Apple's familiar domination elusive in China

November 25 2010, By John Boudreau

Apple logo.

Apple is learning to speak Chinese. The Cupertino, Calif., company is on a store-building binge in hopes of creating a massive new market for its products. With two stores already in the capital city, and another two in Shanghai, Apple plans to have 25 stores open in China by the end of next year. And it just revamped its iTunes and App store, allowing locals for the first time to shop online in Chinese.

Analysts say it is critical for Apple to be in China to tap into its growing middle class. In the next two years, Apple could triple its revenue from China to $9 billion a year, according to Morgan Stanley. But Apple's pricey products - and Western-oriented applications - could limit its appeal, experts here say.

The emerging economic giant has a growing class of spenders hungry for luxury products, though it is still a developing country. China has 800 million mobile users and an online population of 400 million - the world's largest for both categories - but a culture of piracy that makes it difficult for Western companies to profit from them.

Apple, which relaunched its Chinese iTunes and App Store in October - it now spotlights localized apps - is moving to counter the competition. Previously, customers had to use a U.S. credit card, or one with dual currency, to make online purchases. The new site has a payment system that allows consumers to transfer money from banks, the preferred method of making Internet purchases in China.

Nonetheless, the company is far from owning this market and might be at risk of losing ground, according to some experts here.

The China App Store offers few applications created by independent developers specifically for Chinese, said Bo Wang, CEO of Bokan Technologies, one of the largest iPhone app developers in China. "Two-thirds of our downloads come from the United States. The rest are from Europe and Japan. In terms of the Chinese market, it's almost zero," he said.

Already, a number of low-end local app stores for other devices have emerged in China, including Sky-Mobi, backed by Sequoia China, said Michael Zhang, founder of a popular tech blog, Apple4.us, in China. Likewise, Motorola recently created a Chinese-language app store for its Android-operated devices in China.

"There are many, many competitors like Sky-Mobi, and there will be more. They have a closer relationship with developers and carriers, and they can help their partners make money," he said. "How will Apple catch up?"

Apple may have trouble convincing top Chinese developers to make iPhone apps specific to the country, Wang said, because of China's copycat culture. Most of them prefer to work for major companies, such as Tencent QQ, the popular portal and instant messaging service, that offer good salaries to engineers who know Apple's iOS mobile platform, he said. Independent developers can make money off services provided through apps but not necessarily from the sales of apps, which can be copied, Wang added.

Without a strong offering of local apps, Apple could miss out on the increasing numbers of wealthy Chinese who don't speak English, who could turn to devices that have a strong ecosystem of China-specific apps, said Si Shen, CEO of PapayaMobile, a game platform built on Android's mobile operating system. Shen said her company switched from Apple's iOS to Android because of other difficulties it had working with Apple. "Apple is at risk of losing rich Chinese in the future."

Apple needs to create closer relationships with Chinese developers - or risk falling behind in the market, said Zhang, who is also an investment manager with Innovation Works, an early-stage venture capital firm founded by Kai-Fu Lee, who until last year headed up Google's China operation.

"You have to make money from low-end users," Zhang said. "There are more than 800 million mobile users now; how many people out of them will be iPhone users? No doubt the iPhone can dominate (among) high-end consumers, maybe tens of millions. But if Android has hundreds of millions low-end users, you will see where app developers go."

But Apple has never been a low-end player in any market and it doesn't make sense for the company to change, said Shanghai-based Gartner analyst Sandy Shen. Its shoot-for-the-high-end philosophy has made the company the world's most valuable tech company by market

capitalization.

"If Apple's strategy is to maximize profit margin instead of market share, then this serves the strategy well," she said. "Apple is not for the mass market but the tech geeks and elites who don't care about the lack of China-specific content."

Most of its customers are highly educated elites, often with experience living outside China, or even wealthy Chinese who give iPhones and iPads as gifts to those with little understanding of how the devices work, said Wang, whose apps include Cute Math, a top-ranked educational program for children.

"They usually use it as a camera or for its phone service," he said. "They are not using it as an applications player. They don't have Apple accounts. They don't know how to download apps."

Apple's China model, Wang said, is like that of other luxury brands here: Aim for the high-end and forget the rest.

"In China, the iPhone is a premium product," he said. "It's not for random people on the street."

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