import

As shown in Figure 4.3, the price of goods in the domestic market adapts to the world price and an excess demand is created, which is met by importation of the goods. Consumer surplus before international trade is the triangle delimited by area A and the producer surplus is the triangle delimited by area B+C. Following the start of international trade the consumer surplus becomes the triangle delimited by area A+B+C, while the producer surplus becomes the triangle delimited by area C. The surplus from the trade therefore increases by the triangle delimited by area D. The consumer surplus increases by more than the loss of producer surplus. Opening up to imports and exports thus results in a significant surplus, whether or not the country becomes an importer or exporter.

If a country permits trade and becomes an importer for reasons of lower prices abroad, domestic consumers benefit, while domestic producers lose. Conversely, if a country becomes an exporter of products the producers profit while consumers will suffer. However, in either case the trade will entail greater profit than loss, with the result that living standards will improve as a result of foreign trade. International trade is efficient, and restrictions on such trade have a negative impact on living conditions in the countries that impose the restrictions; this applies to trade in cultural goods just as it applies to all other trade. It makes no difference in this context whether the trade in cultural goods is supported by government or not. The efficiency of free trade between countries is one of the fundamental laws of economics.

Nevertheless, while liberalised international trade may be efficient, it may still be necessary to take steps to protect cultural diversity. Many countries take measures to ensure a certain minimum supply of their own culture. It is not uncommon, for instance, for state broadcasting media to be required to broadcast domestic programming in significant quantities in order to counteract the overwhelming influence of American popular culture. For years work on reducing tariffs and eliminating restrictions on trade was conducted within the framework of the General Agreement on Tariffs and Trade (GATT). The role of GATT was subsequently assumed by the World Trade Organisation, which is intended to promote liberalised international trade.

### 4.3 Marketing mix

A firm's marketing strategy will normally have three principal aspects: a decision needs to be made on marketing expenditures, including advertising; on the division of marketing costs between individual products; and on the proper mix of selling solutions or marketing solutions. This 'marketing mix' refers to decision making on four ingredients: product, price, place and promotion, often called the 'four Ps'.

This traditional marketing mix, involving the four Ps, can be restated using four other concepts (sometimes referred to as the four Cs): customer value (instead of product), customer costs (not just price), convenience (instead of place) and communication (instead of promotion).<sup>13</sup> This concept is better suited to the cultural sector, since value and communication are important to consumers and price is what an individual pays, while value is what the individual receives.<sup>14</sup>

Making a decision on marketing consists, among other things, in deciding what product categories should be produced, at what price they should be sold, how they should be promoted or advertised, and when and where the products should be sold – for example whether they should be sold in a supermarket or a specialty shop. Decisions on choice of product include the product and service range, and the price is connected with various factors, such as payment terms.

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<sup>13</sup> For a discussion of marketing in the cultural sector see Bernstein (2007)

<sup>14</sup> For a discussion of the difference between price and value see Buffet (1996).

The promotion of goods and services is a prominent feature of modern economies, and this is particularly true of the culture industry, where competition is fierce. Advertising is an important feature of promotion, particularly in competition, but consumers can also be reached by other means, such as direct marketing and public relations. Advertising is often used to build a certain image of a company in the eyes of the public. To give an example, the Metropolitan Opera in New York and the Scala Opera in Milan have built a reputation for quality staging of operas.

Advertising is closely related to branding. Firms will frequently attempt to link their products to a brand in order to create an image of quality, a strategy that enables them to sell their products at a higher price. Critics of branding allege that brands are used to create a false distinction between products that in reality are the same and that a generic product, especially in the pharmaceutical industry, is often just as good as a brand-name product. Some critics say that consumers prepared to pay a higher price for brand names are acting irrationally in response to elaborate advertising campaigns, especially those mounted on television. The brand-name advocates, on the other hand, claim that brand names are an assurance of quality. It is contended that a brand name conveys information on quality and responsibility in production and that inherent in a brand is an incentive for business firms to maintain their market strength, since the brand itself represents established value that influences other aspects of a company's work. In the cultural industry brands have a special importance, since works of art are almost invariably associated with the names of their creators or performers, as the case may be, and those names then become, in effect, brand names.

A brand reflects trust between a company and its customers, and it is, therefore, important for the brand to reflect the company's image and its positive bond with customers. It is also important for the brand to contribute to the creation of a loyal and stable customer base, where customers engage in a steady business, for instance by attending regular performances at a certain theatre or buying and reading all the books of a particular novelist. Business firms, therefore, have to take good care of their brands. In the culture sector it is often of primary importance for customers' experiences to meet the expectations raised by a brand name, whether the brand name is associated with an individual artist, an orchestra, a publishing company or any other entity that produces cultural goods. Illustration 4 describes many of the concepts discussed in this chapter.

#### Illustration 4: International marketing in culture

International marketing is not a new phenomenon, and history can provide numerous examples of countries creating international markets for their products and even attempting to corner markets and keep them for themselves. Silk, for instance, was an important and extremely valuable Chinese export for centuries and measures were taken to prevent the export of the moth that made silk production possible – measures that were effective for a long time.

Some products are marketed all over the world, a case in point being the 120-year-old soft drink Coca Cola, which can be bought almost anywhere on the globe. The Coca Cola brand is one of the best known and most valuable brands in the world, and its logo is equally recognisable and distinctive. A brand can also take different forms. The name of an artist, or a building, can become a sort of brand name: the name of Steven Spielberg will attract customers to films, and the name of the Louvre will attract customers to Paris.

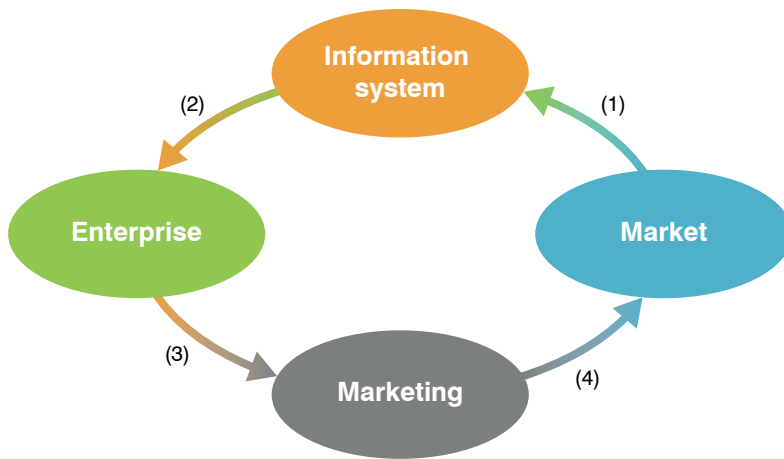
Precise planning and market strategy is essential for success in the cultural sector. An example of a successful effort in this direction is the San Francisco Ballet, which gained a new lease on life under the artistic direction of Helgi Tomasson in 1985. The methods used were based on professional and precise planning over the course of a number of years, drawing on all the most recent and advanced scholarship in the field, and the San Francisco Ballet is to this day recognised as one of the foremost ballet companies in the world.

Mass production has also been a feature of artistic creation for a long time. Take, for instance, the case of the well-known composer Johann Strauss, the Elder. In the heyday of the Vienna waltz the City of Vienna was a city of music. In this setting Strauss, the Elder, formed a number of orchestras. They performed in the evenings in Vienna, and Strauss himself made the rounds, occasionally taking the baton in hand and making his mark on the music. This was mass production in a sense, although somewhat specialised in nature. The novelist Alexandre Dumas, to take another example, negotiated a contract with his publishers to be paid by the line. His stories first appeared in print in magazines. He would decide on a plot and hire people to write drafts for him, which he then read and edited. This was yet another form of mass production for its time. Dumas is one of the best known writers of adventurous tales of all times, and his *The Three Musketeers* and *The Count of Monte Christo* are known and sold all over the world.

But contracting in the cultural industry can be difficult, since it is impossible to know the success of the product beforehand. The Beatles became one of the most successful bands in music history, but their contracts with EMI were far from lucrative for them and it would be many years before they were offered the contracts that made them wealthy. Counterfeits can also have a huge impact on many aspects of the cultural sector, at enormous cost to artists. Illegal downloading is the most prominent current example, but forgeries of paintings are also a common means of profiting from the illicit use of artists' names. Works by Salvador Dali, for instance, were forged mercilessly.

## 4.4 Market forms and market models

Any cultural institution or enterprise will in a number of ways confront market conditions that are unique, and very often methods used in selling consumer goods cannot be transferred to the sale of cultural goods. In individual cases marketing will often need to be customised to the cultural goods being sold.<sup>15</sup> Figure 4.4 depicts a traditional marketing model.

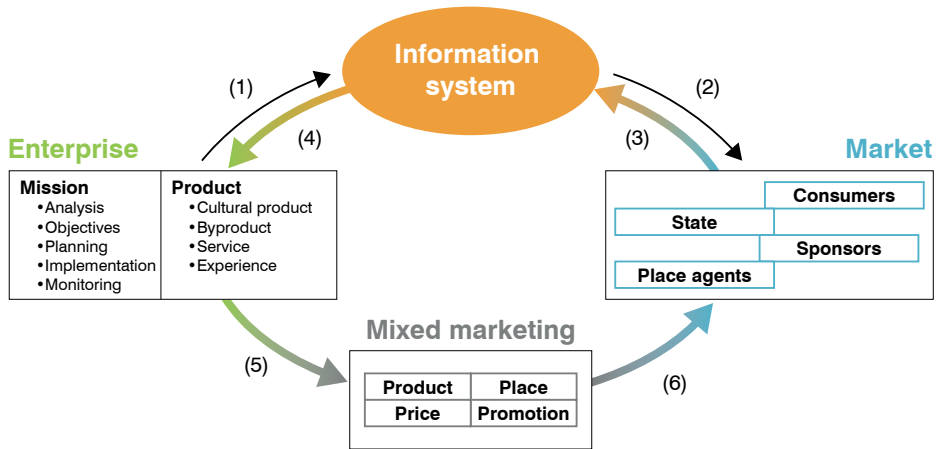


**Figure 4.4:** Traditional marketing model

In Figure 4.4 information is received from the market (the arrow marked 1) and entered into an information system and from that system to business firms engaging in the production of cultural goods (2), which market the goods (3) for the market (4). This is a simplified illustration, but Figure 4.5 shows a more complex model for marketing in the cultural sector.<sup>16</sup>

<sup>15</sup> For a discussion of the marketing work of cultural enterprises see, e.g., Kotler and Scheff (1997) and Bernstein (2007).

<sup>16</sup> For a discussion of marketing cultural goods see Colbert *et al.* (2008)



**Figure 4.5:** Marketing model in the cultural sector

Marketing in the cultural sector, according to Figure 4.5, starts in the company, which feeds information about its production into an information system (the arrow marked 1), which forwards the information to the market (2), which provides feedback (3) that is carried back to the firm (4). The marketing then begins in the lower part of Figure 4.5, based on the firm's strategy, and is carried into the market (6). The company formulates a strategy based on analysis, establishing objectives, a plan, implementation of the plan and monitoring results. For a company, time and the features that distinguish it from competitors are of the essence. The market is divided into spheres or sources of influence, such as consumers, government and the private sector. As a matter of fact, the circumstances of artists or firms engaging in the production of cultural goods can differ vastly; some may be driven by the joy of creation, others by anticipations of profit and still others by hopes of support from government or other sponsors. These different perspectives influence the approaches used in marketing the goods in question. In most markets there is competition and factors that are difficult, or even impossible, to foresee, such as changes in tastes and fashion or purely economic factors, such as currency trends.

Market forms can differ depending on the intensity of competition. Firstly, a competitive market is one in which numerous buyers and numerous sellers compete against each other and where the products in the market are quite alike to the point of homogeneity. Secondly, and conversely, if there is only one seller in the market a monopoly exists. Thirdly, some markets have only a few sellers, in which case an oligopoly reigns supreme. Fourthly, a market form is known as 'monopolistic

competition', where numerous buyers and sellers are active, but the products in the marketplace are mixed or heterogeneous. In a market of this kind sellers have a sort of monopoly on their specific products, but the product is in competition with a number of similar products.<sup>17</sup> The market for cultural goods is an example of this kind of market, as is the market for automobiles. In these markets there is competition, but each cultural good, or automobile, has its special character. Normally there will also be numerous buyers in these markets.

In the case of culture there are usually many different consumers. There are usually also many dissimilar suppliers, whether firms or governmental or non-governmental organisations. In some cases, however, there will be few suppliers, as in the case of theatres, or even just one supplier, as in the case of collections of ancient manuscripts for public display. In many places antitrust and competition laws have been passed to prevent market dominance and monopolies. Such legislation focuses, among other things, on verifying specifically whether mergers of companies can result in monopolies.

When firms sell the same product at different prices to many customers, this phenomenon is referred to as price differentiation. In a competitive market, competition will normally prevent the possibility of different prices for the same product. An example of price differentiation is the publication of a book in both an elaborate hard-cover edition and a plain paperback version. Those who buy the book in paperback form are willing to buy the book at a certain price, while those who opt for the fancier hard cover are prepared to buy at a higher price. If a single average price were set and a single version of the book published, then the publisher would lose revenue.<sup>18</sup>

**Mærsk Mc-Kinney Møller** was born in 1913 in Denmark and died in 2012. He was the CEO of the huge Danish company A.P. Møller – Mærsk, whose core services include shipping. He was an extraordinarily capable business leader and the best known of all Danish business leaders around the world. Møller was the wealthiest man in Denmark and served on the boards of directors of a number of companies. He also received a number of awards. He was a generous man and supported science and the arts on a greater scale than anyone else in Denmark. His last donation was the Copenhagen Opera House in Copenhagen, the city of his birth, which was inaugurated in 2005. He was a personal friend of the Danish royal family and was greatly admired for his achievements.

<sup>17</sup> For a discussion of monopolistic competition see, e.g., Wöhe and Döring (2010).

<sup>18</sup> The phenomenon of one author using both a real name and a nom de plume is also not unknown; see, for example, Ruth Rendall/Barbara Vine. The stated objective of writing under an assumed name is, among other reasons, for marketing purposes, often to create another kind of writing than that which has become known to readers.



A marketing strategy can be divided into three stages: analysis, planning and implementation. The strategic planning takes place in eight stages, including market analysis, SWOT analysis (which is described further in the next chapter), setting targets, marketing strategy, marketing mix, an action plan, budget and monitoring, as shown in Figure 4.6.



**Figure 4.6:** Marketing strategy and its components

In addition to the eight components of strategic planning, a documented marketing strategy is usually accompanied by a summary. Market analysis consists in obtaining sound knowledge of a firm's environment, not only its internal environment but also its external environment, including laws and regulations. Customers' perception of goods and services can be analysed and criteria can be established to rank businesses and individuals in some sort of order. This order gives a fair view of the market, goods or service in question.

A key aspect of marketing is patterns of consumers' buying behaviour, which provide information on who the buyers are, from whom they tend to buy, when they buy, how, where and why. The factors of influence in buying-behaviour are many and varied and they can be of a personal, cultural, social and psychological nature.

## 4.5 Aspects of marketing

Marketing cultural goods can be similar to marketing goods and services in general, but it does not revolve simply around filling seats in a theatre, but in creating real value for customers. Marketing is the act of assisting customers in gaining a better position than they had before.<sup>19</sup> Competition, and in particular variety, can often make the sale of cultural goods more complex than retailing simpler consumer goods, such as bread and butter. Consumer views or tastes largely determine the success of the goods, and the experience and atmosphere of consumption is often significant, just as timing in an artistic performance can be of paramount importance. If the experience matches expectations, the product receives favourable discussion, which influences other consumers. Discussion of this kind, which has been mentioned earlier, is a characteristic of trade in cultural goods, but is not as common in the case of other goods.

In actuality, it may well be that producers of cultural goods will see it as their role to be as independent of the market and market demands as possible, and the driving force may be the need for self-expression. It also needs to be kept in mind that customers in the marketplace are often not individuals, but specialised institutions such as museums or schools.

Cost and production processes of businesses vary and make their respective competitive positions different. The better the control that a business exercises over its costs and production, the better its financial performance will be in comparison with other businesses. A business which has reduced its production costs using knowledge and experience, that is to say the learning curve, will have an advantage over other businesses.

The financial situations of businesses can differ vastly. Some enjoy a strong financial position, while others are weak. Some businesses are well placed in terms of assets but may still experience operating difficulties, while others have large reserves of cash but may be heavily in debt. Markets may be separated by distance, borders, or tariffs. A typical market separation is between export markets and domestic markets. In some cases this will enable the application of different prices in different markets using price differentiation, as discussed earlier.

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<sup>19</sup> For a discussion of corporate marketing see, e.g., Kotler (2007).

Individual products of the same business firm can be linked in revenue. This principle refers, on the one hand, to direct sales links between substitute goods and, on the other hand, to indirect sale links between complementary goods. Direct sales links mean that sales of product A influence the volume of sales of product B. In the case of substitute goods, such as two plays running in the same theatre for a limited time, a good house for one of the plays may curtail attendance of the other play, since most people prefer a little breathing room between their attendances of plays, not to mention the budgetary considerations of most playgoers.

The product selection of an organisation is the range of products or service that it offers, for example the variety of plays in a theatre company's repertoire. A distinction needs to be made between two types of product range, that is to say breadth and depth. The breadth of a product range refers to the number of product types; for instance a number of artists may produce CDs for release by a record company. The depth of the range of products refers to the specialisation of a business, for instance a shop that specialises in the sale of CDs with classic operas and little else.

Just as consumer behaviour and consumer demand are shaped by con-

**Pablo Picasso** was born in Spain in 1881 and died in 1973. He was a painter of great natural talent and he is widely considered the greatest painter of the 20<sup>th</sup> century. He was also a sculptor and he tried his hand at a number of arts with much success. Among his legacies is the development of cubism along with his good friend Georges Braque. Picasso lived for a long time in Paris, having severed his relations with his home country in the Franco era. Among world famous paintings by Picasso are *Les Femmes d'Alger*, preserved in the Museum of Modern Art (MoMa) in New York, and *Guernica*, painted in memory of the air raids on the town of Guernica in the Spanish Civil War. The painting is preserved in the Museo Reina Sofía in Madrid. Picasso's versatility was unique, and the American painter, Jason Pollock said of him: „That guy missed nothing.“

sumer needs and expectations, a business needs to tailor its marketing work to the needs of its customers, whether they are individuals or organisations.<sup>20</sup> An organisation has to define its range of customers, how they are to be reached and what marketing actions need to be organised and managed. This applies to marketing of cultural goods as much as it does to bread and butter.

The factors that have to be taken into account in analysing customers are who they are, what influences their buying behaviour and what types of goods or services they are prepared to support. A business needs to base its operations on knowledge of customer needs in order to be able to identify the target group it wants as its customers. Identifying target

<sup>20</sup> For a discussion of customer needs in marketing see, e.g., Diederich (1992) and Kotler and Armstrong (2011).

groups consists in dividing a market into smaller groups in order to enable a business to concentrate on certain parts of a market and, thereby, a limited group of consumers. A market can be split up and analysed; that is, divided into target groups of potential customers based on various criteria, such as geographic, demographic or ethical variables. Some consumers will buy a product for its taste, others for its wholesomeness, still others for its price and yet others for its appearance.

A satisfied customer is valuable, and word of mouth or a good reputation over an extended period of time are invaluable. It is, therefore, an asset for a business to possess a reputation for good services to customers. Almost everyone has at one time or another been the recipient of such poor service that it results in a solemn oath never again to set foot in some retail outlet or another. A negative attitude of this kind, which is often communicated freely to others, can do serious damage to a start-up small business. This is particularly true in the cultural sector, where consumers can be not only demanding but eager to express their dissatisfaction if they see reason to do so.<sup>21</sup>

It is important for any business organisation to be aware of where it stands in the competition with other businesses. Important factors in such a comparison are market size, production capacity, position in research and development and employee and management competence. Leaders of a business organisation need to examine various aspects of their environment in formulating their strategy. It is of great importance for them to understand where the business has a competitive advantage over other competing businesses and to put this advantage to the best possible use.

A market can be observed from several perspectives in assessing a business organisation's potentials. These include market size, location, growth potential, quality awareness, availability of energy, raw materials and environmental situation. Business organisations have different areas of focus in their activities. Some organisations focus on the technical aspects of production, others on variety in product range and yet others on extensive advertising. Some businesses concentrate on defining their markets as precisely as possible. Competitive advantage can be achieved through all these approaches, depending on market conditions, and principally on the level of competition. All of these factors apply to the cultural sector.

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<sup>21</sup> For a discussion of consumer attitude in the cultural sector see, e.g., Colbert *et al.* (2008).

However, a sound knowledge of the market is the most important means of achieving results. This knowledge, once acquired, then has to be disseminated throughout the organisation and followed up using all the means needed and available. Consumers in our times are paying growing attention to environmental matters and other matters of community importance. Businesses need to take as much account of these perspectives in their marketing as to other consumer perspectives. Consumer protection, the activities of consumer organisations and various ethical organisations all play a role in this regard.

Product development is a protracted process. A long time will normally pass before an idea for a new or improved product is born until it becomes a reality. This is especially evident in the cultural sector, where only a very small minority of ideas ever become reality or result in a marketable product. A product has to be designed, the market has to be surveyed and an operating and financial plan has to be prepared before the product is made. Consumer needs, competitive conditions in the market and technical opportunities are among the factors that need to be researched before goods or services are ready for sale.

One method of analysing a new product or idea is to define the purpose and form of the product, consumer expectations regarding the product and the way in which consumers will differentiate it from other products in the market. An example of the purpose of a product type is that a book is intended for reading. The form of a product type refers to the fact that a book is normally rectangular and printed or ready for reading in an electronic device. Consumer expectations in this case are that the consumer will expect to enjoy the book during and after its reading. Differentiation from competitors means, among other things, that the contents of the books and the approach to the subject matter should differ from that of other writers.

It is important to be able to draw attention to the product in its marketing, to disseminate knowledge and understanding and to convince prospective buyers of the quality of the product. The objective is to persuade them to purchase the product or service. This goal applies to marketing in general, but as regards cultural goods it is often important to disseminate knowledge and understanding of the product, whether a work of art or the staging of a play, since the production of cultural goods is often complex and requires a great deal of knowledge for them to be enjoyed to the fullest.<sup>22</sup>

<sup>22</sup> For a discussion of the importance of knowledge in marketing cultural goods see, e.g., Martin (2008).

The restrictions on marketing cultural goods are more often than not financial; a business or institution may have little cash to work with, which restricts the scope of the marketing of its goods. Another factor that can delay or inhibit sales is slack management of a cultural firm or institution that will be reflected in poor marketing or inadequate product quality. A lack of communication between a marketing division and other aspects of production or the lack of a clear vision of customer needs can also inhibit successful sales.

The promotion of cultural goods has become much simpler and at the same time much more extensive as a result of progress in Internet and software technology. This is also apparent in the collection and processing of data; it is now much easier to find information (via the Internet) than before and to make comparisons of prices and quality, including information on buyers and their preferences. This improvement in technology has made it possible to make more accurate predictions about product sales.

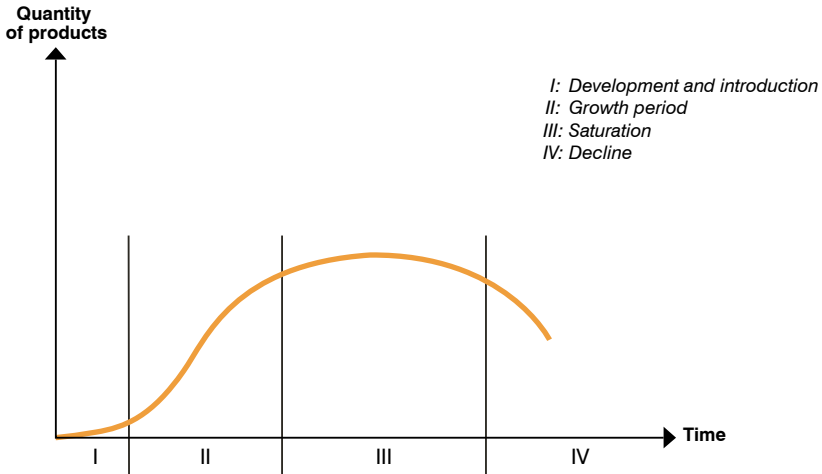
If a business is in a position to decide on the price of a new product or service, various questions will arise as regards the optimum price. Normally, it will be based, at least in part, on the price of a similar product or service already on the market. However, this may not be appropriate in all cases. Perhaps the company may consider it a good option to attempt to convince consumers by means of a powerful advertising campaign that its product is better than other similar products offered by a competitor. It is easier now than ever before to change the price of a product as demand changes – for instance to change the price of a seat in a theatre as the performance draws nearer – so that the idea of the same price for everything is a thing of the past.<sup>23</sup> This trend can also be observed in other business sectors, as in the case of air fares, which airlines can readily change depending on demand.

#### **4.6 Product life cycle, income share of product types and market position**

The life cycle of a product is generally divided into four phases. The first phase involves development and introduction; most products do not pass this phase. The second phase is a growth phase, the time during which a product sells well. The third phase is the maturity phase, which

<sup>23</sup> For a discussion of different prices in the culture sector see, e.g., Ravanas (2008).

represents the limit of the product's sales. Sales will stagnate, making it necessary to make a change and develop new products. The fourth phase is a phase of decline, or deterioration, at which time sales will fall. Figure 4.7 shows the product life cycle.



**Figure 4.7:** Product life cycle

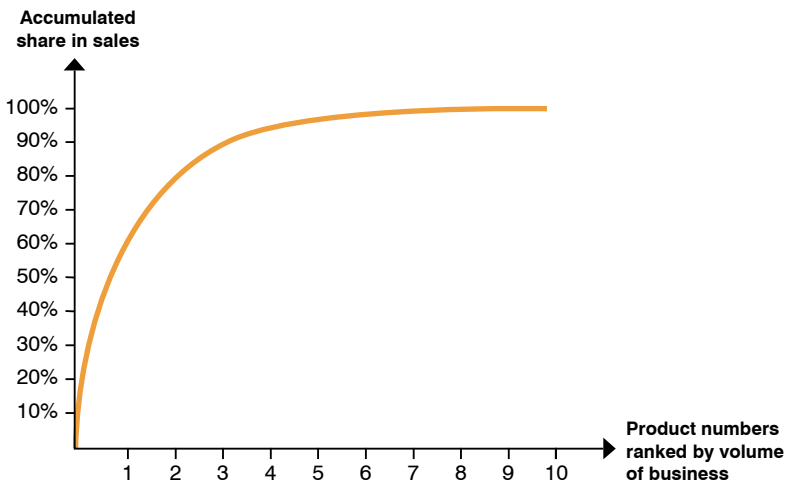
As shown in Figure 4.6 the life cycle of a product begins with development and introduction (I), with most products not advancing beyond this phase; it is characterised by the work of entrepreneurs. The next phase is the growth phase (II), which is characterised by significant increases in sales; the marketing staff of the business is most prominent at this stage. The third phase (III) is the maturity phase, in the course of which sales reach their maximum level, but then taper off with financial management often the most important factor. The last phase is the decline (IV) when sales fall and the business eventually ceases to sell the product in its current form.

Any business needs to have a clear vision of where in their life cycles its principal products can be placed. It is important to consider in a timely manner new product types or new versions of older products. A product's life cycle can be compared to a human lifespan or to a business enterprise's lifetime, which is divided into periods of development, growth, maturity and decline.

In many businesses, including businesses in the cultural sector, only a small part of the product range will generate the lion's share of the sales.

It is common for about 20% of the product range of a business to return about 80% of sales. Product types are categorised by sales value into three categories: Category A comprises the products that sell best and account for 80% of turnover; Category B comprises the products that account for the next 15% of sales, and Category C comprises the products that return the smallest income of the business in question, about 5%. These proportions are variable, but the general rule is that a small minority of the product types return the largest part of the income. This analysis is known as the ABC analysis, or the 80-20 rule, and it is widely used in ranking items by importance.

Product types are organised by turnover, so that the product type that sells best is assigned the number 1, the one that sells next best is assigned 2 and so on. An example of the use of ABC analysis is when customers are ranked in the order of the quantities of an organisation's production that they buy. Category A then comprises customers number 1 and 2, that is to say the two who buy the most; Category B comprises the customers ranked from number 3 through 7, and Category C comprises customers ranked from 8 through 10. Figure 4.8 illustrates the ABC analysis.

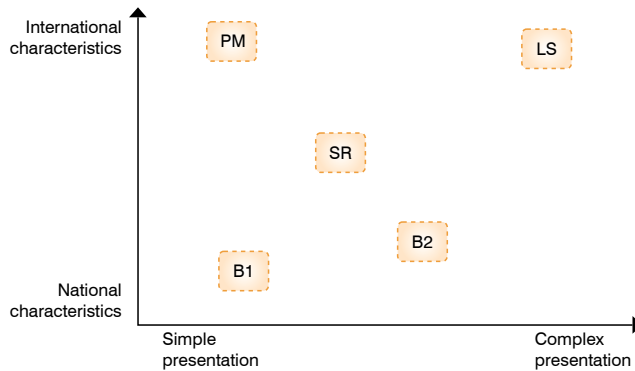


**Figure 4.8:** ABC analysis

Figure 4.8 shows that two products account for 80% of the business firm's sales, as in a case where two motion pictures out of ten produced by a production company generate 80% of the company's revenues.



Differentiation in the market can be depicted in a simple two-dimensional illustration, as shown in Figure 4.9.



**Figure 4.9:** The position of music in the market in a two-dimensional model

The music of the Icelandic musician Björk (B1 and B2 in Figure 4.9) has strong national characteristics, and at first its performance was not complex, but in recent years it has become much more complex with increasingly varied accompaniment. The trend can be said to have been from B1 to B2, as shown in Figure 4.9. The music of the Icelandic band Sigur Rós (SR in Figure 4.9) also has strong national characteristics, and in Figure 4.9 the presentation is set at the centre.<sup>24</sup> The London Symphony Orchestra (LS in Figure 4.9) has a complex presentation and a number of performers and normally plays music with international characteristics, mainly classical music. Pop music (PM in Figure 4.9) is usually played by a small number of performers, but has clear international characteristics and follows international trends.

This is a simple example of marketing, and it can be used to analyse market position, although it is used here merely as an example of the possibilities or marketing. Based on an analysis of this kind, it is possible to decide what kind of market positioning has the best potential. For example, it would probably be difficult to establish a foothold on the basis of international characteristics in the gigantic music market. A very complex presentation costs a great deal, especially in the case of concerts. Market positioning is particularly important in the cultural

<sup>24</sup> Björk has been nominated for an Oscar and a number of Grammy awards, in addition to other awards. Sigur Rós has received a number of international awards.

sector, and it is important to revise the positioning regularly because of the rapid changes in the world of culture and in the production of cultural goods.

Most business enterprises try to find themselves a position that is not occupied by another business firm, that is, a market niche. Firms will have different points of emphasis in their marketing, but normally they will attempt to have the same products and services on offer for the entire market; they will adapt their products and services to one or more target groups and concentrate on a suitable market niche or target group.

Among the changes that have occurred in marketing in the cultural sector is that people decide on participation in cultural events at shorter notice than before, and subscription rates, for instance to theatre tickets, have fallen in recent years. Since subscribers are often the most loyal customers of cultural institutions and cultural businesses, this trend calls for changed approaches in marketing.

Culture, which in some ways is the framework of human relations in society, has great significance in marketing. Sound knowledge of the culture of countries and market areas is of fundamental importance in the growth market of international relations.

Consumers have developed different patterns of behaviour in their purchases of goods and services; some consumers will focus on brand names, while others have no interest in them; some will spend a great deal of time on research and thought, while others buy goods or services on impulse. This pattern applies to individual consumers, but the analysis of the buying behaviour of business firms is a rather different prospect from analysing individuals, since businesses are usually larger buyers, reliability is an important factor and, therefore, relations between buyer and seller are often both close and extensive.

Marketing research is an important tool for businesses to collect the best possible knowledge of the factors that are relevant to marketing. Among other things, the cost of market research needs to be estimated,

**William Shakespeare** was born in 1564 and died in 1616. He is the foremost dramatist of all times, but apart from his career as a playwright he was also an actor, director and part owner and manager of a theatre company. Shakespeare worked mostly in London and in Stratford-upon-Avon. His plays were extremely popular among the public in London. His tragedies, such as *Macbeth*, *Hamlet*, and *King Lear*, are universally acclaimed as masterpieces, displaying both Shakespeare's insight into human nature and his extraordinary command of the English language. He wrote a number of historical plays as well on former kings of England, as well as a number of comedies. Shakespeare's plays remain popular to this day, many of them, if not all, have been filmed a number of times and actors and actresses see it as an honour to be cast in major roles in his works, whether on stage or on screen.

information gathered, the sales network and sellers assessed, including staff, and surveys conducted, for example, using focus groups.<sup>25</sup>

There are many specialised companies that do marketing research for other companies, but large companies will often have their own market research divisions. Market research is used to anticipate the demand for a product and make decisions on prices, packaging, market areas, target groups, substitute goods, the position of competitors, likely trends in tastes and potential changes in culture.

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<sup>25</sup> For a discussion of market research and culture see, e.g., Steenkamp (2001) and Bernstein (2007).

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## 5. Finance and management in the cultural industry

Finance is among the most important aspects of any business operation, whether inside or outside the cultural sector. Although most aspects of finance are common to all organisations, there are always some unique factors in any sector of the economy, and the same is true of the cultural sector. Finance is often the limiting factor in the operation of cultural institutions as in other business operations, and this restriction is a matter of frequent public debate. Such restrictions make clear that the production of public goods, like so much in culture, cannot be allowed to place an excessive burden on public finance.

Organisation and management is a multifaceted task, for cultural production is varied and circumstances differ widely. It is, therefore, important for managers in this area to possess a good understanding of the basic principles of culture, the economic links between those principles and those of finance, organisation and management in businesses and institutions.

### 5.1 Finances

#### 5.1.1 Capital requirements

Capital exists in several forms. Tangible capital is represented by the value of assets; assets are divided into capital assets, such as inventory, receivables and cash, and fixed assets, such as real property, machinery, stocks or other long-term securities. Without capital and financing, combined with good financial organisation, no business will survive for long, whether in the cultural or any other sector. An organisation requires capital, or start-up capital, to prepare and launch its operations, and operating capital for its continuing operation. A large part of the capital needs of organisations in the cultural sector are met by means

of unrecoverable contributions from government or private entities that are intended to support the activity in question. In the cultural sector there are three principal means of financing: sales in the market, government contributions and contributions from patrons, whether private individuals or businesses, sometimes in the form of sponsorships.<sup>1</sup>

### 5.1.2 Financing

Setting up a business operation requires an assessment of capital needs. Establishing a print shop, for example, requires premises and a printing press, which are fixed assets. In addition, the organisation will need cash, inventory and supplies, which are current assets. The first step is to prepare a precise capital needs assessment specifying how much is needed, when and at what cost. The length of time that initial capital is tied up in business operation's assets can vary greatly. The capital and assets of a theatre may be tied up for decades, while the capital tied up in an artist's brushes and paints may be a month or less. The financial situation of an individual or organisation will, to a large extent, be determined by the length of time that capital is tied up.

It is not enough just to establish a company with capital goods, inventory and supplies. The company also needs to be run. This requires working or operating capital. Working capital is needed if cash expenditures precede cash receipts in time. If two thousand books are printed early in a year, for example, and they are not sold until the Christmas season, then there will be a need for working capital, since basic supplies such as paper and ink will need to be paid for. The balance between cash outflow and cash inflow has to be funded.

The working capital requirement is often the most difficult problem faced by business firms in their day-to-day operations. This need may be different depending on the nature of the business activity, and periodic fluctuations can be significant. And not to forget: capital costs money. In normal conditions capital can usually be obtained on rental terms, where the rent is the interest that the borrower must pay.

Underestimating the need for working capital has been the downfall of many business undertakings. A carefully crafted operating plan with details of the projected income and expenses over a specified period of time, for instance the ensuing year, is a prerequisite for a successful

<sup>1</sup> For a discussion of the principal aspects of corporate finance in the cultural sector see, e.g., Vogel (2011) and Rich (2008).

business operation. Many aspects of cultural production involve significant financial risk, which means, of course, that careful financial planning in the cultural sector is a condition for successful operation, and financial plans will normally include provisions for monitoring. The budget needs to be compared with reality from month to month.<sup>2</sup>

Most people are familiar with the situation of deciding whether to obtain a loan to purchase some prized item, for example, a new television, or of saving up the expenditure to avoid going into debt. This kind of financing is also carried out in the financial market, where the savings of one person are used for investment by another. Saving and investment are key features of value creation. For example, if a larger proportion of Gross Domestic Product (GDP) is kept in savings, there are more funds available for investment, which in turn leads to increased GDP in the future. The financial markets bring together savers and investors; this is yet another example of the old law of supply and demand.

Financing in the cultural sector takes the form of external financing and internal financing. External financing is divided into loan financing, which in turn is divided into long-term borrowings and short-term borrowings, and contributions, which are divided into public contributions from the state and/or local government, and from private parties, whether individuals or corporations.

Normally an attempt is made to finance assets for a period that is equivalent to their lifetimes. Thus, short-term assets are financed by means of short-term borrowings, while long-term assets will normally be financed by means of long-term borrowings. Long-term borrowings are usually defined as loans taken for a period longer than one year.

Contributions, which may take the form of donations or sponsorships, have two forms: they can be originated from government entities, state or local; or from private entities, that is, individuals or corporations. Sometimes these contributions may derive from special funds, often with precise conditions regarding the use of the contributions or acknowledging or naming of the contributor, although it is not unknown for cultural institutions such as museums to receive anonymous contributions, sometimes with strict instructions regarding anonymity.

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<sup>2</sup> For a discussion of financial risk in cultural business operations see, e.g., Brigham (2011) and Chong (2010).

Internal financing consists in financing through owners' contributions, for instance in the form of share capital, and retained earnings. Retained earnings refer to a company's own contribution of the funds needed to meet financial needs. These methods are normally mixed together in corporate financing, which is common in the operation of cultural enterprises.

In estimating financing needs, an operating and payment plan are first prepared, after which the financing needs will be known. Management will then need to decide what financing option or options will be selected and, in the latter case, in what proportions. Assuming that there are no limitations on financing, the most favourable route is, of course, to choose the cheapest option. However, the options available to a business to obtain financing or capital may be limited, and the cheapest option may not be available.

In cultural production, particularly in the arts, it is not uncommon for disputes to emerge relating to cost between an artistic director, on the one hand, and executives or financial controllers, on the other hand, particularly if an artistic director wants to invest significant amounts in a particular work or equipment and the funds are not readily available. The financiers do not always emerge victorious, and there are examples of disastrous consequences.<sup>3</sup> Some historical facts about money are highlighted in Illustration 5.

### Illustration 5: Money and its influence

**M**oney first appeared on the scene when bartering had become so extensive that simplification was needed. Initially, money was a representation of the value of a certain quantity of a commodity. For a long time money had the value of the commodity it represented, as in the case of gold coins. The quantity of gold in a coin had a specific value which was generally accepted. Subsequently, kings and other personages of power began to guarantee the value of a simpler form of money, often by using their coats of arms. Holders of such coins were assured that they could present themselves and obtain the value of the coins in gold or other comparable commodities. Much later, a simplified form of money was introduced, including paper money, the value of which was guaranteed by government.

The traditional definition of money is that it is tender that can be used to purchase goods and services. Money can be used in three ways. Firstly, it is tender. A person can take money to a shop and purchase goods. An exchange is made of the money and a certain quantity of goods. Secondly, money is a measure of value. Admission to a concert will cost a certain amount of money, while admission to a film in a cinema

<sup>3</sup> For a discussion of disputes between artistic directors and finance directors see, e.g., Byrnes (2009).

will cost another amount. Each can be valued in terms of currencies such as dollars, pounds or euros. Among themselves, these currencies will have a relative value expressed as an exchange rate. Thirdly, use of money is conservation; money can be used to conserve value. The value of something can be conserved in the form of, say, a thousand dollars, whether under a mattress or in a deposit account. There are numerous other assets that can perform these three functions, that is as tender, measures of value or means of conservation. To give an example, the tender in prison camps in World War II was not in the form of bills, but cigarettes. A cigarette-based economy was formed that served all three functions.

Inflation is a general increase in price levels over a longer term. Deflation, conversely, is a decrease in price levels over a longer term. Even if the price of a good goes up by 10%-20%, this rise does not represent inflation unless there is a general increase in prices. There are various examples of hyperinflation in history, as in the case of the Weimar Republic in Germany in the 1920s. Inflation in one country that exceeds the inflation in another country can undermine the competitiveness of the country in question.

Money and greed for money are a recurrent theme in literature. One example is the story of Midas, an ancient king in Phrygia in Asia Minor, who made a wish to the gods that everything he touched would turn into gold. His wish was granted and everything he touched was instantly transformed into gold, including his food and his daughter, so that his happiness was short-lived. Midas appealed to the gods to take back their gift, and they did so.

Thirty pieces of silver have become a symbol of betrayal and bribery, at least for Christians, since Judas betrayed Jesus into the hands of his executioners for that sum.

Another well known story is that of the Merchant of Venice in Shakespeare's play of the same name, where a Jew named Shylock lent a large sum of money to another merchant and accepted as security a pound of the merchant's flesh. The merchant then suffered a series of setbacks, the loan fell due and Shylock demanded his security, even though an offer was made to pay back double the original sum of the loan. The matter was referred to the courts of law and the wife of one of the merchant's friends, Portia, masqueraded as a man and defended the merchant on the grounds that Shylock could have his pound of flesh but that if blood were spilled in the process, the contract was null and void. The judges accepted this argument, Shylock lost the case and was ordered to pay a large fine.

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Financial accounts are used to calculate a variety of financial ratios. A financial ratio is a value expressed as a relative magnitude of two figures that sheds a light on a certain aspect of a business undertaking's operation. If an organisation's turnover in a single year is \$50 million and its profit is \$1 million, its profit ratio is  $1/50$ , or 2%. If the turnover is \$70 million the next year and the profit is \$1,750,000, then the profit ratio is 2.5%. Financial ratios are useful tools in analysing the operations and financial standing of enterprises. Ratios can be used for three purposes: firstly, a ratio can be compared with the same ratio for the same



organisation from an earlier period, as in the comparison of the profit ratio of a theatre between two seasons; secondly, a ratio can be compared to a projected ratio of the same undertaking; that is, reality is compared to estimates; and, thirdly, a ratio can be compared with the corresponding ratio of another organisation over the same period; that is, the profit ratio of one theatre in the 2015 season can be compared to the corresponding ratio of other theatres over the same period.

## **5.2 Organisation and management**

### **5.2.1 Organisation**

The organisation of a business enterprise is primarily an internal matter defined as the structure of relations within the enterprise. Closely connected with the organisation of a firm is its legal, or corporate, form. This corporate form refers to how the firm is legally constituted and largely determines its external aspect. The organisation of a firm relates to the way in which the production of goods or services is conducted, whether in cultural enterprises or institutions or other organisations; an organisation is defined as a system of human actions, or a group of persons working in a systematic manner toward the same goal. Among other things, the organisation represents the hierarchy and division of powers and responsibility within this system. The organisation will determine how a firm is managed; for instance, how information is communicated throughout the firm and how the manufacturing process is conducted.

Economic activity is reflected in business undertakings and institutions, and since most enterprises operate in open markets there are numerous factors that affect their internal and external organisation. The structure of an enterprise describes the relations between people, the division into departments and the relations between departments. Among the factors that can constitute weaknesses in organisations are slow decision-making, failure to react promptly to changes in external circumstances and ongoing disagreement among decision makers.

The organisation of an enterprise also relates to responses to external conditions, which have changed profoundly in recent decades as a result of globalisation and cultural diversity, even within individual market areas. The cultural environment has a huge influence on corporate management and requires a great deal of acumen. Culture differs from one region to another; among other things there may be differences

in attitudes to uncertainty and risk, to collectivity and individuality, to gender equality and values. Knowledge of these matters will increase the likelihood of success in organising the management of an enterprise that operates in a multinational market and employs people from a variety of different cultural or ethnic communities.

The organisation of enterprises extends to responsibilities, relations between departments and groups within the undertaking and should represent a system which is capable of linking and coordinating individual aspects of the enterprise's business activity. The division of labour in an enterprise can be horizontal or vertical. A horizontal structure refers to a situation where relations between parties are at the same level with no hierarchy. An example of a horizontal division of labour could be illustrated by the way in which musicians decide who should play what. Vertical structures, conversely, are characterised by hierarchical relationships between parties who are not at the same level in the firm and actions by one are taken at the order of another. An example of a vertical structure could be the staging of a play where a director leads a team of actors who obey the director's instructions. It is important for power and accountability to go together in an organisation.

It is possible for an enterprise to have a very limited organisation. Everyone simply addresses a task and completes it, as in the case of farmwork. Typically, all the employees on a farm will be capable of tending to all the chores that need to be done, from milking cows, to mending fences and pitching in at harvest time; a specialist farmhand is scarcely conceivable except in a highly industrialised operation. Another example could be a small gallery, where all employees will do the all work that needs to be done. Loose organisation of this kind is common in small businesses, including those in the cultural sector, such as art galleries.

A plan is an organised preparation for decision making which looks to the future. A plan

**Adam Smith** was born in Scotland in 1723 and died in 1790. He is often referred to as the father of economics. Adam Smith was a professor in Glasgow in 1750 and was greatly influenced by his friendship with one of the greatest thinkers of his time, the philosopher David Hume. For most of his career Adam Smith was engaged in writing his principal work, *An Inquiry into the Nature and Causes of the Wealth of Nations*, which appeared in 1776. In *The Wealth of Nations*, as the book is generally known, he gathered all the knowledge available on economics and systematically organised the results. The book is regarded as marking the beginning of economics as a science. In 1778 Adam Smith was appointed Comptroller of the Customs in Scotland, and although tariffs were not desirable according to his theories the position secured for him a comfortable life. In his works Adam Smith wrote a great deal about culture and the arts, in which he had great interest. His last task was to burn all his manuscripts which he believed not to be suitable for public reading.

addresses what needs to be done, when it needs to be done, who should do it and how. The result of the plan is a decision, or a series of decisions, that determines the operation of the enterprise. The results of the plan then have to be compared with the real results of the firm's operation. A number of plans are made within an organisation, such as a financial plan, or budget, and a manufacturing plan. A business plan is one such plan, which encompasses most of the major aspects of an firm's operation and is necessary to draw the attention of investors and credit undertakings to the potential of the enterprise. A business plan will include a description of the firm, its products and supplies. It will also describe the firm's management system, its marketing strategy and financial structure.<sup>4</sup>

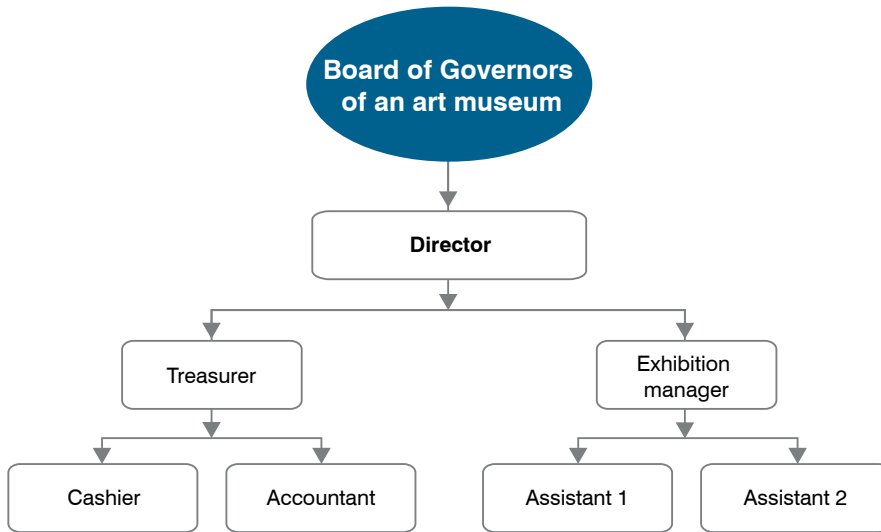
In all enterprises virtually all employees have a superior although some employees may actually be their own masters in exceptional cases, even though they may work within a larger unit. An example could be a taxi driver who drives for a taxicab company, but owns and operates his or her own vehicle. A comparable example could be an auditor who works at an auditing firm as a shareholder or partner, but has no superior. To take an example from the cultural sector, it is common for sole trad-

ers to engage in the production of art, such as painters or writers, who work completely independently. However, these are exceptions, and in most enterprises in most sectors the ranking of officers and the limits of their authority are usually quite clear.

Relationships between employees in a business firm, or the arrangement of work processes, are inherent in a firm's structure and normally shown in the form of an organisational chart. Organisational charts illustrate graphically the hierarchies and spheres of competence and authority of officers and employees and their relationships with other employees; Figure 5.1 shows an example of the organisational chart of an art museum.

**Socrates** is believed to have been born in 469 B.C. and he died in 399 B.C. He is best known for his philosophy, but his influence on culture was extensive. Socrates was the originator of ethics, where the central theme and focus was on moderation and moral excellence. He taught by conversing with people, asking questions and analysing the answers. Plato, the great Greek philosopher, was a disciple of Socrates. Plato wrote a great deal about Socrates and his conversations with others, but it is believed that Plato's own views are frequently blended into these conversations. The philosopher Xenophon also wrote about Socrates. Socrates served for some time as a soldier with some distinction, but he was a thorn in the side of the leaders of Athens with his sharp criticism. However, he was left in peace until his old age, when he was sentenced to death. He could easily have avoided death, but chose not to.

<sup>4</sup> For a discussion of the organisation of undertakings and business plans see, e.g., Diederich (1992), Lynggaard (2008) and Daft (2010).



**Figure 5.1:** Organisational Chart

Figure 5.1 shows two employees, a treasurer and a exhibition manager, both of whom have two assistants, working under the supervision of a director. The treasurer has two underlings, a cashier and an accountant. The accountant takes orders from the treasurer, but not from the cashier or stage manager. Even though the director is the head officer, he or she will only give orders to the accountant in exceptional cases, since the accountant is directly answerable to the treasurer. The director or executive of a museum, or of any company, works under the authority of a board of governors. In the case of corporations a board of directors is elected by the corporation's owners at an annual general meeting.

The value of organisational charts must not be overestimated. They cannot replace definitions of functions and job descriptions. Sometimes there may be deviations from a previously established system, whether formal or informal, in which case the change can prove beneficial or not. Changes in organisation can take place at the departmental level, initiated by the head of the department, with or without the consent of his or her superior. In some cases consultations may be held with the employees affected by the change, but this is not always the case. Organisational changes often occur in the wake of audits by external consultants appointed to submit recommendations regarding improvements in the operation of individual enterprises.

It must be possible to evaluate the quality of an enterprise's organisation. Two items in particular show how an organisation is performing: one is whether the operation is proceeding smoothly, and another is whether a firm is capable of adapting quickly to changes. The organisation must also be conducive to conflict-free operation. If there are constant or frequent incidents in a production process, such as inconsistency in orders and sales, disputes between department heads or financial irregularities, then there is something wrong with the organisation. Good organisation cannot save companies that find themselves in hopeless situations, but it can be the difference between whether an enterprise survives temporary difficulties or not.

One form of organisation and cooperation between companies is what is known as a network of firms. This refers to an organised collaboration between firms, in particular smaller businesses operating in specific fields, for example, in sales. The goal of such networking is to reduce the inefficiency that is often inherent in the operation of small businesses and to enable them to compete more efficiently with larger companies. The cooperation within a network of firms may involve joint product development, joint sales agencies, a common marketing strategy and joint office facilities or collaboration on research and development. This form of networking can be very suitable for the culture industry, for instance where painters and sculptors share a studio and/or exhibition facilities.

### 5.2.2 Strategic planning

Management is a chain of events, or a process, within an organisation, that is, a business firm or institution that consists in its administration and in the allocation of available resources. The business operations of enterprises consist in setting goals, establishing a strategy, making decisions, implementing the strategy and monitoring. These elements are interrelated, and good relations are necessary in a firm to achieve its objectives; managers encourage people to achieve goals. Management theory includes a broad array of methods that top management and other managers can use to run their enterprises.

The role of top management in an enterprise, the leaders of an organisation, is to decide on the goals, strategy and framework of the enterprise and adapt them to changes in that may occur in the enterprise's environment. Success is of course dependent on the qualities of the individuals

in question and the factors that determine the success of those individuals are the subject of management theory, which addresses issues that influence management, such as competition (in a global context), corporate culture, corporate growth and advancement, corporate structure, assignment of responsibilities, decision making processes, design of work processes, disputes within organisations, establishing targets, ethics, flow of information, governance, human relations (in their widest sense), leadership, and supervision.

Conditions in the external environment of business firms change constantly and are subject to great uncertainty. Individual corporate divisions or departments may respond to these changes in different ways, and coordination can be problematic. An excellent method to use in a business operation is to monitor competitors closely, and a common means of dealing with uncertainty is to do as the competitors do. Uncertainty also encourages leaders of business enterprises to plan carefully.

Corporate strategy, one of the principal areas of business economics, consists in defining an enterprise's principal role, position and image. In a strategy of this kind the groundwork is laid for a vision which describes what management wants the enterprise to look like after a certain number of years or even decades. A framework is also defined which includes the enterprise's policy and the goals that need to be achieved for the future vision to materialise. A detailed and scheduled strategic plan then needs to be established which describes how these goals should be achieved.<sup>5</sup>

A key point is to provide a clear explanation of the roles and objectives of organisations, whether the organisation is a business firm or an institution. Strategic planning involves getting as many people as possible, both management and other employees, to work on the organisation's strategy, and such cooperation requires coordination.

An effective way of achieving a competitive advantage is to focus on minimising cost or somehow achieving a distinction from competitors. The importance of these two approaches is highlighted in the context of the most common market form, monopolistic competition, where price is for the most part a fixed value. A business firm can only maintain profitability over the long term through lower costs than those of their competitors or by distinguishing themselves in some way from other companies in the market, so that products and services will be heterogeneous, as

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<sup>5</sup> For a discussion of the future vision of business firms see, e.g., Porter (1980) and Bilton (2007).

is commonly the case in the market for cultural goods. An organisation will also need to decide whether it will operate in a limited area of a market, a market niche, or in the marketplace as a whole.<sup>6</sup>

In the course of strategic planning in a business four important factors need to be taken into account in assessing a firm's current position: strength (S), weaknesses (W), opportunities (O) and threats (T). This methodology is abbreviated as 'SWOT' analysis.

A SWOT analysis consists in assessing four elements of an enterprise's current position, starting with strengths, which, for instance in the case of a concert hall, could be the size of the hall and its acoustics. An enterprise's strengths may also consist in a qualified staff, sound finances or a good reputation. The second element to analyse is weaknesses. These can manifest themselves in poor financial management or poor executive management. The third element to analyse is opportunities. These can consist, again in the case of a concert hall, in forthcoming performances of musical works that are known to attract large audiences, the launch of an improved advertisement campaign or possibilities for entering new markets, for instance through cooperation with foreign concert halls. The fourth step is to analyse the threats that an enterprise may face. These can consist in competitors entering the market, changed leg-

islation or, in the case of the music recording industry, technological progress in streaming music on the Internet.

SWOT analysis is used in a variety of circumstances and is important in analysing an enterprise's situation in an efficient and organised manner; however, it must be kept firmly in mind that overdependence on SWOT analysis should be avoided. The analysis can give

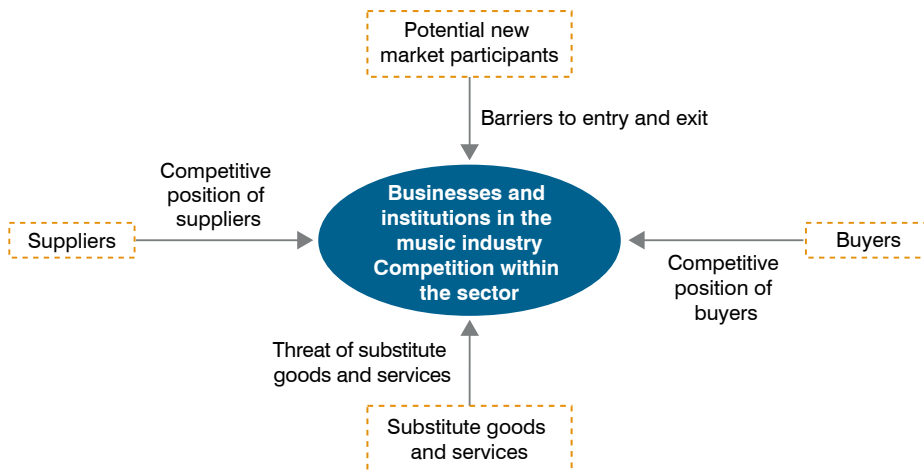
**David Throsby** was born in Australia in 1939. He is one of the best known cultural economists of the world. His book, *The Economics of the Performing Arts*, written with Glenn Withers and published in 1979, was an important milestone in the study of the economics of the arts. Throsby, a professor at Macquarie University in Sydney, has held numerous posts of trust, notably as president of the Association for Cultural Economics International, as member of the editorial boards of numerous periodicals and as an advisor to international organisations and state governments. Throsby is a prolific scholar and his book, *The Economics of Cultural Policy*, appeared in 2010; the book puts cultural policy in an economic context and thereby links together a number of trends in the research of recent years and decades.

<sup>6</sup> An example is The Stuttgart Ballet which was successful for so many years because of the work of the director, John Cranco, and the prima ballerina Marcia Haydée. Together they developed a style of dancing that was immediately recognisable among its aficionados, even after Marcia Haydée was no longer active as a ballerina. The company was successful not because it imitated other distinguished companies, such as the Bolshoi Ballet, the New York City Ballet (under the choreographers George Balanchine and Jerome Robbins), and the London Ballet Company but because it created something unique. Ballet companies, like football teams, live and die with the stars they are able to attract to their companies.

a good picture of an enterprise's situation for the short term, but rapid changes in its environment can quickly lead to obsolescence. SWOT analysis is, therefore, a good example of an analytical tool that needs to be continually reviewed to preserve its usefulness.

Strategic planning, for instance in marketing within the cultural sector, involves organised work methods as in other fields, since strategy is one of the management factors of production. Circumstances need to be analysed and a strategy formulated, laid down in detail and monitored. Strategic planning in marketing is based on the same basic principles as other planning. Various models are used in marketing for the analysis of factors such as market growth, market share, new products and new markets.

The competitive position of enterprises can be shown using Porter's five-force model.<sup>7</sup> Figure 5.2 explains this methodology using music as an example.<sup>8</sup>



**Figure 5.2:** Porter's five forces model on competitive position in the music industry

For this approach to be useful the diversity of the music industry is so vast that a distinction needs to be made between individual enterprises and organisations. Nevertheless, there are many common features, such as the buyers of the music. Most of the activities within the music industry focus on individuals as buyers, as shown to the right in Figure 5.2.

<sup>7</sup> For a discussion of competitive position see Porter (1980).

<sup>8</sup> For a discussion of competitive position in the music industry see Einarsson (2004).

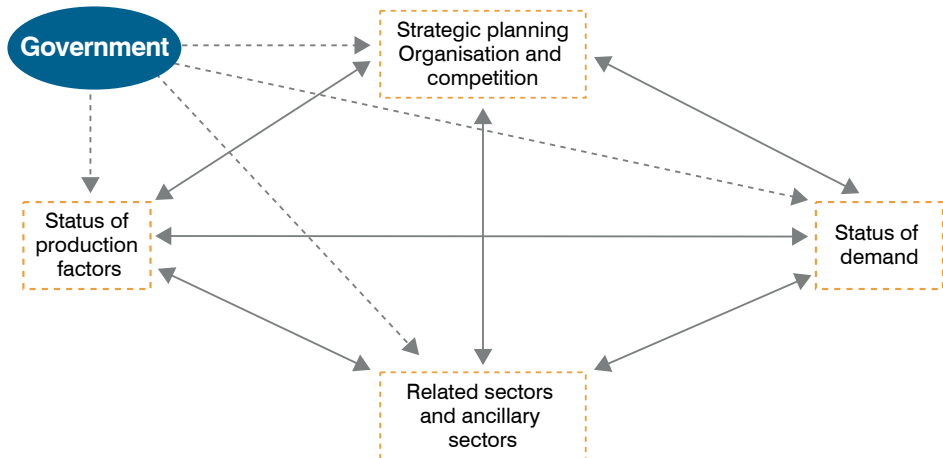


The position of consumers is strong, as music is in competition with various other entertainments. The same applies to localised products and services, many of which are connected with music, and other branches of art and various types of recreation; these are shown at the bottom of the illustration.

Suppliers in the music industry, shown to the left in Figure 5.2, are of various kinds, for example, musicians supplying publishers, music teachers supplying music schools and producers supplying the media. The competitive position of suppliers is usually not particularly strong in the music industry, for competition tends to be fierce. The key factor lies in the middle of the model, which shows the extent of the competition between enterprises within the industry. Competition between business firms is usually extensive in most fields of the music industry.<sup>9</sup>

The top of the illustration shows the possible new stakeholders in the music market. Barriers to entry are usually small. This does not apply, however, to the parts of the market that require substantial capital investment, such as opera houses and concert halls.

This idea can be transposed to the competitiveness of nations.<sup>10</sup> This model examines what has been called Porter's diamond, which is applied here to the music market of a country and shown in Figure 5.3.



**Figure 5.3:** Competitiveness of nations in the music sector

<sup>9</sup> A good example of the way in which demand changes is the trend in Hollywood of producing ever more extensive series of sequels, as in the case of *Mission Impossible*, *The Hobbit* and *Transformers* in a form of recycling. See Beier (2015).

<sup>10</sup> For a discussion of the competitiveness of nations see Porter (1990).

The production factors, shown on the left in Figure 5.3, are labour, natural resources, financial capital, knowledge, human resources, organisation, technology and institutions. In the music industry qualified employees and capital are of the greatest importance. Unskilled labour, for instance, is not prominent in the music industry.<sup>11</sup>

Demand, shown to the right in Figure 5.3, can be unusual in less populous countries because the home market is small, but it is often possible to make inroads into foreign markets from a small market, and there are many examples of such successes as Björk and Sigur Rós from Iceland, as mentioned earlier.

Related industries and support industries, shown at the bottom of Figure 5.3, include music teaching and the media. Music teaching is quite extensive in many places, but reinforcing it undoubtedly strengthens the music industry still further. As regards strategic planning, organisation and competition, shown at the top of Figure 5.3, it is apparent that the financial market is usually weak in the music industry, and it is difficult to obtain financing for new ideas, for instance in the stock market. It is also of relevance here that jobs in the music industry are not very easily identifiable in the labour market and are widely regarded as low-income jobs. Competition in the music industry can promote increased efficiency and greater creative energy within the art. The principal advantage of the environment of the music industry is often well educated or skilled labour, notwithstanding the fact that many popular artists may be self-taught.

Government, shown at the top left of Figure 5.3, can use a variety of measures to strengthen the competitiveness of their respective countries in music and culture in general. Competitiveness can be enhanced through financial support and an improved infrastructure or stronger institutions and better facilities. The creative industries can be strengthened through tax incentives, improvements in the education system, setting more stringent demands for the sector, acknowledging the importance of the industries and promoting research. Relations with the government are shown by a dotted line in the illustration, which means that the government can impact individual factors of the model directly.

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<sup>11</sup> For a discussion of the music sector see, e.g., Burrows (1994) and Menger (2008).



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## 6. Conclusions

‘Culture’ is an extremely broad concept with innumerable definitions. The original meaning is cultivation of the soil, but the word subsequently came to be used to denote activities undertaken by individuals in the context of their communities involving progress and the development of ideas in the framework of human society.

Culture is human behaviour that is carried from one generation to the next and is, therefore, not the possession of single generation but owned and shaped by a succession of generations. It describes, creates, preserves and disseminates human emotions and thoughts through the production of, among other things, cultural goods, ideas, sports, art, languages, religions and customs. But culture also encompasses all the work of presenting and disseminating culture. This book focuses primarily on the arts and cultural goods, the process of their creation and production and the extensive participation by government in cultural matters. The fact is that culture in its widest sense generates more of economic activity than might appear at first sight.

The introductory chapter of the book suggests, among other things, that the fundamentals of economics are easily applied in cultural economics, but there are special features of culture that justify cultural economics as a discrete and independent special field of study. Culture is inextricably woven into the fabric of the past history, current life and future of humankind and, therefore, deserves separate and detailed scrutiny, especially in our times of rapid change and the ongoing process of globalisation.

One of the effects of increased cultural activity is the positive externalities that it creates, which, in and of themselves, provide an incentive for government to provide support for culture. This effect is especially true since it is likely that cultural production will assume increasing importance in the future, because the general public has more and more time

at its disposal for recreation and experience; already, in fact, the experience industry is said to be the world's largest economic sector. Assigning economic and cultural value to cultural activities, as this book attempts to do, provides us with a method of defining a clear economic framework for cultural activities.

Although creation has always been a fundamental feature of human life and progress, it has never been more so than now, with more and more jobs being generated within the creative industries. This in turn has called for greater research in a broad array of areas, such as intellectual property rights, creative clusters and creative cities, and in the course of this research various definitions have been suggested for the creative industries, some of which are discussed in this book with the recommendation that precedence should be given to the definition developed by UNESCO in international comparisons for the purposes of judging the significance of culture in global economies, for collecting and processing such data is increasingly important and widespread.

There are many indications that the creative industries will in this century become a major driving force in the economies of many countries, in particular those of the western world. In fact, the world can be seen to be in the midst of an economic revolution in our time and since the last revolution, the industrial revolution, occurred some two and a half centuries ago the current generation is living one of the greatest, if not the greatest, transformational periods in human history. The role of cultural economics is largely to explain, shape and participate in this transformation.

The second chapter of the book describes companies and institutions in the culture sector and highlights their special characteristics as producers and sources of cultural goods. The production process is described as a value chain which is adapted specifically to the cultural sector. The demand for cultural products is special in comparison with most other goods and services as the interest in, and need for, cultural production increases with greater consumption, unlike most other goods. This means that the potential for creating jobs and increasing productivity is extensive in the cultural sector. But changes in the sector's environment are extensive and rapid and therefore the supply and production of cultural goods needs to be able to adapt quickly.

Many of the goods and services produced in the cultural sector fall within the classification of public goods, which are often either government-supplied or government-supported through the tax system. One catalyst for increased production and productivity in the cultural sector is the formation of delimited areas or communities where the focus is on cultural production because such conditions are ideal for the rapid dissemination of knowledge and expertise, and with increasing capabilities and knowledge of employees and managers the cost of production will decrease with time. The formation of such areas depends to a great extent on the work of entrepreneurs, with their insights, innovative skills and creativity, that make intellectual property law, a domain of government, one of the most fundamental requirements for the continued existence of a strong cultural sector.

Notwithstanding various unique characteristics of culture, the traditional laws and methods of economics can be applied in the cultural sector, as explained in this book, by means of appropriate adaptation to the special character of culture, resulting in models which can be used to explain and analyse such concepts as supply, demand, production, business and marketing for the purposes of both academic scrutiny and practical management.

Chapter three discusses the many reasons that it makes sense for government to support culture and cultural production. Among the purely practical reasons for such support is the important role of culture in support of regional development via the tourist industry. It is recommended that government should establish a formal cultural policy, and a description is provided of the substantial elements of such policies. Since government in any form plays a significant role in the cultural sector with the objective of improving human relations and encouraging public participation in cultural events and generally raising living standards, it is a reasonable endeavour to codify the government's role in a formal policy.

**Ruth Towse** was born in Britain shortly before 1950. She is Professor Emerita of Erasmus University Rotterdam and professor of Economics of Creative Industries at Bournemouth University in Britain. She has conducted and published extensive research in cultural economics and is one of the leading cultural economists of the world. Her most recent book, *A Textbook of Cultural Economics*, first published in 2009, is a comprehensive and integrated overview of all aspects of cultural economics. The book is widely used as a textbook in the study of cultural economics. Towse has held top positions of trust in the academic community. Her husband, Mark Blaug (1927–2011), was a known economist, specialising in the history of economic thought and the methodology of economics. Blaug was also involved in cultural economics, where he enjoyed a good reputation, and he occasionally worked with his wife, Ruth Towse, on research projects.

The chapter describes some effective methods of strengthening cultural work through exports and foreign sales of cultural products, tax incentives, support for art education in schools and studies of successes and failures in the experiences of other nations in their policies. Culture needs to be made as accessible as possible to the general public, and as equal access in general is an important element of all government policy, it should also extend to culture.

Because cultural heritage is one of the most valuable assets that a nation can own, both for its economic and social value, attention to its preservation clearly falls within the responsibility of government. The book discusses policymaking in this light and touches on the usefulness of technological advances, such as, for example, the Internet, in exhibiting, viewing and preserving cultural heritage.

Sustainability, which is the obligation of humankind to take account of the interests of coming generations, is a fundamental theme in current cultural economics, so the chapter discusses culture in the context of sustainability and refers to the links between culture and international development and cooperation. Ideas based on culture, such as the human charity that features in most world religions, could provide useful signposts for humankind's journey through uncertainty, overpopulation, growing inequality and hunger.

Chapter four of the book discusses the ramifications of international trade and its significance for culture and cultural production. An account is given of the manner in which education, culture and growing globalisation in the context of democracy and the rule of law provide a foundation for successful economic organisation, because the nations that emphasise these fundamentals enjoy the highest living standards in the world.

Culture is by nature global, and cultural trade and relations between countries and individuals have existed throughout recorded history. However, trade in cultural goods has grown tremendously in recent decades, and the complexity of this trade and increasing competition now calls for careful marketing based on the most recent advances in marketing theory. The chapter addresses this matter, but also the different market forms and their characteristics, using marketing models which have been adapted to circumstances in the cultural sector with respect to product development and marketing strategy. The distribution of cultural goods is in many ways easier in contemporary times as a result of

improved computer hardware and software, but this also calls for swifter action and increased adaptability in the operation of cultural businesses and institutions.

However, the speed of communications and resulting ease of distribution are also putting cultural diversity in smaller communities at risk, since there is less time to respond to changed circumstances and inflows of cultural trends. The chapter, therefore, addresses some of the work being done by the UN to protect fundamental values in this regard.

Chapter five discusses some means of financing in the cultural sector, where financing is not always an easy matter. The chapter also discusses the use of ratios, which are traditional tools in economics and as useful in the cultural industry as they are in other industries. Since finances in the cultural sectors are often characterised by significant government participation, the chapter discusses that aspect of financing. In addition, the chapter discusses the methods of financial planning, which is as necessary in the cultural sector as in other sectors in order to achieve results.

Strategic planning is an important factor in the cultural industry. But although planning and management in the cultural sector have similarities with planning and management in other sectors, special consideration needs to be given to the fact that work in the sector is often rooted in an artist's or creator's self-image and their personal involvement in their work needs to be taken into account by corporate management.

The volume of production of cultural goods has grown exponentially, and culture is becoming an ever more important part of the world's economy. It is the belief of the author of this book that the production and sales of cultural goods will grow even more, both worldwide and in individual countries, and that increased participation in the global cultural sector could provide a variety of opportunities for improved living conditions in the future. Cultural economics can help to shape that future.





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## About this book

As a key element of any society, culture generates a great deal of economic activity. This book addresses a diversity of topics and concepts relating to this economic activity, such as value, creation and the creative industries, supply and demand in the cultural sector, the role of government and the purpose and formulation of public cultural policy.

Increased and enhanced cultural activity engenders positive externalities, which provides reasons for government encouragement, promotion and support. Another reason is that there are indications that the creative industries will play a fundamental role in the economies of numerous countries in the present century, particularly in western countries.

The author also discusses cultural heritage in the context of development aid, international trade and markets, finance and management. Underlying this discussion is the author's conviction that trade in cultural goods could be even more extensive than it is currently and that active involvement in the international cultural sector can lead to opportunities for an improved quality of living in the future. This book is valuable reading for anyone who takes an interest in culture.

Interspersed throughout the book are brief biographies of individuals who have been influential in culture and cultural economics, along with a number of charts, tables and brief narratives that illustrate the principles of some economic theories in practice..



## About the author



Dr. Ágúst Einarsson is Professor of Economics and former Rector at the University of Bifröst in Iceland. He studied business economics in Germany and defended his doctoral thesis at the University of Hamburg. He began his academic career at the University of Iceland, where he was Professor of Economics for many years, serving during his tenure both as Head of Department and Dean of Faculty.

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Dr. Einarsson has published twenty-six books, including collections of articles, works on microeconomics, on the economic impact of music and film and on cultural economics. He has also published articles in academic publications on business economics, cultural economics and fisheries, as well as chapters in various books and proceedings of conferences. Dr. Einarsson is married to Kolbrún Sigurbjörg Ingólfssdóttur, a biomedical scientist and historian. They have three sons and four granddaughters

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