Chinese video websites in court as industry grows

JOE McDONALD - AP Business Writer - Associated Press

China's two biggest video websites are fighting in court over accusations they are misusing each other's programming as rivalry heats up in an industry that is luring viewers from bland state TV.

The conflict between Youku.com Inc. and Tudou Inc. is part of a struggle for dominance in an online market with nearly 400 million viewers and dozens of privately owned outlets that might represent the future of China's video watching and a lucrative advertising stream.

"Everybody is shooting for that golden demographic - the young people who are just out of school, have a lot of disposable income and that watch online video instead of television," said David Wolf, a marketing consultant in Beijing.

China's video websites started out imitating YouTube, relying on users to upload cat videos and other free material. But to lock in affluent viewers, the most ambitious started to imitate TV stations, paying to import foreign programs or create their own.

Still more viewers might be driven to video websites by a new government campaign to clean up China's airwaves and promote "socialist core values."

Rules that took effect Sunday strike at a hugely popular market segment for China's ambitious local broadcasters by slashing the number of reality, talent and dating shows they can show on satellite channels. State media say the number of prime-time entertainment shows plunged from 126 in December to just 38 this week.

That hurts local stations just as rising revenues allow online rivals to produce even more content, highlighted by the court fight between Youku and Tudou.

In a Dec. 16 lawsuit, Youku accused Tudou of stealing 60 of its programs including serials called "The Emperor's Harem," ''Hip-Hop Office Quartet" and "Miss Puff."

Tudou says it has filed suit in Shanghai and Beijing accusing Youku of showing a Taiwanese series, "Kangxi Has Come," after Tudou obtained rights to it. The company claims Youku showed Japanese cartoons without the owner's permission.

The companies, both of which have shares traded on U.S. exchanges, accuse each other of trying to use legal claims to gain a competitive edge.

"Youku think they can live on free traffic without paying for the content," said Tudou CEO Gary Wang in a statement, "and they are trying to hide the fact that they are actually not as competitive as they pretend to be."

Both companies reject the accusations in the lawsuits.

"Tudou is playing games," said a Youku spokeswoman, Jean Shao.

Beijing has allowed such private companies to flourish with fewer of the controls imposed on China's entirely state-owned newspapers, TV and radio, possibly to avoid stifling what is seen as a promising high-tech industry.

Their surging popularity threatens to erode viewership for state TV, which Beijing sees as a tool to mold public opinion. That raises the threat communist leaders might tighten controls to protect their media presence.

Tighter regulation might "threaten private online video sites' very existence, and put investors at risk," said CMM Intelligence, a media consulting firm in Beijing, in a March report.

Chinese video websites make money from advertising and also have pay-per-view and other premium services. But while viewership and revenue are soaring, companies are losing money as costs for programs, marketing and Internet bandwidth rise.

The number of Chinese who watch online video jumped from 284 million in 2010 to 394 million in 2011, according to CMM Intelligence. It said the total might pass 445 million by the end of 2012.

Total industry revenue rose 139 percent over a year ago in the three months ending in September to 1.5 billion yuan ($238 million), according to Analysys International, a research firm. Youku had 25.6 percent of the market and Tudou 14.5 percent. Sohu Video, part of Internet portal Sohu Corp., was close behind at 13.3 percent.

Youku, founded in 2006, says it gets 200 million visitors a month. It reported quarterly revenues surged 129 percent over a year earlier but it still reported a 47.5 million yuan ($7.4 million) loss. Tudou, which says it has 90 million registered users, lost 55.6 million yuan ($8.7 million) despite a 52 percent jump in revenue.

Other outlets include Ku6.com, with shares traded in United States, and LeTV, listed on the Shanghai stock market.

Youku has a venture with state-owned China Telecom Ltd. to distribute video on mobile phones and announced a deal in August to show DreamWorks Animation SKG, Inc.'s "Kung Fu Panda" movies on its premium service. Tudou said in November it will show TV Tokyo Corp.'s animated series online one hour after they air in Japan.

Online video also gives foreign broadcasters access to China, where they are barred from most cable systems. Viacom Inc.'s MTV Networks, the Discovery Channel and others have struck deals with partners such as search engine Baidu Inc. to distribute programs.

Managers of China Central Television and local state-owned broadcasters have tried to become more commercial. But the government bars foreign programs from prime time and any material deemed racy or vulgar, leading to a schedule heavy with family-friendly but dull historical sagas and variety shows.

Video websites, with looser controls, show dramas and comedies from the United States, Taiwan and Europe and their own programs. Viewers can download shows to watch on mobile phones during their morning subway ride.

Neither the government nor private researchers have reported on how many online viewers might have abandoned state TV outright.

"We all know it's taking place but nobody wants to go out and publicize the data," said Wolf, chairman of Wolf Group Asia. "The online video guys are terrified that if there are statistics that show the 'golden demographic' dropping TV to watch online video, then the government is going to come after them."