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[Tech firms take great leap forward](#)

[They buy into China's infant Net market](#)

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Yahoo will pay \$1 billion for a stake in Chinese e-commerce firm Alibaba.com as it battles other U.S. Internet companies for a foothold in China's fast-growing Internet market.

Other major U.S. Web players such as eBay, Amazon.com, Barry Diller's Interactive Corp. and Monster.com are shelling out big bucks for Chinese companies, although Yahoo hit a new record.

Why the spending spree?

The same reason U.S. companies from Coca-Cola to General Motors have long beat a path to China's door: The nation has a lot of people. And now it has a burgeoning middle class, primed to revel in prosperity by buying consumer goods.

Fewer than 8 percent of China's 1.3 trillion people are online -- but that still gives it 103 million Internet users, second only to the United States with 203 million. By 2009, the number of Chinese Netizens is expected to surpass the number of Americans online. That same year, Chinese e-commerce will be a \$390.9 billion market, according to research firm IDC.

Those colossal projections have U.S. investors salivating -- even though actual Internet sales in China to date are minuscule. Yahoo's billion-dollar deal Thursday gives it a 40 percent stake in a company with just \$68 million in 2004 revenue. It follows last week's dot-com-like debut of Baidu.com -- "the Google of China" -- which skyrocketed 354 percent on its opening day of trading on the Nasdaq stock market, despite having just \$13.4 million in 2004 revenues. Google has a 2.6 percent stake in Baidu and reportedly would like to own more.

Moreover, e-commerce has some big obstacles in a country where credit cards are still rare. Internet transactions are sometimes paid for by sending bicycle messengers with cash. PCs are beyond the reach of most of the multitudes, who had a gross national income per capita in 2002 of just \$940, according to the World Bank.

But its massive demographics and surging economy -- China's GDP grew 9 percent in 2004 -- make the People's Republic seem all the riper to U.S. companies. Now that their early explosive growth has slowed in the United States, Internet moguls see China as vast virgin territory.

"We are doubling down in China because the potential for Internet commerce in that country is simply extraordinary," eBay CEO Meg Whitman told analysts in February. She predicted the number of Chinese online would surpass the number of Americans online by 2009.

"Behind that growth will be 170 million middle-class households by 2010," Whitman said. "In short, five to 10 years from now, (a company's) share of e-commerce in China is likely to be the defining measure of business success on the Net."

Internet companies in China "are getting in at the very beginning of a consumer economy that's really nascent," said Laura Martin, senior analyst with SoleiMedia Metrics in Pasadena. "First movers have the best advantage at creating enormous amounts of value."

Add to that the Chinese propensity for home-grown enterprises, and you've got a mini-gold rush as U.S. Internet firms vie for Chinese partners to help them penetrate beyond the Great Wall.

Peter Sealey, an adjunct professor of marketing at UC Berkeley's Haas School of Business, was chief marketing officer for the Coca-Cola Corp. in 1979 when it entered China.

Like the U.S. Internet firms, Coke allied with Chinese companies. "You always want a partner on the ground who's native to the territory, who knows the political system, who has connections," Sealey said.

The soft-drink firm faced some marketing challenges.

“Coke is an acquired taste,” he said. “We had Fanta Orange soda -- a taste (the Chinese) were accustomed to. We used to take a case of 24 bottles of Fanta and swap in two bottles of Coke. Then we had to run ads explaining that Coke should be consumed cold.”

Internet firms are likely to face a different set of cultural barriers.

The reliance on a cash economy is a big one. To help spur Web transactions, eBay is introducing its online payment system Paypal in China this year. Alibaba, Yahoo’s new partner, already has a payment system called Alipay.

Then there’s cost. “To use the Internet you have to have access to a PC, and PCs are multihundred-dollar items, whereas Coke is a 39-cent good in China,” Martin said.

China does have a growing number of Internet cafes, offering a low-cost way to get online. It also has cell phones galore -- which provide a vehicle for people to shop, search, text-message and make other online transactions.

“Chinese are crazy about cell phones; the penetration is incredible,” said Chris McNally, a China analyst at the East-West Center in Honolulu. “I traveled through a remote, scarcely populated part of Tibet and along the roadside saw poor farm girls speaking on cell phones with their friends.”

Broadband Internet access -- which eases online shopping because it’s not as agonizingly slow as dial-up -- is growing rapidly. About 43 million Chinese have broadband access up from 31.1 million last year.

Still, the infrastructure challenges mean the pay-off for Internet firms could be a while coming.

“We’re talking about a multidecade period here over which things will unfold,” Martin said.

Amazon CEO Jeff Bezos said as much to shareholders at the company’s annual meeting in May, discussing Amazon’s \$75 million purchase of Joyo.com, China’s leading online seller of books, music and videos.

“This is an investment that will take many years to succeed, but it’s an investment worth making in a country like China that’s growing so rapidly,” he said.

U.S. Internet firms pursue China

Yahoo. Spent \$1 billion for 40% stake in Alibaba.com, Chinese e-commerce and auction site (announced Thursday).

Bought Chinese search firm 3721 Network Software for \$120 million in 2004.

Google. Owns a 2.6% stake in Chinese search firm Baidu.com, which went public last week, soaring 354% on opening day. Opened a Shanghai office in May. Partnered with Tencent, leading Chinese instant-message firm, in February.

Amazon.com. Bought Chinese e-tailer Joyo.com for \$75 million in 2004.

EBay. Bought Chinese auction site Eachnet for \$150 million in 2003, a year after investing \$30 million in it.

Microsoft. MSN launched a Chinese-language portal in May as a joint venture with Shanghai Alliance Investment Ltd.

Microsoft is suing Google for hiring away a top Microsoft exec to open an R&D lab in China.

Monster.com. Paid \$50 million for 40 percent of job-recruitment site ChinaHR.com this year.

InterActive Corp. Paid \$168 million for 52 percent of Chinese travel site eLong Online in 2004.

Source: Chronicle research