

Gloves come off when Chinese Web firms chase customers

November 12 2010, By John Boudreau

In China's young Internet industry, competitors draw blood. When Binghao Cheng launched a social networking site two years ago, he named it Kaixin, or Happiness. But he didn't have the money to spare to buy the domain name "Kaixin." So he used Kaixin001, which was not already owned by someone else.

As his company quickly gained popularity, a rival swooped in and bought the easier-to-remember domain name Kaixin - and redirected users of Kaixin001 to its site.

"It's like a knife fight here," said Thomas Chu, chief strategy officer for Kaixin001.

U.S. Internet companies have long eyed China's Internet market, fast approaching a half-billion users, as critical to their growth strategies. Facebook founder [Mark Zuckerberg](#), who has talked about setting up operations in China, is studying Mandarin. Experts, though, say it will take much more than language lessons to survive here.

The Communist government's censorship rules - and behind-scenes-moves long suspected by U.S. executives to help local companies edge out foreign ones - are major obstacles. Google, which never gained large market share in China, stopped blocking sensitive search results earlier this year, triggering a clash with officials and a further drop in usage among Chinese. Other companies, such as [Twitter](#) and [Facebook](#), are blocked by China's Great Firewall.

But it would be wrong to blame the failures of U.S. companies here just on government interference, those in China's Internet industry say. The intense - some would say ruthless and even at times unethical - competition in China, and the speed at which companies are started and change, creates a business climate few Westerners are prepared for.

"It's like a gladiatorial, no-holds-barred fight to the death," said Dan Brody, Google's first employee in China who now runs an Internet investment company in Beijing.

It took Bo Wu, founder of Lashou.com, a Groupon-type deal-of-the-day site, five years to learn how to do business in China after returning from the Silicon Valley in 2000. "When I talk with a customer or a partner, I have to ask myself, 'Is his 'yes' really a 'yes'? Or is it 60 percent 'no'? Is it 'yes-no'?"

Competitors steal each others' employees, if not their intellectual property. They rat out competitors for violations of regulations to the Communist government, disable each other's Web sites and engage in other hardball tactics rarely seen in the U.S. Established Internet companies copy business plans of startups - then set out to destroy the small companies.

"The cost of labor is cheap, and there is no shame in copying," said Hans Tung, a partner at Shanghai-based Qiming Venture Partners, which backs a number of Internet companies, including Kaixin001.

"The (Silicon Valley) culture doesn't work in East Asia," said Jeremy Goldkorn, an Internet analyst who for years has operated a popular blog, danwei.org, which the government began blocking during the summer.

"There are no rules."

There is, though, one rule everyone seems to agree on: Secrets don't

remain secret.

Simply hiring employees can be perilous because "they could be spies for other companies," said Si Shen, CEO of PapayaMobile, an Android-based gaming platform. "They will steal your code and your interface. They don't even change the icons. This is how things go in China."

While the robust competition creates survival-of-the-fittest companies, some in the industry worry that it could in the long run squelch innovation. In the United States, giants like Google and Cisco regularly acquire start-ups with fresh ideas and technology, which in turn encourages other entrepreneurs to create new companies.

One reason large Chinese companies are hesitant to buy start-ups is the persistent question of the loyalty of their employees who, even if they don't steal intellectual property could jump to a competitor in a heartbeat, said Shen Haoyu, senior vice president of operations at search giant Baidu, which has acquired new companies. "People poach employees from each other," he said. "So it gives acquirers a lot less security. What exactly are you acquiring?"

Silicon Valley is a pretty tough place to do business, as well. Corporate giants cooperate with other companies while simultaneously trying to eviscerate them. Company executives trade insults with rivals. Start-ups are constantly rising up and creating new markets and technology to destroy competitors.

But Richard Lim, managing director of GSR Ventures with extensive experience in Asia and a backer of Lashou.com, admits that the "nature of competition is a little bit different" in China.

Zhou Hongyi, founder of anti-virus software company Qihoo 360, puts it more bluntly: "The Internet in China is like a jungle." Zhou, who used to

head up Yahoo's China operations before a falling-out with the company, is known as much for his brilliance as his war-like tactics.

Qihoo 360 is locked in a battle with a former partner, another anti-virus company called Kingsoft. After their alliance ended earlier this year, the companies began targeting each other's software as malware. Each has filed a lawsuit against the other.

"This kind of warfare is interminable," said Kaiser Kuo, spokesman for search giant Baidu. It is not uncommon, he added, for companies to pay local reporters to write something bad about competitors.

Spurring the frenetic fighting is the fact that it's not easy to sell services to several hundred million Internet users in a culture that expects most things to be free online, Kaixin001's Chu said.

Nonetheless, there are riches to be made in China's Internet industry. Online ad revenue is expected to be about \$4.4 billion this year, and Web games could bring in \$5 billion - with projected annual growth rates of 50 percent and 30 percent, respectively - while e-commerce, estimated to generate \$60 billion in 2010, is expanding 45 percent a year, Tung said.

"The stakes are so high - 430 million users in China - that you do whatever you can do to stop the other guy," he said.

The cut-throat nature of the industry has historic roots, said Kai-Fu Lee, the former head of [Google China](#) who now heads up a Beijing-based early stage venture fund, Innovation Works. "People here want money more than people in the United States," he said. "Many families have been poor 100, 200 years and this is their big chance. It's that strong desire for materialism."

It's survival of the hungriest - and fastest.

"We are like groups of armies fighting," Lashou.com's Wu said of the 50 or so deal-of-the-day sites in Beijing alone.

Not long ago, he learned at midnight that a competing site launched a campaign that promised a secret prize to users. Wu, "shaking" with competitive drive, called a 3 a.m. meeting at company headquarters to devise a counter strategy to be deployed immediately - a drawing for a free iPhone for those using Lashou, which effectively blunted the competitor's move.

"If you want to do something, you have to do it fast," Wu said. "In Silicon Valley, people shut their cell phones off after 10 p.m. But that slows you down."

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