



Destination Digital: Opportunities in China's media and advertising market

INFORMATION, COMMUNICATIONS & ENTERTAINMENT

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Introduction from Edwin Fung

By many measures, China is already the world's biggest media market and boasts the fastest growing middle- and luxury-classes.

China is the world's largest media market by consumer volume, with more TV viewers, radio listeners, newspaper readers and movie watchers than any other nation. There are 253 million Internet users, 97 million broadband subscribers, and 601 million mobile phone users. Total media industry revenues reached almost USD 26 billion in 2007.¹

However, China has no stand-out traditional media company resembling a Time Warner, News Corporation, Bertelsmann, Hachette, or Dentsu. Nor is it a market that these foreign media giants have found it easy to penetrate.

Some commentators attribute this to the fact that individual media consumption in China is still at a modest level. But this is only a small part of the story. The fact that there is still so much room for the market to grow is cause for optimism, but also a little apprehension.

Edwin Fung

Partner in charge
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If advertising and media companies have not been able to make money thus far, they will need to adapt or seize new opportunities in the years ahead.

Fragmentation of the market has been a key roadblock for traditional media companies, but it has not proved such a challenge for digital media players. Many have quickly consolidated their position in different spheres and have ambitious plans for further growth.

This aspect of media development, particularly the exciting developments in digital media in China, is something which we address in this report.

We hope you find this report interesting and we would value the opportunity to discuss the findings with you.



Edwin Fung

¹ China Internet Information Centre (CNNIC): "Statistical Survey Report on Internet Development in China," July 2008

Introduction from John Ure and Peter Lovelock



John Ure



Peter Lovelock

This report on digital media in China, produced by the Telecommunications Research Project Corporate (TRPC), is a product of our ongoing collaboration with KPMG across the telecommunications, new media, and payments sectors. Two upcoming reports, one on telecom developments across Asia, and another on payments systems, will further emphasise one of the central points made in this report: Asia, and China in particular, is playing an increasingly profound role in the adoption of new systems, new services and, perhaps most importantly, the adoption of new business models.

It is for this reason that the underlying question to the research for this report has been: when will China become the next big media market? China's media market is large and growing fast, but on a revenue per capita basis, it remains a relative minnow. For foreign companies this has historically made participation a challenge. However, media consumption in China is changing dramatically, and much of this is due to the emergence and rapid adoption of digital media.

Newspapers, magazines, television broadcasts, radio transmissions have all been broadly consumed across China for many years. The state-run 7pm nightly news, with more than 500 million viewers, is the most watched

program in the world. However, there has traditionally been a lack of diversity and state subsidies had removed much of the commercial imperative. Digital media has dramatically begun to change the media landscape by providing an alternative means of access to a range of new and existing content, it has sparked a veritable revolution in new media offerings and it has given rise to conversations that would otherwise not occur.

This includes the interaction between marketers and their audiences. Across an ever increasing array of devices and formats, advertisers and marketers are increasingly able to target and engage consumers. As a result, both the media and the programs with which audiences engage are increasing in value as consumer spending increases.

As this report illustrates, media groups in China have become remarkably adept at defining these discrete audience segments and monetising them. It is this success that foreign firms will want to understand as Chinese media companies begin to expand internationally. In the meantime, their domestic success has helped broaden the mainland market out to one where advertising revenues are expanding rapidly making the various new media sectors attractive — if challenging — opportunities in their own right.

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Digital media: Ready to take off? ▢



Digital media can be defined as any content that has been digitised. It can be any form of information stored in a computer or storage device. It can include voice and video data, online news, including TV network and trade press Web sites, as well as blogs. Digital media networks are spreading from the home and the office to locations such as shopping malls, franchises, trains, buses, outdoor billboards and sporting arenas.

However, digital media is not simply about digitisation or *bits*. Digital media is about uniting various different types of content through a single distribution media, or 'pipe', or holding different content on a single platform that can be accessed remotely. This convergence of media raises many opportunities, just as it can dramatically fragment the audience base.

Digital moves mainstream

The vision of a new digital media landscape, where advertisers can post high-definition posters at key times of day, broadcast animated adverts on giant outdoor screens or run sequential copy along a series of screens, has long been anticipated. Recent developments, fuelled by significant investments, means many such visions are now becoming reality. In China, cities such as Shanghai, Hangzhou and Dongguan have emerged as some of the world's most digitised locations.

Any investor looking at digital media needs to consider what interactivity can be enabled once content has been digitised. Where traditional media can be thought of as closed, in the sense that the audience is told what to look at (and when), digital media is interactive, participatory and when it

encompasses Web2.0 technologies such as social networking sites, it becomes 'open' media — open for adaptation by, and with, the audience. In a society where the government exerts a strong influence on different forms of media, efforts are hurriedly being made to bring this new medium under the control of a common regulatory structure.

A growing number of people are logging onto digital networks and searching for all manner of content and entertainment — be it printed, televised, streamed, or downloaded; broadcast, multicast, podcast, or simulcast. This opening up of media has left the world's media and technology companies struggling to find sound and sustainable revenue models.

It is this coming together of content over various networks that we refer to here as 'digital media' and, as such, this necessarily encompasses much of traditional media. Moreover, it is the focus upon sustainable revenue models that necessarily brings into relief the advertising and media buying sectors, as these are the groups that, in most cases, pay for the content to be delivered to the audience. In China, both of these transitioning relationships — the move from traditional media to digital media, and the fragmentation of mass market audiences — have national characteristics that are unique and challenging.

While some successful digital media companies are emerging in China, many successful global media companies are still struggling to find a foothold. Investors looking to champion the next media opportunity remain confused by the many levels of bureaucracy, the complex business relationships and the different tastes and styles that need to be accommodated in different parts of the country.

Content: Quality and quantity

China has more television stations, more viewers, and more televised content than any other country on earth. From a television station perspective, the ability to launch more stations digitally creates the challenge of content. If viewers want a more personalised experience, television producers need to work ever harder to ensure the right content is on the right channel.

An influx of new TV channels should logically have a two-fold effect. First, it should stimulate more local production. Second, it should induce Chinese producers to look elsewhere, including overseas, to secure external content rights. The government has stepped in to encourage producers to deliver engaging local content and to find ways to make it commercially viable.²

² One example is illustrative: the government has a stated aim to expand the GDP contribution from cartoons tenfold over the next 5-10 years. Concomitantly, cartoon production volume in China has surged more than 70 percent annually over the past five years. Part of the driver for animation has been the phenomenal growth in online gaming. For more information, see "The Video Games Market in China: Moving online," published by KPMG China, December 2007



Some broadcasters, such as Hunan TV and Broadcast Group, have been able to step up to this challenge. Hunan TV is listed on the Shenzhen stock exchange and is the originator of a number of popular entertainment shows including *Happy Paradise* (快乐大本营), *Super Girl* (超级女声) and *I am the Champion* (我是冠军). Despite its provincial origins, Hunan TV generates some of the highest advertisement fees in the country. By contrast, many other broadcasters lack the depth of resources and experience to support the demand for switching over and will rely heavily on back-dated content. This is further spurring the demand for other forms of content and entertainment, including those delivered over the web.

In 2007, China's Internet users spent an average of 2.7 hours a day surfing the Internet.³ Thus, while conventional wisdom still holds that Internet and mobile services in China are more primitive than those in the West, the reality is that China leads the way in its adoption of many technologies and applications.

Several hundred million Chinese consumers use instant messaging (IM) software to communicate, bypassing email altogether. According to one estimate, more than 100 million Chinese already write or participate on blog sites.⁴ Chinese consumers frequently use their mobile phones and computers to watch movies, play games and share music.

³ "China's Digital Generations: The 570-Million-Hour Opportunity", Boston Consulting Group, 2008

⁴ China Internet Information Centre (CNNIC): "Statistical Survey Report on Internet Development in China," July 2008

While these applications remained niche areas of development, they benefited from official enthusiasm for the Internet and the ongoing policy of national 'informatisation'. However, leading online video sites now regularly serve tens of millions of users with millions of videos per day. As such, they constitute a new mass medium with extensive reach and impact. This transformation of services such as online video from a niche application to a mass market now presents concerns for traditional broadcasters, business models and the government. Efforts are hurriedly being made to bring this new medium under closer supervision.

Beyond the regulatory challenges, most Chinese online video sites, in line with their counterparts overseas, have yet to generate sufficient advertising

or subscription revenues to offset their expenditures on hosting and bandwidth.

Finally, digital piracy and low price levels have led to some scepticism about the ability of companies to make money in China's digital markets. While local players have been able to adopt creative solutions to produce profits and stimulate share price growth, the challenges for content-based foreign ventures continue to be profound.

Thus, while the uptake in China is extraordinarily exciting and rife with possibility, it is far from clear how many of these companies will survive over the medium and long term. Meanwhile, more traditional media companies are now adapting to the new landscape.



Screening room

Cindy Chen, Chief Strategy Officer, Focus Media

In China, the average time spent waiting for an elevator in a commercial building is over two minutes. But while lifts may move faster in other countries, China leads the way in adopting new technologies to target this captive audience.

"In the US and Europe, lifts are often much faster," explains Focus Media Chief Strategy Officer Cindy Chen. "In China there is more waiting time, so elevator LCD advertising can have a much greater impact."

For Focus Media, the results have been substantial. In 2003, Focus Media started installing flat-panel LCD television displays in high-traffic areas, such as office lobbies. Since then, the group has expanded to commercial location networks, in-store networks, poster frame networks and outdoor LED networks.

In 2007, revenue surged 139 percent to USD 506.6 million. This followed a 242 percent increase in revenue the previous year. This success has cemented Focus Media's position as the largest outdoor media company in China, with some 112,000 flat-panel LCD television displays in over 90 cities across the country.

The key, according to Ms. Chen, is to focus on high-value audiences, which she defines as those earning at least RMB 3,000 per month. Focus Media targets captive environments, such as the hypermarket point-of-sale, the office lobby or the movie theatre. Significantly, the focus upon mid- to high end demographics has meant that the company has steered away from

transportation displays such as those in train stations, bus stops and on the back of taxi headrests.

However, this strategic focus on market segmentation is only one reason for the company's success. The other is a determination to be dominant in whichever sector they enter, which has resulted in growth that has been as acquisitive as it has been organic.

In April 2005, Focus Media began establishing its in-store network, targeting hypermarket shoppers at the point-of-purchase through flat panel displays at prominent locations. By the end of 2007, it had an in-store network of 50,000 flat panel displays installed in approximately 4,000 sites around the country. In December 2007, Focus Media purchased CGEN Digital, its primary competitor.

With the purchase, Focus Media's share of marketplace advertising grew to more than 88 percent, giving it the largest advertising platform in the retail sector to promote sales at the point of purchase.

In addition to this, Focus Media has made a string of acquisitions to consolidate its position in every sector in which it operates. In January 2006 it acquired Target Media, China's second largest commercial location advertising operator, with coverage in 100 cities. They then acquired the elevator poster frame advertiser Framedia; theatre advertising specialist ACL; and Allies Information Technology, the country's largest Internet advertising and interactive marketing services provider.



With the appearance of LCD screens in every conceivable location in China, Focus Media is well positioned to keep growing and encroaching on the advertising budgets normally allocated to traditional media. As Ms. Chen points out according to CTR, in 2007 advertising spend for outdoor media was down 4 percent; for newspapers it was down 1 percent; LCD media, on the other hand, saw advertising spending rise 80 percent.

Looking beyond the numbers, the story of Focus Media also highlights an important change taking place in the advertising industry: while traditional media sectors remain fragmented and heavily commoditised, successful new media companies — other examples being Baidu, Netease and Shanda — have grown to dominate their sectors.

Guiding spirit

Matt Roberts, General Manager, About.com China

About.com, the lifestyle content site, purchased by The New York Times in 2005, established its China presence in January 2007 under General Manager, Matt Roberts, a long time veteran of the Internet and media scenes in China. With revenues exceeding USD 100 million in 2007,⁵ the About Group (which includes the web sites of About.com, ConsumerSearch.com, UCompareHealthCare.com and Calorie-Count.com) is one of the Web's largest producers of original content. *Abang.com*, the Chinese version of About.com, is the first wholly-owned international version.⁶

Roberts opened the China office in January 2007, began running the beta version in November, and formally launched the site in June 2008, after a year recruiting topic experts. As of September, the site had more than 130 such experts, or guides writing about more than 1,000 topics spread across eleven channels, including fashion, foods, health, hobbies, pets, digital, travel, education, sports, toys, and games.

The name Abang, was derived from the Chinese character bang, which means group or community. (*Bang* is also part of the character *bangzhu*, meaning help and *bangshou* meaning helper, which is what the site's guides are called in Chinese. The "a" makes reference to the southern Chinese colloquial honorific when addressing a friend.)

The layout for the Chinese version is considerably different from the U.S. site even though both sites are set up with the same purpose. This reflects

the differences, often quite notable, in the tastes of Chinese web users. For example, Chinese users tend to be wary of commercial websites. "Chinese have been exposed to official messages and soft content for so long that they are very savvy," suggests Roberts. Thus, while American users may instinctively trust a website that looks very professionally put-together, Chinese users instead place greater value on evidence of grassroots user support and participation over sleek design.

In terms of design, another observation is that Chinese users prefer justified text, and find it annoying to run through a list of titles that do not run down the page evenly. Like many major Chinese portals that rewrite titles of news stories to fit the standard length of their homepage, About.com China features justified article text and same-length headlines throughout its site.

The About.com China site can even be quite different in terms of the topics it features and its content structure. The food pages of the site have been particularly popular in China, leading to adaptations, including more nutritional information on recipes. For example, where the English version may cover Chinese cuisine as one topic, the Chinese version breaks foods into the eight major regional cuisines of China.

About.com China uses allyes.com (now owned by Focus Media) to provide advertisers reliable third party statistics to measure an ad campaign's effectiveness.



"One of the challenges that Chinese Internet users face is determining the source and credibility of online content. For this reason, we prominently feature the name, photo and bio of the guide who authored the article," says Roberts.

"Our core offering is credible information and advice designed to help Internet users solve their problems. We're unique in that our content is original and provided by credentialed experts." For About.com it is this structure and breadth which they are counting on to bring about a level of 'stickiness' that advertisers find compelling. If users can be induced to not only return, but to engage in conversation within the site, then advertisers will be presented with a dynamic audience that they can not only market to, but engage with. For Roberts, this is where the future of online marketing in China lies.

⁵ The New York Times Company posted 2007 revenues of USD 3.2 billion. The About Group does not formally break out revenues by territory, but Mr. Roberts pointed out that the Group was "pleased with [the Chinese operation] results since launch."

⁶ The Japan site *Allabout.co.jp*, is an independent company that licenses the brand and technology for the Japanese market.

The transition from traditional to digital media



With an audience of over one billion people, broadcast television remains the dominant media player in terms of audience size, revenues, content, and influence. In 2006, there were 1.19 billion TV viewers above the age of four, three times the US level.⁷ Their average viewing time was 176 minutes per day, which compares to 301 minutes for Japanese viewers and 286 minutes for Americans. By 2008, there were 151.2 million cable TV homes, accounting for more than one-third of the global cable TV viewer base.⁸ Television continues to account for more than 60 percent of all media revenues.

A similar legacy dominance accrues to newspapers, and book and magazine publishing, despite each area seeing their revenues challenged by the

migration of advertisers to new media sectors. There are approximately 2,000 newspapers and over 9,500 magazines circulating in China, 50 percent more than the amount in the US. China circulates 20 percent more newspapers than second-ranked India.⁹

Radio has staged a comeback over the last decade as more urban Chinese own and drive cars. Radio seems set to consolidate as a media niche, aided by broadband Internet delivery.

This chapter therefore examines the nature of the transition from traditional to digital media consumption in China, the emergence of new media players and the role and response of existing media companies, advertisers and media buying agencies.

⁷ CSM Media Research

⁸ National Bureau of Statistics

⁹ In 2007, there were 573 publishing houses including 220 national publishing houses, and 353 regional or local publishing houses. The number of book publications reached 6.5 billion and the number of journals was 9468. In 2007, 1931 individual newspaper brands were published with a total circulation of 41.26 billion units and sales revenue of RMB26.1 billion. There were 220 national newspapers, 815 provincial newspapers, 877 city newspapers and 19 township newspapers.

While TV's revenue market share has declined since the late 1990s, it is still a growth market across the mainland. In 2000 there were 320 TV stations across mainland China; by the end of 2007, there were 683 TV stations.¹⁰

Broadcast industry revenue in China is comprised of advertising revenues, cable TV fees and operating revenues. In 2007, cable TV network revenues reached RMB 25.2 billion (USD 3.5 billion) from 151 million users. Cable

TV revenues include the monthly cable TV fee (RMB 18.4 billion), new services fee (RMB 523 million) and value-added services based on cable networks (RMB 6.3 billion).¹⁰

For the broadcast industry, delivering strong audience numbers and making an impact locally is critical. National radio and TV station revenue accounts for just 17 percent of total revenues generated in the sector.

Table 1: Media market overview

	2001	2002	2003	2004	2005	2006	2007	2008f	2009f
Media (USD mIn)									
TV	3,375	4,694	6,800	8,987	11,247	14,173	16,765	19,977	23,173
Radio					301	501	664	1,000	1,334
Newspapers	1,104	1,521	2,020	2,621	2,764	2,979	3,230	3,451	3,622
Magazines	66	100	178	229	282	357	431	518	622
Outdoor	1,078	1,290	1,468	1,514	1,992	2,461	2,739	3,086	3,898
Internet	60	79	169	303	527	783	1,395	2,305	3,236
Other digital*						333	735	1,338	1,961
Total	5,682	7,684	10,636	13,654	17,113	21,586	25,959	31,675	37,846
YOY % change									
TV	28.6	39.1	44.9	32.2	25.1	26.0	16.4	19.2	16.0
Radio						66.3	30.4	50.6	33.4
Newspapers	15.2	37.8	32.8	29.8	5.5	7.8	6.7	6.8	5.0
Magazines	31.2	51.3	77.7	28.6	22.9	26.7	18.8	20.0	20.0
Outdoor		19.7	13.8	3.1	31.6	23.5	9.5	12.7	26.3
Internet**	41.5	32.6	114.8	78.6	73.9	48.6	75.4	65.3	40.4
Other digital*							117.5	82.0	46.5
Total	43.2	35.2	38.4	28.4	25.3	26.1	18.3	22.0	19.5
% share of media									
TV	59.4	61.1	63.9	65.8	65.7	65.7	64.6	63.1	61.0
Radio					1.8	2.3	2.6	3.2	3.5
Newspapers	19.4	19.8	19.0	19.2	16.2	13.8	12.4	10.9	9.6
Magazines	1.2	1.3	1.7	1.7	1.6	1.7	1.7	1.6	1.6
Outdoor	19.0	16.8	13.8	11.1	11.6	11.4	10.5	9.7	10.3
Internet	1.0	1.0	1.6	2.2	3.1	3.6	5.4	7.3	8.5
Other digital*						1.5	2.8	4.2	5.2
Total	100	100	100	100	100	100	100	100	100

* "Other digital" includes 'screens', ie, wireless (mobile phone), office and in-store LCD, mobile TV and e-magazine.

** Internet includes brand display, paid search, text link ads, classified, rich media ads, e-mail ads and others.

Sources: NMR; iResearch (China online ad market report (Feb. 2008) & iAdTracker); CODC; cited in GroupM.

¹⁰ "Blue Book of China Media," China Social Sciences Academic Press, 2008

As in developed markets, newspapers, once a vital mouthpiece of the Chinese government, are seeing weaker revenue growth. The newspaper sector is growing, but only at single-digit rates: in 2008, newspapers will be lucky to command half the 19.4 percent share of media investment they enjoyed in 2001.

In any city — first, second, third, or fourth tier — it is possible to find bulletin boards placed strategically in the main thoroughfares with copies of the day's newspaper pinned up for anyone to stand and read. The readership of the major newspapers in China, including *People's Daily*, is still phenomenally large, and is still one of the best ways to get a message out across the nation. However, the ability for publishers and advertisers to make money from the medium is diminishing.

The lack of audited circulation figures also makes it difficult to gauge the extent to which circulation may actually be growing. Moreover, in newspaper publishing, carefully-regulated content and a less commercial outlook are still more common. The fact that classified and especially smaller advertisers are being lost to online has made it even harder for these traditional publishers.

Although magazines can be affected by poor circulation and readership data in the same way as newspapers, the medium has been more successful in keeping up with general media growth. Privatisation, or at least semi-privatisation, has resulted in the magazine sector being relatively less regulated. Local publishers have been able to harness their local knowledge with inventive international partners and the results have been strong in lifestyle, leisure and finance publications.¹¹

Magazines have provided one of the important paths into the media market for foreign operators, and there have been a number of very successful publishers such as Conde Nast, Hachette Filipacchi, Hearst and Axel Springer launching titles including *Sports Illustrated*, *Forbes* and *Fortune*.

Another example is the growth of golf-related titles. There is an increasing passion for golf among the affluent, and affluent-aspirants in China, which, despite the volume of titles have produced a high number of profitable ventures. With China emerging as one of the largest markets for luxury goods and lifestyle products, the future for such magazines looks decidedly brighter than it does for newspapers.¹²

¹¹ GroupM: "This Year, Next Year: China Media Forecasts," 2008

¹² See "Luxury Consumers in China: Moving up the curve," published by KPMG China, April 2008



Digital media development overview

The way the Chinese are consuming media is rapidly evolving and the fragmentation of traditional media has created greater space for new media formats to flourish. As Christoph Nettesheim, Managing Director China, of Boston Consulting Group puts it, "Conventional wisdom holds that Internet and mobile services in China are more primitive than those offered in the West. The reality is that China leads the West in a number of Web2.0 technologies and applications — instant messaging (IM), community development, and cross-platform services, for example."

As of the end of June 2008, Chinese Internet users numbered 253 million, more than any other country in the world.¹³ China added 91 million new users between 2007 and 2008, a year-on-year increase of

56.2 percent. Internet penetration reached 19.1 percent, with broadband internet access reaching 214 million subscribers — the second highest of any country. Moreover, as new media booms, only 19 percent of Chinese people are currently online — far below the 60-70 percent in advanced markets, such as the US, Japan, and Korea, and even still below the global average of 21.2 percent.¹⁴

Mobile internet users numbered more than 73 million by mid-2008.¹³ The total number of phone users reached 957.1 million across China, of which 601 million were mobile phone users, an increase of 53.5 million on the end of 2007. In other words, despite having a phone population of almost 1 billion, mobile phone subscribers were still being added at the rate of almost 9 million every month.¹⁵

¹³ China Internet Information Centre (CNNIC): "Statistical Survey Report on Internet Development in China," July 2008

¹⁴ www.internetworldstats.com

¹⁵ Ministry of Industry and Information Technology (MIIT)

Young Chinese, in particular, are taking to the Internet in greater numbers than anywhere else in the world. Among this group, Internet usage has increased by 274 percent since 2003. By comparison, TV viewership has been static and there has been a 6 percent decline in magazine reading.¹⁶ This suggests that young people are not so much 'dropping' TV and print as finding extra time for the new media. According to Marlin and Associates, the Chinese spend a cumulative 1.8 billion hours a week online, 14 times more than the US. IPTV, mobile and digital TV, among others, are offering new ways for entertainment-seeking Chinese to find content.

In 2007, digital goods and services generated an estimated RMB 580 billion in revenues. Revenues are

expected to exceed RMB 1.8 trillion by 2015.¹⁷ Therefore, while there is scepticism about the ability to make money in China's digital markets, China has produced several leading local players who have been able to beat their global counterparts by investing aggressively, customising their services to suit Chinese tastes, and deciding which promising business models to pursue.

Having started from a much lower level, new media companies have achieved far higher growth than their old media rivals and now play a key role in driving media spending in China. Between 2003 and 2007, online advertising sales accelerated by more than 60 percent annually, as compared with around 10 percent for newspaper and TV advertising.



¹⁶ "New media find a place in the high-speed China market," *Admap*, February 2008

¹⁷ "China's Digital Generations: The 570-Million-Hour Opportunity", Boston Consulting Group, 2008

Crucially, new media leaders often dominate their markets in China, unlike their old media counterparts:

- Focus Media commands 95 percent market share in commercial building advertising
- Tencent attracts 80 percent of all instant messaging users
- Sina and Sohu combine for around 40 percent of China's online brand advertising sales
- Baidu, Google China and Yahoo China account for 95 percent of the search market and Baidu attracts around 80 percent of music search traffic market share.

The rapid proliferation of web sites and services in China means that segment dominance is crucial for success. Music and video are currently two of the most popular online services in China (see Table 2). Baidu's dominance of music search traffic has enabled the company to sign strategic partnerships with some 60 overseas and domestic music record companies, including EMI, and Rock Music Group.

This points to another, related trend. China's traditional media companies are looking for ways to cooperate with, if not coopt, new media so as to maintain their own growth. Several of the large portals, including Sina, Sohu, Netease and Tom have begun cooperating with TV stations to provide online video channels for their users.

Table 2: Activities online usage rate, July 2008

Online music	84.5%
Online news	81.5%
Instant messaging	77.2%
Online video	71.0%
Search engine	69.2%
Email	62.6%
Online games	58.3%
E-commerce	57.5%
Blog/space updates	42.3%
Online shopping	25.0%
Online banking	23.4%
Online payment	22.5%
Online education	18.5%
Online stocks	16.9%
Online job hunting	14.9%

Source: CNNIC

Sina has sealed agreements with more than 50 TV channels and over 1,000 content suppliers, including CCTV, Phoenix TV, and Hunan Satellite TV, on content sharing for both videos and live TV programs. It also reached an agreement with Hong Kong Phoenix TV to provide Phoenix programs in Sina's video channel in 2006.

At the same time, IPTV and mobile TV are beginning to generate substantial audiences. China Netcom and China Telecom both have online TV channels under cooperation with various TV stations and traditional publications have also been working with the mobile operators to provide content for mobile services. China Mobile launched its handset newspaper in 2006, providing various newspapers



for subscription, with users able to read the news from their handsets. China Mobile has also teamed up with organisations such as MTV and NBA to launch channels within their value-added range of services.

Online gaming has become one of the most profitable areas for online media, accounting for 80 percent of Netease revenues, and 90 percent for Shanda and 9City, as well as 20 percent for Tencent in 2006. Online formats allow games to achieve a loyalty and longevity rarely seen before. An example is NetEase's *Fantasy Westward Journey* (梦幻西游), which hit a new record number of users in April 2008 more than four years after it was first launched.¹⁸

Perhaps less recognised is the role that online gaming is beginning to

play in advertising. With 120 million online gamers already in China in by 2007, there will be huge growth in embedded advertising in online games.

Now that 3G licenses have been determined, China's mobile media market is bracing for a new phase of growth. In 2007, China had over 50,000 mobile WAP websites providing handset media services to over 100 million users in 2007. Handset media revenues, including handset ringtones, games, handset cartoons, and other publications generated RMB 8 billion. And, as we have seen, online video websites have become increasingly popular — and increasingly problematic — in China, beginning in 2006 and becoming a favorite investment target for foreign investors. Youku, Tudou, ku6 and TVix all obtained substantial foreign investment in 2006 and 2007.

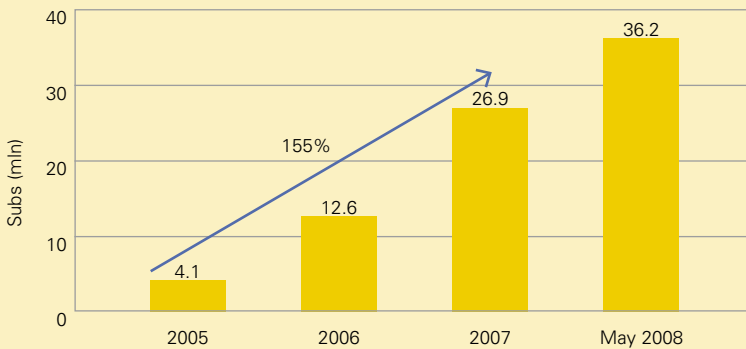
¹⁸ Morgan Stanley Research: "China Media," 27 July 2008

The digital TV market

China's digital TV market has been increasing rapidly during the past few years. From 2005 to 2007, the number of Chinese digital TV subscribers increased at a compound rate of 155 percent reaching 26.9 million (Figure 2). Entering 2008, the digital TV market was adding nearly two million new subscribers every month. By the end of 2007, the top 10 digital TV markets (in terms of number of subscribers) were: Guangdong, Jiangsu, Guangxi, Zhejiang, Shandong, Liaoning, Tianjin, Hubei, Beijing, Hunan and Inner Mongolia.

However, while the digital TV subscriber growth rate has been strong, revenues have been growing relatively slowly. In 2006, TV operators generated RMB 533 million from digital TV services.

Figure 1: Number of digital TV subscribers, 2005-2007



Source: SARFT

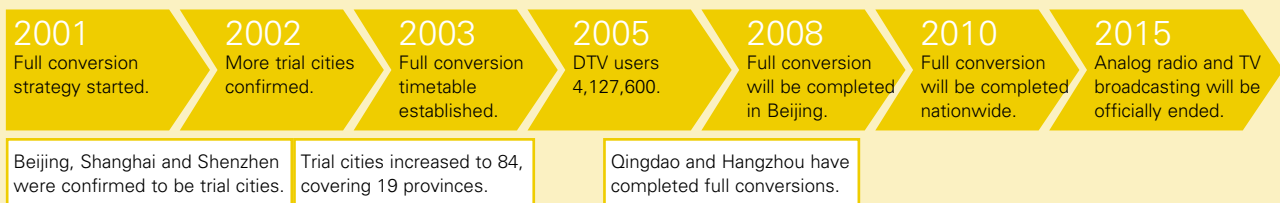
Cable TV operators have been aggressively promoting digital TV services in China. Very similar to the promotion of broadband ADSL services by the fixed-line telecommunication operators in recent years, cable TV operators have been providing free digital TV set-top boxes to subscribers. Subscribers are also motivated to sign up for digital TV services because cable TV operators have been reducing the number of channels on their existing services.

Once a subscriber signs up for digital TV services, they need to pay a monthly subscription fee, which is around 50 percent higher than a cable TV subscription. In some markets, such as Shanghai, the subscription fee can be as much as RMB 80 (USD 11.70) per month — nearly three times higher than the previous Cable TV subscription fee.

Subscribers also have to pay separate fees for other services such as VOD services, subscriptions to premium channels such as English Premier League football. However, not all cable TV operators have been able to attract significant fees for VOD services because of the lack of quality and attractive content. In China, VOD services are also heavily affected by the proliferation of counterfeit DVD programs. Subscribers can easily buy most updated movie and drama at a very low price, making it difficult for the cable TV services to compete.

According to the State Administration of Radio, Film and Television (SARFT), cable TV operators across the country will complete their network digitisation by 2015.¹⁹ By the end of 2007, 53 Chinese cities had established digital cable TV systems, while operators in 31 cities in China had completed network digitisation.

Figure 2: SARFT timetable for analogue television switch-off in China.



¹⁹ SARFT is actually aiming to convert all broadcasts of radio and TV programs in China to digital by 2010, while continuing to offer analogue signals, with a complete switch over to DTV to be completed by 2015. This would be three years after the UK switch-off (2012) and six years after the US switch-off (2009).

Media buying overview

As shown above, China is the world's largest media market by consumer volume. However, advertising spending per capita in China approximates only 2-3 percent of the level in the US. This is despite the fact that advertising sales in China rose fivefold between 1996 and 2007.

Similarly, China's movie box office sales have grown 39 percent annually over the past four years, to USD460 million in 2007. Yet this still represents only 5 percent of the amount in the US.²⁰

On the one hand, this suggests a market rife with promise. Demand is a long way from being sated, and expenditure into these sectors seems sure to increase. On the other, there is a gap between consumer demand and consumer spending. Table 1 (see page 11) shows the Internet to be the fastest-growing advertising medium

with 65 percent revenue growth expected in 2008 and 40 percent growth in 2009. This means that for those looking to make money in China's media markets, the Internet will increasingly dominate marketing thinking, with the biggest growth areas being embedded display ads, sponsorships, associations and created content.

As Alfonso de Dios of P&G, Greater China puts it, "The battleground now is branded entertainment and media innovation. . . we are focusing on digital marketing to build long term and meaningful consumer relationships. We've escalated the spending and the quality of what we do online. That means going beyond web pages to IPTV, as well as mobile phones, social networks, search marketing and other high-tech applications. China has become a learning lab in an ecosystem of providers and platforms."



²⁰ In 2007, Chinese people spent an average of USD 0.3-0.4 individually on movie watching, an amount barely enough to buy half a can of Coca-Cola.

China Central Television

Established in 1958, state-owned China Central Television (CCTV) is the largest TV operator in China. By the end of 2005, CCTV could be received by nearly 96 percent of the country's population.²¹ CCTV currently operates 17 free-to-air channels, and 40 network and digital pay TV channels. The most popular channels are CCTV-1 ('synthesis' channel), CCTV-8 (soap operas), CCTV-3 (synthesis skill), CCTV-6 (movies), CCTV-5²² (sports), CCTV-2 (economics), CCTV-4 (international), CCTV-10 (science and technology) and CCTV News (Table 4). According to CSM Media Research, these nine CCTV channels accounted for 31.1 percent of the Chinese TV market in 2006, and 29.7 percent in 2007.

Table 3: Leading TV channels, 2006 & 2007

2006			2007		
Rank	TV channel	Market share	Rank	TV channel	Market share
1	CCTV-1	9.9%	1	CCTV-1	9.0%
2	CCTV-8	4%	2	CCTV-8	4.0%
3	CCTV-3	3.8%	3	CCTV-3	3.9%
4	CCTV-5	3.7%	4	CCTV-6	3.5%
5	CCTV-6	3.4%	5	CCTV-5	3.0%
6	Hunan Satellite	3%	6	Hunan Satellite	2.9%
7	CCTV-2	1.9%	7	Anhui Satellite	1.9%
8	CCTV-4	1.6%	8	CCTV-2	1.8%
9	Anhui Satellite	1.6%	9	CCTV-4	1.8%
10	CCTV news	1.5%	10	CCTV-10	1.4%
11	CCTV-10	1.3%	11	CCTV news	1.3%
12	Jiangsu Satellite	1.2%	12	Jiangsu Satellite	1.3%
13	Shandong Satellite	1.1%	13	Jiangxi Satellite	1.2%
14	Jiangxi Satellite	1.1%	14	Sichuan Satellite	1.1%
15	Sichuan Satellite	1.0%	15	Chongqing Satellite	1.1%

Source: CSM Media Research

From 2004 to 2007, CCTV's advertising revenue grew at a compound rate of 8 percent, significantly lower than national average of 15 percent.²³ However, CCTV still dominated the market with 22.6 percent share, more than tripling the ad revenues of the Shanghai Media Group, CCTV's closest competitor, according to CSM Media Research.

Every year, CCTV holds an open bidding competition for advertising during its peak hours.²⁴ In 2008, total bidding value surpassed RMB 8 billion, an increase of 11.8 percent on the previous year. Each of the top four advertisers, including RedBull (food & beverage industry), China Life Insurance, the NICE Group (oral care products) and Wahaha Group (food & beverage industry), spent over RMB 100 million to buy advertising hours from CCTV.

²¹ SARFT and CCTV website

²² CCTV-5 was renamed CCTV Olympic for January to September of this year, and during the Games a further six dedicated channels were provided: CCTV-1, CCTV-2, CCTV-7, CCTV-HDTV, CCTV-Football and CCTV-Golf & Tennis.

²³ SARFT website

²⁴ The annual *CCTV Spring Festival Gala* is estimated to be among the most expensive programs for advertising in the world. The advertisement for the 10-second New Year countdown costs as much as RMB 43 million (USD6 million), and the sponsorship for 'My Favorite Spring Festival Program' election exceeded RMB 55 million (USD8 million) in 2008.



At the same time, the business volume of Internet advertising is still only RMB 10 billion, or less than 3 percent of the annual total of China's advertising industry at large. Indeed, even though China now has more internet subscribers, the revenue share is only one-tenth that of the United States.

For marketers, the question becomes one of where to focus and how to mix the various media to successfully target a rapidly fragmenting audience. The Data Center of China Internet (DCCI) found that for the first half of 2008, every Internet user's visits to every website was down 2.7 visits monthly, yet a visit to a site lasted 13.6 minutes longer every month. The fewer visits pointed to lower loyalty, implying greater difficulty for advertising on websites.²⁵

Another emerging media format in China is mobile and LCD screens. The combined advertising spend on these is likely to grow at a higher pace than the Internet — around 82 percent in 2008. LCD screen advertising can be found in more than 100 cities across the country and is growing strongly in commercial buildings, residences, supermarkets, railways and airports. Growth in the sector is occurring across the board, driven by rate hikes, a broadening client base and expansion into smaller cities.

One consequence of Focus Media's success has been that many municipal governments have begun to back their own local LCD ad network on buses or other transport networks. Mobile TVs showing actual broadcast content are also growing rapidly. In Shanghai this medium reaches more than three

²⁵ "China Internet-based consumption rises more than 50% in 1st half," *ChinaView*, 16 July 2008

million people a day. For example, Bus-Online had 25,000 buses at the end of 2007, covering 350 million commuters daily, and it expects to reach 40,000 buses in 30 cities by the end of 2008. The recently relaunched Touch Media runs interactive LCD screens in 50,000 taxis in Beijing and Shanghai, while Universe Holdings, previously known as Epin Media, has installed broadband media systems across the country's high-speed rail network.

The story is similar for television in China. Cable and digital TV in China increasingly offer not just TV channels, but also interactive gaming and simulcast program schedules. The impact of these formats will depend on how they affect traditional TV viewing.²⁶ (By August 2007, there were 24 million Cable DTV homes, a 92

percent increase on 2006.) Powerful monitoring tools and advanced CRM techniques allow brands to gauge the market, and better understand and guide their customers' experiences.

The future of TV in China depends on how marketers integrate television communication with new screen-based digital platforms and content sites. Media agencies must discover the true implications for television audience of the rising 'web warriors' who spend an increasingly large amount of their time socialising, shopping and spending free of the government's traditional media restrictions. In the future, new channels will create new opportunities for media owners, agencies and advertisers to work together to create relevant, engaging, targeted content which is commercially viable.



²⁶ It is also notable that penetration varies by city. Hangzhou for example has a 96 percent digital cable penetration rate, but in Shanghai it is only 6 percent because the local government prefers IPTV — see Chapter 4.

Investor issues in the media sector

China's media and advertising sector has been the scene of frenetic merger and acquisition activity over the past two years, with consolidation in many digital advertising segments and growing interest from private equity and venture capital investors. However, investors should remember that in China, like many other emerging markets, the due diligence process can pose unique challenges.

Understanding historical performance is no doubt a top priority for investors, but a lack of transparency and concerns over the integrity of financial data can significantly diminish the ability to get a true picture of past results. Revenue recognition issues and under-accrued expenses are relatively common, and may distort financial results. This is particularly concerning in an industry that generally deals in intangibles where there can be less evident proof of delivery or complex timing elements. Indeed, certain expenses may go unrecorded altogether. As a corollary of this, it can be challenging to truly understand working capital requirements.

More broadly, investors need to understand their exposure to financial contingencies. Non-compliant business practices around the administration of employee benefits and approaches used to minimise taxes may lead to significant contingent liabilities.

As the saying goes, past performance is no indication of future results and this a mantra that is particularly apt in the media and advertising sector in China, where competition and innovation have made long-term valuations of target companies challenging. Having grown rapidly, many digital media companies not yet have fully-developed budgeting and forecasting processes and non-financial metrics. The complex regulatory environment and the need to obtain licences at different levels or in different regions may also influence the ability of a target company to achieve its stated growth strategy. Moreover, since many media companies have grown quickly, issues may exist in terms of the capabilities of the staff and companies may be overly-reliant on certain key management or creative staff to drive their success.

By identifying the key risks and exposures within this sector, investors can significantly increase their chances of closing a deal.

It's all in the mix

Bessie Lee, CEO, GroupM China

Chinese television broadcasts 2,000 TV channels produced by some 600 government broadcasters, "There isn't exactly a lot of variety in the content out there," according to GroupM China CEO, Bessie Lee. "That means traditional advertising has less of an effect. You need to find another way to make an impact, or you spend the same amount of money but get a lot less than before."

On the other hand, Ms. Lee believes that as new media is still relatively cheap, there is room for experimentation. Thus, for media buying network GroupM, the most important issue is to get the mix right by using a variety of channels that maximise impact. TV, print and outdoor campaigns still have their role to play in China, particularly in Tier 2 and Tier 3 cities where traditional networks remain dominant. But GroupM predicts that spending on digital platforms will rise by 60 percent in 2008 — far faster than any other platform — and new media has become a crucial part of the mix.

In 2007, GroupM subsidiary MindShare worked with Nike on their latest campaign in China to demonstrate the impact of multiple new channels. The 'Zoom' campaign integrated proximity marketing with outdoor and Bluetooth technology by inviting shoppers to race from a digitally-enabled starting point marked by a light-box to a Nike store. The Bluetooth function measured the time taken by each runner to reach the store, and the fastest customer each day won a pair of Nike Zoom shoes and their name on the light-box.

"People really got into the campaign," says Ms. Lee. "We recorded people running to the nearest store, only to turnaround and try all over again. We realised they were actually timing themselves and practicing to try to get there faster." As a result, more than 15,000 people took part in the campaign and sent 250,000 Bluetooth messages.

The issue here is not simply one of impact or of integrating new technologies to attract a specific market segment — it is the use of digital media to interact with the customer base and to reliably gather and track user information. The mass media campaigns on TV, which still attract an overwhelming 70 percent of the advertising budget in China have their place, but they are far less effective in measuring direct impact or providing reliable feedback. Such problems increase the further one moves away from the Tier 1 cities.

Although TV audience data is now fully available in more than 100 cities, the management cost of media planning and buying in such detail is often prohibitively expensive for many local or smaller multinational advertisers. Moreover, the stories of non-enforceability of media placement in smaller markets (where an advertiser pays for premium spacing only to find that they have been dropped for another advertiser) are numerous. Monitoring such media purchases across the diverse national landscape can be trying and expensive. Digital media technologies that allow for immediate measurement and assessment radically change this equation.



For many advertisers, it is not practical to buy time on multiple local TV stations at a premium. It can take years to establish national distribution amid the scale and diversity of China's market. As such, new media is gaining critical mass and moving towards the point where integrated media campaigns are becoming the norm. "People feel left behind if they don't jump in," explains Ms. Lee. "TV, print and outdoor campaigns will still play their role, but new media offer opportunities no advertiser can afford to ignore."

Regulatory developments

Governments around the world are struggling to create the right policy and regulatory mix to support the development of digital media. Often the struggle boils down to whether the emphasis should be on the digital side (the network), or the media side (the content). In this regard, China is no different to many other countries. Indeed, aspects of the recent government and industry restructurings were undertaken precisely to be better able to address these issues.

Recent decisions in countries such as Singapore and Australia have focused on development of the networks, believing that content will naturally follow. However, these are markets that are already inundated with foreign programming. China, by contrast, is determined to build a more vibrant domestic content industry that at the same time utilises digital media to promote wider access. As such, the

government remains central to the development of digital media across the country, as reflected in several important initiatives.

Provincial media bases

Beginning in 2001, with the Tenth Five Year Plan (第十个五年计划), the government began consolidating China's diverse media properties, previously operated by local, provincial and national authorities, into a handful of big, powerful players. A key example, Shanghai Media and Entertainment Group (SMEG), is a state-owned conglomerate with 50 subsidiaries, among them two TV stations, film studios, and a number of newspapers. At the national level, the government grouped some of China's most valuable media assets, including China Central Television (CCTV) into the mammoth China Radio Film and Television Group.

With the advent of the Eleventh Five Year Plan (第十一个五年计划) in 2006, the government's focus shifted from the television and broadcast industries to newspapers and publishing. Three key industry regulations were released by the China National Publications Bureau. These were the *CNPB Working Plans to Further Publications Reform in July*, the *National Newspaper Publication 11th Five-Year Year Key Points* in August and the *National 11th Five-Year Culture Development Planning* in September. The government's focus was the reform of small- and medium-sized newspaper and publishing firms and, specifically, the establishment of 12 cities to become newspaper industry centres, and the creation of 10 media groups.

Simultaneously, the government focused on the development of digital TV and a set of national standards, promoting everything from compression to television transmission. Taken together, these policy-driven changes have provided the framework for digital media to develop.

The result has been the emergence of several cities in inland provinces as important bases for new media developments, in addition to the 'big four' of Beijing, Shanghai, Guangzhou and Shenzhen. Chengdu, for instance has become an industry base for online game and animation industries, Dalian has become a software development centre, and Changsha has provided the country's leading program producer.





This is in addition to various cities becoming centres for specific aspects of digital media development. Hangzhou, for example, has become the centre for e-commerce in China and is home to Alibaba. Dongguan is the most active digital TV market in the country, with 97 percent of homes connected.

Building national champions

This diversity is important on two fronts. It enables the government to distribute resources distinctly, and it promotes broad competition, rather than having development focused solely on a small handful of coastal cities.

The government's objective is to develop strong domestic companies in each key sector, dominant enough in their own market that they can eventually compete internationally.

This is perhaps one of the least understood aspects of China's industrial policy-driven development, particularly in emerging areas such as digital media. The government has for a long time been very clear in its intentions to help foster and develop world-class mobile communications, telecom equipment and IT production companies. More recently, it has been equally clear in supporting national champions in areas such as browser software, search engine, IT security and online games.

As state subsidies are withdrawn from traditional media sectors, and the consolidation of diverse old media operations is pursued, state media outlets are being actively encouraged to compete with each other and the new media upstarts for viewers, ratings and advertising revenue. This has created a market characterised by state guidance and the development of large enterprises, but with fierce competition at the local level.

Network and content separation

One of the most important policies affecting digital media development came at the end of 2007 when the National Development and Reform Commission (NDRC), Ministry of Science and Technology (MOST), MII, General Administration of Taxation and the State Administration of Radio Film and Television (SARFT) jointly published *Several Policies to Encourage Digital TV Industry Development*.

This policy finally lifted the ban on cross-network services between cable and telecom networks, allowing telecom operators to participate in digital TV network operation, and cable networks to provide telecom services such as broadband access.²⁷ The fields open to telecom operators and cable operators are IPTV, mobile TV and digital TV.

The policy had been in development for four years (since 2004) when MOST, MII and SARFT issued the original hearing notice, and its issuance finally broke the line between the telecom (network) and cable (content) worlds — a separation that had been officially set in place in 1999.

What this has meant for China is that where many governments around the world have been moving away from a separation of telecoms and media regulation (or at least seeking a position of working cooperation), the Chinese authorities see content — and the development of a strong domestic content industry — as worthy of separate regulation. SARFT continues to supervise much of new digital media (such as the issuing of IPTV licenses) as well as traditional content.

In July 2007, SARFT published the *Notice to Strengthen Mobile and Digital TV Management*, requiring mobile TV programs to be edited and managed by SARFT-affiliated enterprises; the regulation also mandated that SARFT control over 61 percent of the shares in any mobile TV production firm. In December 2007, SARFT reinforced the rules with a new regulation, the *Notice to Strengthen Video Broadcasting Management in Vehicles, Buildings, and Other Public Areas*, which established the supervision and approval power for the agency over video broadcasting in public areas.

While there has been a subsequent relaxation, the content sectors will continue to be a central focus for the government. Nevertheless, since the early 1990s, the types of media coverage deemed acceptable have continued to rise.

²⁷ The policy became effective on February 1, 2008

Rolling stock

Dr. Feng Li, Chairman, Universe Media

Railways remain the most common mode of long-distance travel among China's emerging middle class, transporting 1.5 billion people each year. Dr. Feng Li, chairman of Universe Media, has found these travellers are a perfect target audience for many of the country's largest consumer brands.

Over the past five years, Dr. Li's company, Universe Media, has created a passenger news and information system that also delivers wireless broadband access on China's upper class air conditioned trains. Dr. Li refers to this emerging advertising medium as '*dung zhong chua me*' (动众传媒), or "media for moving people."

Universe began developing wireless broadband technologies in 2002 and the following year began introducing these systems onto trains. In 2006, it obtained the sole licence from the Ministry of Railways to roll out these applications across the national network.

"We know that if people are travelling, then they are doing so for a purpose and will have needs," he explains. "As such they are a perfect market for advertisers."

Universe itself has taken an extremely interesting journey. "We have seen our role evolve from technology provider to service provider," says Dr. Li. "We develop, install and own the technologies, but on the other side we also work with media agencies and pursue many consumer brands directly and aggressively."

Each train has its own wireless local area network which uploads content. The systems are also available on station platforms and provide a channel for both soft and direct advertising.

The system provides news and entertainment programmes to passengers as well as informative content about each train destination, covering traffic and weather information and advice on the best sights and places to eat. In addition, the system has been used to promote a number of charitable causes. Universe has worked with the United Nations Development Programme to support an AIDS awareness campaign and also provided updates and information from the Red Cross during the recent Sichuan earthquake disaster.

Dr. Li is confident that he has a strong business model, with exciting growth potential and stable costs and revenues. However, he stills sees challenges in conveying the value of this medium to advertisers. "We have to keep emphasising and defining why we are better and also keep an eye out for new revenue models, promoting direct sales or leveraging the provision of wireless networks," he explains.

"We have a captive audience with a strong demographic," Dr. Li continues, "so we have managed to attract some high profile consumer brands and other advertisers such as mobile telephone companies and bank credit cards. China's middle classes are increasingly concerned with raising their quality of life. They equate brand and quality with self-satisfaction, and look to media channels to reinforce their understanding of brands."



A bigger challenge is how to handle the enormous potential of the market and Dr. Li admits that he would like the company to grow even faster. With middle class disposable incomes rising to USD 5,000 and higher in the years ahead, he has no doubt that China's consumer market will continue to grow. He also believes that rail will remain a primary mode of long distance travel and may even attract a more elite customer base as the country's high-speed network expands.

Digital lifestyle and learning

Robby Yang, Business Development Executive, North Asia, Pearson Group

By the standards of many international media companies, Pearson has a long and successful history of operating in China, building across the scope of the group's business interests in education and business information, management and the media.

The Pearson Group's three main arms are education, business information and consumer publishing. In 2007, the Group made USD 8.4 billion globally, an amount that was forecast to increase to USD 9 billion by the end of 2008. While the Group is well-known for its flagship newspaper, the *Financial Times*, around two-thirds of overall sales are generated by its education division. Pearson Education is the world's largest education and technology publisher. Not surprisingly, this has become a particular focus for the company's efforts in China.

Pearson Education is best known in China for co-publishing English language training books, dictionaries and ministry-approved texts. However, these days the growth markets are in specific language proficiency, such as finance, online distribution and exam training and certification programs.²⁸

"Even though China accounts for less than 1 percent of Pearson's revenues, the company has made China a particular focus, both in terms of building market share and in respect to learning how to cross-position its various properties," explains regional business development executive Robby Yang. "Pearson is keen to tap into the rapid growth in Chinese education spending." Both public and private spending on education in China is growing fast.

In early 2008, Pearson entered into the sector by acquiring two English language school chains in China. Learning Education Centre, founded in 2000, provides English-language instruction for children aged five to 12. It has 17 schools, mostly located in Shanghai. Dell English, founded in 1999, offers English-language training to students typically aged between 15 and 35 years old through more than 20 schools, principally in Beijing. These two organisations had combined sales of approximately USD 10 million in 2007.

Pearson quickly developed a cutting edge approach for the two school chains. By integrating white boards, the internet and assessment enhanced interaction, it produced a stimulating learning experience and solid results for the English language students.

Pearson is perhaps best known in China for the Chinese-language version of FT.com, FTChinese.com, and FT Rui, a newly-launched lifestyle magazine. The *Financial Times* has a comparatively longstanding presence in China, with bureaus in Beijing, Shanghai and its main regional editorial centre in Hong Kong. FTChinese.com, was launched in 2003, and by the middle of 2008 had 1.4 million registered users, the majority of whom could be classified as high net worth individuals. And this, according to Yang, is where much of the interest in digital media lies.

"The challenges in China are clear to us," Yang continues. "Specifically, we are determining how to cross-fertilise the different digital platforms, and sell to and monetise this high-end demographic."



According to Yang, Pearson has seen major growth in online advertising as a result of being able to deliver this attractive market segment. However, the Pearson Group worldwide is looking to move away from relying on advertising, since the advertising business globally is "relatively struggling". And in China, price margins face the risk of rapid erosion unless you can stake out a dominant media position.

For the time being, these problems are not overwhelming for Pearson, particularly since growth is still rapid and they have good brand recognition. However, Yang recognises that the various assets need to be brought together into an overall strategic approach to the market so that that Pearson's position can be defended, and the rich vein of content can be leveraged and monetised.

²⁸ Pearson VUE is the electronic testing arm of Pearson Education. It is the authorized global provider of certification testing for GMAT, Microsoft and others. It has more than 130 Pearson VUE Authorised Testing Centres in China.

Regional trends



In China, uneven development and the disparity between urban and rural income levels present enormous challenges for advertising and media companies as they seek to develop an effective business strategy and identify locations with the strongest opportunities.

In recent years, many of the most exciting developments in digital media have occurred in second and third-tier cities, be it Hangzhou's development of e-commerce, Guangdong's leapfrogging into digital TV and mobile newspapers, or Chengdu's animation and games culture.

Second-tier markets growing

The overall development of the Chinese media market remains highly uneven. In 2003, the top three media markets — Beijing, Guangdong and

Shanghai — accounted for over 49 percent of revenue while the top 10 markets attracted over 78 percent.

By 2006, this distribution was even more unequal. Beijing, Guangdong and Shanghai continued to account for nearly 49 percent while the top 10 provincial markets accounted for nearly 90 percent of all revenue. Meanwhile, Qinghai, Ningxia, Hainan, Gansu and Tibet together accounted for less than 1 percent.

Guangdong is presently the biggest provincial media market and by the end of 2007, ranked number one in terms of the number of cable TV subscribers, digital TV subscribers, and newspaper, TV and radio advertising revenues.²⁹ Four out of the top eight newspaper groups in China are located in Guangdong province.

²⁹ This includes taking Guangzhou and Shenzhen city-level stations into consideration.

Compared to the markets in Beijing and Shanghai, the development of digital media in Guangdong is at a far earlier stage. By the end of 2004, only six companies operated online advertising services, with total revenues of less than RMB 8.4 million.

However, several other regional bases are also emerging strongly. Sichuan, the most populous province in western China, is also a large media market in its own right. Much like Guangdong, the traditional media market is dominated by newspaper services. The two largest, Sichuan Daily Newspaper Group and Chengdu Daily Newspaper Group, together generated advertising revenues of nearly RMB 2 billion, accounting for over 50 percent of the total advertising market in Sichuan province. Over the past five years, advertising revenues of the two newspaper groups grew at a compound rate of 16 percent.

Sichuan is also the largest TV market in western China. Sichuan Satellite TV channel was the largest advertising revenue contributor for Sichuan Radio & TV Broadcast Group and has been one of the fastest growing provincial satellite channels in terms of advertising revenues. In 2006, revenues for Sichuan satellite TV reached RMB 600 million, an increase of 37 percent on the previous year. From 2004 to 2007, the viewing population for Sichuan Satellite TV increased by 200 million.

Another surprising feature of the China market is that some relatively small and underdeveloped provinces have emerged to play a key role in certain areas of the media industry.

Gansu, in central China, is home to *Du Zhe* (读者) magazine, one of the top five magazines in the country in terms of both circulation and advertising revenue. In 2006, total circulation for *Du Zhe* hit 10 million, with annual revenues of RMB 300 million and net profits of RMB 40 million. Most of the magazine's advertising revenues came from other provinces.

Another example is Hunan's emergence in the TV sector. Until 2004, Hunan consistently ranked outside the top 15 provincial markets for advertising revenues. With the rapid development of Hunan's TV sector, and in particular Hunan Satellite TV, total advertising revenues in the province surpassed RMB 3 billion in 2006, placing the region eleventh in the country. More than 65 percent of advertising revenues in Hunan came from the TV sector (including provincial level, city level and county level). Hunan satellite TV is now a market leader nationwide, with advertising revenues of over RMB 1.2 billion in 2007.

Hunan TV's rise began in 1997 when the station took advantage of a rule allowing provincial broadcasters to deliver one channel nationally across cable networks. Not content to just retransmit the local agricultural and weather reports — as was the norm on the provincial satellite stations at the time — Hunan came up with a slate of all-new programs geared to popular tastes. Almost immediately its game shows, adapted from relatively conservative Western programs but aimed at a broad entertainment base, became a sensation. Hunan grew so successful that in 1998 it became the first TV studio to list on a Chinese stock market.

Other provinces soon after began competing, and Hunan saw its early lead erode. Their response was to refocus the network almost entirely on

entertainment programming and youth culture, adopting the slogan, "Happy China" and pursuing mass audiences and ratings. Its subsequent successes with *Who's the Hero* (谁是英雄), *Absolute Power* (绝对权力) and, most notably *Supergirl*, have made Hunan China's most successful, and most widely retransmitted station.

A redistribution of revenues

The success of Hunan Satellite's *Supergirl* program has encouraged other provincial satellite channels to try more innovative programming and branded content. There also been an upsurge in local versions of successful Western shows. Provincial satellite TV audiences have grown accordingly, from 19 percent share in 2006 to 21.2 percent in 2007, while CCTV's share has dropped very slightly from 35.8 percent to 33.9 percent.





Satellite vendors are generally much more flexible than CCTV, but a bigger reason for the growth of provincial TV is the cost efficiency gained by migrating from city stations to provincial as marketers expand their distribution footprint.

The question is whether marketers will continue to focus on city-by-city rather than whole provinces at once. Buying a combination of CCTV plus 25 markets is sufficient for most purposes. To buy local TV stations at a premium is simply not possible for many advertisers, and it can take years

to establish national distribution amid China's scale and diversity. When local TV in big markets is too expensive, advertisers have little choice but to rely on CCTV or provincial satellite TV substitutes or other media altogether. As the growth in provincial networks continues, this situation is expected to change.

The growth of China's second-tier cities points to a deeper and even more diverse media market in the years to come, although it may be one that continues to evolve around three or four regional hubs.

Appendices

Cable TV subscribers and penetration by province, 2005 and 2007

Ranking	Province	Cable TV penetration	Cable TV	Cable TV penetration	Cable TV
		(subs per household) 2005	subscribers ('000) 2005	(subs per household) 2007	subscribers ('000) 2007
1	Shanghai	88.7%	4,351	96.9%	4,992
2	Beijing	64.1%	2,820	74.3%	3,443
3	Tianjin	61.5%	1,941	65.6%	2,133
4	Zhejiang	59.0%	8,901	64.8%	10,070
5	Guangdong	58.1%	11,219	67.7%	13,333
6	Fujian	46.4%	4,230	51.3%	4,768
7	Jiangsu	46.1%	10,765	56.7%	13,500
8	Chongqing	42.0%	4,162	42.6%	4,308
9	Shanxi	36.9%	3,104	39.8%	3,413
10	Sichuan	39.9%	10,141	44%	11,194
11	Ningxia	17.20%	340	30.40%	600
12	Liaoning	38.5%	5,164	43.4%	5,944
13	Shandong	36.4%	10,078	45.9%	12,976
14	Xinjiang	35.7%	1,403	40.4%	1,620
15	Guangxi	35.0%	4,500		
16	Jilin	31.0%	2,551	32.5%	2,731
17	Yunnan	30.0%	3,201	37.3%	4,040
18	Inner Mongolia	30.0%	2,131	35.9%	2,600
19	Hainan	29.4%	581	37.9%	764
20	Shaanxi	29.1%	2,997	36.5%	3,837
21	Hubei	29.0%	5,081	36.3%	6,489
22	Guizhou	29.0%	2,803	34.2%	3,334
23	Jiangxi	26.9%	3,289	29.4%	3,667
24	Heilongjiang	26.9%	3,054	34.3%	3,977
25	Gansu	26.5%	1,728	27.1%	1,780
26	Qinghai	24.8%	314	25.1%	322
27	Hebei	24.3%	4,754	33.1%	6,610
28	Tibet	22.6%	1,232		
29	Hunan	21.6%	4,276	25.3%	5,101
30	Henan	18.7%	4,809	20.8%	5,448
31	Anhui	16.7%	3,004	20.6%	3,773

Source: SARFT

Population reached by provincial satellite TV Channel, 2005 and 2006

2005 ranking	Satellite TV channel	Pop. reached by channel in 2005 ('000)	2006 ranking	Satellite TV channel	Pop. reached by channel in 2006 ('000)
1	Zhejiang	737,404	1	Shandong	778,634
2	Shandong	722,866	2	Zhejiang	765,611
3	Hunan	721,619	3	Hunan	757,420
4	Anhui	597,086	4	Anhui	706,688
5	Guangdong	589,095	5	Guangdong	651,557
6	(Southeastern) Fujian	578,613	6	Sichuan	635,691
7	Sichuan	560,963	7	Dragon TV (Shanghai)	607,460
8	Dragon TV (Shanghai)	536,062	8	Jiangsu	559,205
9	Guizhou	498,339	9	Guizhou	517,095
10	Jiangsu	456,606	10	(Southeastern) Fujian	515,371
11	Henan	407,789	11	Beijing	483,040
12	Chongqing	388,120	12	Chongqing	478,859
13	Liaoning	375,535	13	Liaoning	476,277
14	Jiangxi	367,500	14	Jiangxi	472,845
15	Yunnan	362,594	15	Henan	472,291
16	Beijing	350,613	16	Guangxi	433,655
17	Guangxi	329,602	17	Yunnan	392,284
18	Hubei	310,262	18	Hubei	348,970
19	Shaanxi	258,568	19	Heilongjiang	322,589
20	(Travel) Hainan	246,934	20	Shaanxi	303,648
21	Heilongjiang	242,013	21	Jilin	299,336
22	Hebei	220,795	22	Tianjin	287,515
23	Jilin	207,116	23	(Travel) Hainan	282,759
24	Tianjin	196,918	24	Shanxi	244,667
25	Shanxi	193,295	25	Hebei	234,638
26	Inner Mongolia	143,673	26	Inner Mongolia	145,760
27	Gansu	88,106	27	Xinjiang	104,156
28	Xinjiang	82,718	28	Gansu	100,651
29	Qinghai	81,545	29	Qinghai	89,797
30	Ningxia	78,849	30	Ningxia	86,052

Source: China Mainland Information Group

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