

# On-line Film Circulation in China: The Case of Youku Tudou As a Creative Corporate Soft Power Champion.

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## Abstract

Since China's entry in the World Trade Organisation (WTO) in 2001, the development of Chinese start-ups has been explosive. Their representation worldwide has also been notable with such examples as Alibaba or Youku Tudou (YT). A lot of these start-ups have been tightly connected with the expansion into the media sector. During this recent political-economic transition, the media has been used as a soft power vehicle (ruanshili), both internationally and domestically. This makes it a key strategic sector for the Chinese Communist Party (CCP) to control and shape.

Through the case of YT, this paper addresses the following questions: Before and post WTO entry, how has China been managing its political-economic series of transformations to create the current media context? In that context, how is the Chinese government shaping the evolution of its media system towards the creation of national brands and on-line creative champions such as YT? To which extent, is this influencing China's soft power agenda abroad? What does it tell us about the changing relationship of the Chinese government and its creative industries in regards to Intellectual Property (IP)? Is it a step forward to identify and nurture emerging local film talent?

## Introduction

From 2001, when China joined the World Trade Organisation (WTO) to further develop its economy and open it internationally, the media sector in China has become an increasingly powerful economic tool, which now lies at the intersection of political power and economic development. When studying China's contemporary media landscape it is essential to look at the country's broader political-economic context. Since the Mao era and particularly during the Communist Revolution (1949) and the Cultural Revolution (1966-1976), the media has been considered as a powerful political and ideological tool. [1]

The Chinese media is a contributor to political and economic stability as it generates jobs, it is a source of entertainment, and it has become a significant source of revenue for the country. In 2012, television and film alone generated over US\$15 billion in China, while in 2014, China's total box office reached close to US\$4.8 billion, a 36% increase year on year. [2][3] In parallel, Alibaba Group, one of the largest Internet platforms in the world, has recently purchased the totality of Youku

Tudou [优酷土豆] (YT), an online film circulation platform, in which it already held 18.6%, for US\$3.6 billion and a total estimated deal of US\$4.2 billion.[4][5] This follows Alibaba's plans to expand in the film and creative industries sector since 2013. To that extent, the term creative industries will be used throughout the length of this paper. Although the use of cultural and creative industries is important in the Chinese context, where the terms "creative industries" and "cultural industries" have been used with different connotations (for example "creative" in Shanghai, and "cultural" for more conservative reasons in Beijing). [6] The emphasis of this work is to demonstrate the use of online companies as branded businesses to promote soft power abroad, with arguably a limited emphasis on cultural capital - although it might sometimes be coined as such as part of the promotion of cultural identity by the Beijing-based government.

During the recent political-economic transition of China, the media has also been used as a "soft power" vehicle (ruanshili), both internationally and domestically. [7][8] This makes it a key strategic sector for the Chinese Communist Party (CCP) to control and shape (Chinese media is to this date attached to the Department of Propaganda). This control strategy had already started during the Mao era, from 1949, when the media was totally controlled by the government and officially termed "propaganda." [9][10][11] This approach to media control has constantly evolved and it has been adapted throughout the years with the economic reforms of the late 1970s, after the Tiananmen Square incident of 1989 and after the WTO accession. Over this period, the media has been closely related to political forces and increasingly connected to the economy. With the economic reforms implemented over the past thirty five years, the media in China has also evolved in its structure and its approach. The Chinese economy has increasingly been integrated internationally. Therefore, in this paper, the term soft power will mainly relate to the political agenda of China and its influence abroad by promoting its online brands internationally, while controlling and shaping the media sector domestically.

This research aims to answer the following questions: Before and post WTO entry, how has China been

managing its political-economic series of transformations to create the current media context? In that context, how is the Chinese government shaping the evolution of its media system towards the creation of national brands and creative champions such as YT? To which extent, is this influencing China's soft power agenda abroad? What does it tell us about the political economic characteristics of the power in place and its changing relationship with Intellectual Property (IP)?

This paper addresses the recent political-economic media transformations and processes of change in China from a historical perspective. This historical process will be analysed both in political and economic terms. Although this research does not position itself strictly speaking in the field of political economy but rather in the field of the creative industries, it is important to understand the key political-economic transformation mechanisms that took place in China pre and post WTO accession. These changes were initiated and implemented over a rather long period of time (more than six decades), so the core of the analysis will focus mostly on the period immediately preceding and following the entry of China at the WTO. This study is presented in three parts; 1) an overview of the key political-economic developments and transformations of China before its WTO entry and after, which have been leading to the current state of play in the local media landscape, 2) a case study of YT which reflects these changes. This case study will look at Youku and Tudou as separate entities first while 3) the third part will investigate the nature of the YT merger just before the Alibaba take over announcement. The case study of YT is central to this research, as it describes the creation and the development of one of the key champions promoted by the Chinese government as a microcosm the forces operating at large and the emergence of a creative corporate soft power model with Chinese characteristics.

## **1. China's political economic changes and the definition of a new media context with Chinese characteristics:**

### **Control and reforms in a changing global landscape**

With an estimated population of 1.3bn people, China has gone through a succession of political and economic changes since the 1950s. These transitions have taken over sixty-years to be implemented and can be differentiated into seven key steps occurring before and after Mao's period of rule. Most of the economic reforms led by Deng Xiaoping, from the late 1970s, have been incremental and were the work of a planned political economy and its various adaptations. [12]

Reforms in economics and politics have manifested across all sectors, sometimes outside of the five-year plan framework. The pace of economic reforms has been

cautious and adaptive. Most changes in Chinese economic and social structure appear to have followed this approach, including developments in the media sector. [13] Similarly, Rabiger demonstrates that a documentary represents a slice of society. [14] This suggests that the government's strategic decisions and its representations have deeply influenced the development of the media sector. This sector can be considered a 'microcosm' of the political forces at play. [15] Politically, successive governments were slowly selected and introduced to bring about reforms as smoothly as possible while maintaining the legitimacy of the Party. This reflects the priority of the Chinese government, to provide the stability of society to one of the largest populations on earth. [16]

To put things into perspective, prior to the 1950s the Chinese government had to focus on providing food and basic commodities to a large population and maintain economic growth. According to some, these have been the most notable achievements of the Party and also key features of its legitimacy. [17][18] The resulting, current Chinese political-economic system has been developed over decades and been studied by both academics and practitioners. Some claim that the Chinese system now in place is still fundamentally Communist, [19] while others debate whether it is now effectively a capitalist system. [20] The consensus is that China's system has developed into a dual system and I will apply the term 'hybrid', a more nuanced categorisation that takes account of, and critiques, the Chinese government's officially sanctioned term to describe its system as "Socialist with Chinese characteristics." [21] Since this term is quite vague, it leaves room for interpretation of the intent of the Chinese government, and of how the current political economic system can be defined. My view is that the current system is dynamic. It reflects the existence of a Communist political system that coexists with, and controls, a market economy that is adapting to both external and internal forces.

China's Communist political system and the market economy have developed conjunctly and they contribute to the stability of the Chinese society which is subject to tensions and challenges that the government has to tackle, such as the ageing population, the one child policy and its demographic consequences, environmental issues and corruption. Of equal importance is the promotion of a national cultural identity inside China and abroad, which is commonly called "soft power" and which is greatly facilitated by the media industries which is why, one could argue, the media is closely watched. [22] To that extent, the government has revived some traditional cultural elements such as Confucianism. [23] This trend is accompanied by a tendency of the government to create unity in China through the fostering of a nationalistic sentiment or even "neo-nationalism" whilst reinventing and exporting its culture abroad after the void left by the cultural revolution. [24]

However, promoting nationalism could easily backfire against the controlling power and the Party is increasingly developing inner and outer soft power to rally its masses and the international communities to its way of thinking [25][26] - Neo-nationalism has already led to recent and sometimes violent anti-foreign incidents against the USA, Japan or France for instance. After the Tiananmen Square incident (1989) and subsequent WTO entry, the government became increasingly aware of its international representation and the need to diffuse a positive image of China abroad as well as domestically. The sole use of internal propaganda was no longer an adequate tool. Through soft power, directed both inwards and outwards, the government would have more chances to maintain the country's social harmony and political stability. In this context, in 2004 Jiang Zemin initiated the "Three Represents" theory to promote Chinese culture and identity. [27] The theory was both intended for the Chinese Communist Party's (CCP) own cadres and for Chinese citizens, trying to rally them to a traditional Chinese cultural identity, which disappeared with the Cultural Revolution less than forty years earlier. "Three Represents" was also directed to other nations through the entry of China in the WTO as a soft power tool to try to restore the image of China abroad. It was also used as a means to limit the cultural influence of other countries such as the USA in China by promoting China's own cultural characteristics as being strong and resilient. [28] Additionally, the "Three Represents" theory has paved the way for more soft power slogans with the Hu Jintao's "Harmonious Society" and Xi Jinping's "Chinese Dream." [29]

### **Soft power agenda: the emergence of creative champions**

The promotion of China's culture is central to the way that the creative and media industries have developed post-WTO entry. Chinese media industries are subject to both economic imperatives and above this, tight political agenda and rules. Tensions around the latter are particularly vivid in the eyes of the Chinese government because of the perceived potential for politics to be negatively disrupted as a result of technological forces, especially the Internet, at least as seen in other parts of the world. [30] In principle, the shift to develop culture allows for a greater freedom of speech and a free flow of critical and creative ideas. In the context of potentially disrupting media, how has the government responded and adapted its soft power agenda?

The Chinese government has maintained tight control over its own creative industries, particularly film content. Arguably, the government is the key engine of development of media in the People's Republic of China (PRC). This is evidenced by how the government has shaped all aspects of the media through the issuance of licenses, the imposition of censorship, and the enforcement of quotas for foreign productions to protect its own creative industries and cultural identity. The

building of China's great firewall over more than twenty years is emblematic of this control. It is not only content that has been kept out of China, online foreign media companies have been prevented from setting up business within Mainland China whereas Chinese investments have allowed China to exert some influence on several Hollywood studios, notably through the Wanda group that purchased US-based AMC Theatres in May 2012. [31] It seems that the global IP agenda pushed on to China (mostly by the USA), may not have been that disruptive after all, as it has been harnessed by the Chinese government, through its national champion brands although not without controversies. This has contributed to expand its soft power abroad while the country's economy is further integrated globally. [32]

Although the term champion is not officially sanctioned by the Chinese government, this paper sheds light on how companies such as Youku Tudou are used as brands or champions to promote the Chinese political-economic soft power internationally. The Chinese government has allowed corporations such as Youku Tudou (YT) to expand beyond China's borders. This strategy has been economically supported by transnational investments (FDIs) and substantially from Chinese companies' Initial Public Offerings (IPOs) taking place abroad from the late 90s to the early 2000s. [33] Therefore, the Chinese government seems to have facilitated the emergence and the development of selected digital creative and cultural champions such as YT.

## **2. Youku Tudou as microcosm of the key forces operating at large**

The transition of China from a planned economy to a market economy particularly after China's entry in the WTO in 2001 can be studied through an analysis of YT. The way YT has developed demonstrates China's ongoing tight political control over the media and its concurrent support of Chinese businesses, brands and their use in China's strategies of soft power abroad. YT also illustrates the technological transition of film circulation from being viewed on TV sets to online and simultaneously the rationalisation of the Chinese media sector, which is moving away from piracy and formalising by adopting legitimate practices where copyrights have an increasingly central role.

YT integrates two websites that used to be pirate platforms and are now legitimate online platforms listed on the New York stock exchange (NYSE). Born from a recent merger, YT has become one of the largest legitimate online video provider in China and the second largest worldwide after YouTube, according to Alexa rankings. YT's market share was around 35.5% of the entire Chinese online film-viewing market and it provided films for close to 400 million Chinese users per month in 2012-2013 and now to over 500 million. [34] [35] Although both Youku and Tudou used to infringe copyrights, they now seem to have formalised their

activities and made a transition towards an IP-centred business model. This merged legitimate platform diffuses local, regional, national and foreign content for which it now purchases the rights. Following the success of YT's model and its competitors' the sector has been instrumental in reducing physical and even online piracy by placing IP at the centre of their business model.

This model also facilitates the monitoring and control over the type of content, which circulates online with economic and political implications. Economically, advertising is more targeted and therefore more effective. Audiences can be channelled through these platforms in hundreds of millions which allows for large viewer bases that the US or European markets cannot match. Politically, although this is outside of the focus of this paper, it is relevant to acknowledge that these online champions can be used as surveillance platforms from which the government can control the dissemination of content and ideas. It has managed to migrate local audiences in "controlled spaces." [36] YT also serves the political purpose of expanding China's soft power abroad as a growing brand name and a successful business. With the planned future integration to Alibaba Group, it will undoubtedly help promote further the group's brand name and operations both locally and abroad.

To understand this process, I will analyse YT's as two separate entities before their merger and then observe their key synergies as a single entity.

### **Youku: Prime content and IP emphasis**

The development of Youku has been led by Victor Koo, a Stanford graduate and former President of Sohu, who initially raised finance to create Youku (优酷) through his own fund (1Verge) in 2006. Youku went through several steps before being finally licensed by the government to offer films online legitimately and to produce its own content in a similar way to Netflix. Originally, Youku hosted mostly User Generated Content (UGC) much as YouTube does in the West. It also featured local and foreign pirated content. But Youku's path followed a different trajectory from its Western counterpart: as early as 2009, 70% of Youku's content had become professional and 30% was semi-professional or amateur. [37] The particularity of Youku is that, since the start, it has authorised its users to upload material irrespective of length. This feature was particularly problematic in the early development of Youku, when entire feature films were uploaded on the website and violated copyrights. Youku progressively came into agreements with over 1,500 producers and distributors from the film and TV industries to provide professional content to their viewers. The following study of Youku shows how this transition from being a pirate platform to becoming a legitimate business has taken place.

The year 2009 was pivotal for Youku, since it coincided with vast censorship and anti-piracy operations initiated by the Chinese government. During this anti-piracy campaign, the Chinese Film Bureau shut down hundreds of pirate websites and requested that online film-viewing platforms apply for a license, forcing hundreds of websites to close down including the foreign competitor, YouTube, which was blocked in China. [38] As a result, only a handful of local websites such as Ku6, PPS, iQiyi and YT were able to provide online film circulation to the wider Chinese audience. It allowed Youku and its most legitimate local competitors to gain market shares in the online video sector to the detriment of other platforms, which were screening exclusively pirated content. By January 2010, Youku became the number one Chinese online video provider after the website successfully managed to win over 50% of the online video market, in terms of time spent. [39][40] It also forced viewers to migrate from other pirate platforms and foreign competitors to the remaining local players (about 10 in total), therefore growing their audience and concentrating the sector.

Without a license, online video companies could not continue their business. SARFT's new license became a compulsory element for all the video-sharing companies: for example, BitTorrent file-sharing company BTChina was shut down by the authorities for not being able to secure a license. In the eyes of the Chinese government, the license system would help tackle pirate websites and at the same time formalise the online video-sharing sector, keep foreign platforms at bay, and retain control over the sector's concentration. The license, in effect, gave power to the licensees to legitimately cooperate with TV stations, video production companies and to air their content after purchasing the appropriate rights. It also significantly limited the chances of new players entering the sector as they would have to obtain a license before running their video-sharing business. [41] This move contributed further in the migration of viewers from TV to PC and online viewing contexts.

This government initiative was timed for implementation just before the Initial Public Offering (IPO) of Youku on the NYSE in 2010. It is widely accepted that the crackdown on foreign sites could have also been motivated by a wish to promote Youku along with other Chinese companies that were seeking funding. In 2009, China represented 45% of the entire IPO volume in the US with a record high of 183 ventures launched on the stockmarket. [42] As a reference point, China sold over US\$50 billion worth of shares compared to US\$24 billion for the USA that year. 2010 was also a good year with the capitalisation of 22 Chinese companies on the NYSE including Youku, Bona Film Group and ChinaCache. Without YouTube and other foreign rival companies on the Chinese market, the perceived value of Chinese brands, such as Youku's would increase their chances to attract capital and enhance their business prospects. [43]

However, the success of Youku cannot solely be attributed to the wide-reaching government operations of 2009, which targeted a large number of pirate and foreign Internet platforms; it is also the result of a distinctive, well-designed and implemented business model within a very competitive context. A large proportion of Youku's revenues had been derived from advertising - quite similar to YouTube - and to a very small extent, from subscriptions and pay-per-view (PPV), although these revenue streams have recently been increasing which also contributed to fuel both the cost of local and foreign content. Before the merger, programming accounted for almost 30% of Youku's costs. [44][45]

When Youku was first launched, some of its content infringed copyrights and most feature films uploaded on the website were broadcast without a license. From January 2010, Youku set up a digital system to minimise the issue of pirated content and progressively proceeded to systematically take down pirate material. These measures coincided with the Joint US-China Commission on Commerce and Trade (JCCT), which addressed issues of piracy in China in October 2009. During the commission, Chinese representatives officially acknowledged the negative effects of piracy on the US creative industries and reassured the US trade representatives that the Chinese government would "impose maximum administrative penalties on Internet infringers." [46]

Youku also took restrictive measures on pirated content just a few months ahead of its IPO announcement at the New York Stock Exchange (NYSE), which indicates that the company intended to legitimise its business in order to attract foreign capital. In an effort to integrate with the global IP regulations, it complied with the international IPR framework and made it a central part of its business model. Youku also allowed the Chinese government to monitor its platform and to decide on what content may be inappropriate and should be removed.

This example shows that a combination of technological, global, legal, economic and political forces have largely shaped the online Chinese media sector. This marks a transition within the Chinese film-viewing sector from being exclusively centred on pirate activities to becoming a legitimate enterprise. It also shows the increasingly central role of IP in China, driven both by transnational and local political forces. This IP centric corporate approach, characteristic of Hollywood, [47][48] makes IP an integrated feature of online players that serves both political and economic agendas in China.

### **The creation and formalisation of Tudou**

While Tudou was created before Youku and represents an important component of YT, it was Youku that effectively purchased Tudou and drove the merger. On 15th April 2005, one year before the creation of Youku, Shanghai-based Tudou (土豆网 or TùdǒuWǎng) was

officially launched by co-founders Gary Wang and Marc Van Der Chrijs. Tudou initially started as a blog hosting website, a few months later, they developed a video-hosting platform, similar in concept and features to YouTube. Before the merger, Tudou had already built a large viewer-base and enables access via mobile telephone technologies, which turned the merger with Youku into a significant opportunity: a brand new hybrid model using both Netflix and Youtube's key features to circulate content across multiple platforms.

In the summer of 2007, Tudou had the fastest Internet growth in China; the number of video clips viewed per week increased from 131 million to 360 million with an average of 40 million visitors per month. [49] Tudou started working on wireless and mobile video technologies as early as September 2007 in collaboration with Intel. As a direct result of its focus on mobile technology, by August 2011, Tudou had close to 15.5 million mobile subscribers on China Mobile alone making it one of the largest mobile operators in China. [50]

Similarly to Youku, state intervention was instrumental in Tudou's transition from a pirate platform to a legitimate online business, but transnational political-economic pressures also contributed to these transformations.

In that sense, Tudou did not try to advertise itself as a challenger of YouTube prior to its IPO, mainly because it was originally used mostly to screen pirated content. For example, in 2007 on TVLinks, a UK website acting as a linkfinder, many US mainstream films were directly connected to Youku, Tudou, and 56.com websites, where the copyrighted content could be accessed for free and sometimes even featured Chinese subtitles. With an estimated 2,000 films infringing copyrights and a traffic ranked 214 on Alexa with 40% of US-based users, Tudou became a significant East-West pirate gateway, which represented a major threat for the right holders in Europe and particularly in the USA. Not only was the US film industry struggling to penetrate the Chinese market with the quotas and censorship restrictions, which prevented access to the large potentially lucrative Chinese market, but they were also running the risk of seeing their own domestic market getting eroded by these Chinese websites. [51]

Despite several attempts from the industry to target the end viewers, very little could be done legally against users watching films in streaming mode, since it was made available by a foreign server. The only way to counter such pirate activity was to shut down the infringing websites which, outside China, required a lengthy and costly legal action. [52] Therefore, it became a priority for the US film industry to lobby internationally to reduce the negative impact of the Chinese websites on their own markets and to formalise

the Chinese sector, for instance during the JCCT and through WTO claims.

To that extent, some commentators have suggested that China has been much more willing than the USA to implement trade and trade-related international agreements and that this willingness to be seen to play by the book can also be considered as a political soft power strategy. [53][54] However, it was also widely suggested that these transnational forces had exercised effectively less influence as what was initially perceived. The government and the media sector itself were largely responsible for the shaping of the online video industries into a legitimate and formalised business. [55]

The US film industry's lobbying efforts cannot be disregarded as contributing factors to the formalisation of the online film-viewing sector in China, but it can be argued that the media sector started regulating itself by bringing more cases to court. In 2009, Tudou was sued by one of its rivals, Joy, and 80 right holders for infringing copyrights on some of their content. [56] Youku and Tudou also sued each other ahead of their merger in regards to copyright infringement issues. [57] In one instance, Tudou was fined for a total of RMB50,000 (US\$8,000 equivalent) for screening a Chinese film, Hao Ning's *Crazy Stone* [*Feng kuang de shitou*] (2006), without purchasing the rights from NuCom, an online rival platform. [58][59] As it has been for Youku, the year 2010 was key for Tudou in terms of negotiating a transition from being a platform which operated largely in the informal economy, to becoming a legitimate platform, which operated in the formal economy. From 2010, Tudou posted official guidelines regarding piracy and rules against copyright infringement on its website to raise its users' awareness about piracy. [60]

In 2010, Tudou started to purchase the rights to legitimate and professional film and TV series content. Similarly to Youku, Tudou acquired exclusive film content from Hollywood right holders, which cost the company millions of dollars in licensing fees. The purchase of the rights coincided with both the JCCT and Tudou's own IPO (on NASDAQ). While state intervention placed more emphasis on IP, it also increased government control over the online video sector and contributed largely to shape the existing online media landscape towards an IP controlled corporate model.

### 3. The Youku Tudou Merger: Economies of scale, IP creation, and sector concentration

#### Price of content and economies of scale

At the time Youku and Tudou announced their merger on 12th March 2012, Youku was ranked by Alexa 10th and Tudou 13th in China, which translated respectively as 49th and 65th worldwide. [61] After the merger took

effect in August 2012, the resulting online-video group was the largest in China, with a value of over US\$1 billion, which made it the largest Internet deal in China at the time. [62]

This merger had enormous potential in terms of converging platforms, leading to cost reductions in bandwidth, content acquisitions and increased advertising revenues. Although the two brands remained distinct, the cumulative viewer base of YT made it one of the Internet pioneers in China and abroad. The timing of the merger was expected to take advantage of regulatory changes that would allow online video platforms to strengthen their position within the Chinese media sector and enable them to compete against state television. To that extent, the merger between SARFT and GAPP into SAPPRFT in March 2013 would facilitate this strategy.

The merger was also allied to agendas of the media sector and the government, specifically to identify and promote local IP and film talent, to produce films for its local market and to export them as soft power.

One of the key factors for the merger were the losses that both Youku and Tudou had consistently incurred over the years. Despite rising revenues and a joint market penetration of 75% on average in 2011 and 2012, both Youku and Tudou remained unprofitable businesses. [63] Combined losses persisted after the merger, reaching US\$34.54 million (RMB219 million) in the third quarter of 2013 and US\$55 million (RMB348 million) in the third quarter of 2015. [64][65] These losses were attributed to the rising costs for Internet bandwidth, mobile video services and the significantly heightened cost for purchasing copyrighted content. Even though the merger helped rationalise these costs, they still represented a significant expense.

At the end of December 2012, just a few months after the merger, YT's portal offered a selection of 4,500 films, 2,700 TV series and more than 900 variety shows. The content could either be streamed for free (with advertising) or accessed with paid subscriptions or PPV. This acquisition strategy, implemented over the course of several years, was a fundamental departure from Youku and Tudou's initial business model, and that of most online film-viewing platforms (pirate or legal), including YouTube, which relied almost entirely on advertising revenues. Some of the YT licensed US Hollywood studio productions included *The Vampire Diaries* (2009-2011), *The Walking Dead* (2010), or *Mad Men* (2007), *Schindler's List* (1993), *The Mummy* (1999), *Being John Malkovich* (1999), *The Big Lebowski* (1998), and *Jurassic Park* (1993). [66][67][68][69][70][71][72][73][74][75][76] In that sense, YT developed a new hybrid model for China, which positioned itself between YouTube's and Netflix's business models and tried to take advantage of both worlds: attracting high volumes of viewers through its social network activities and then selling them premium content.

The increasing demand for premium content via the Chinese online platforms and TV channels continued to drive the prices of content up and simultaneously raised the importance of copyright and IP in the media landscape. The transition towards a model that also included subscription and PPV revenue streams was a new concept in China for an audience that, up to then, had mostly benefited from free entertainment and media content. [77][78] However, audiences adopted the new model relatively fast: by November 2012, YT had 2 million paying viewers who could either opt for a RMB15 (US\$2.50) monthly membership (subscription fee) or a RMB5 (80c) fee per film on average for PPV services. [79] Gary Wang, former CEO of Tudou, claimed that viewers were starting to “get used to paying for content.” [80] But to make this strategy viable, online platforms would need to keep securing exclusive access to quality content whose price kept increasing.

In the short term, purchasing rights from regional players such as TVB has helped YT keep their content related costs under control. Various analysts have commented on the fact that the YT merger allows the group to reduce the copyrighted content costs through economies of scale by exchanging and cross-releasing content. [81][82] Compared with online platforms located in other parts of the world, Chinese online video providers such as YT could also take advantage of the lack of structure regarding the distribution windows in China. Until after the merger of SARFT and GAPP in 2013, the Chinese digital release windows had been enjoying more flexible domestic regulations in regards to quotas and censorship than the Chinese theatrical window. When it comes to online film-viewing in China, online video providers also operate on one of the most populated single territories: a potential audience of over 500 million Internet film-viewers, a market for which YT had a dominant market share. [83][84] However, this translates both into higher bandwidth and IP costs.

### **The importance of creating IP**

The increasing price of content had not simply resulted in the integration of copyright and IPR in the online platforms’ business models, but it had also prompted new tactics, particularly from YT. As part of its goal to reduce the cost of purchasing content, YT had started to emphasize the production of its own original content to simultaneously reduce content acquisition costs in the short-term and to become less reliant on it in the long-term. Both Youku and Tudou had initiated the production of their own content prior to 2012. For instance, Youku financed and produced *Hip Hop Office Quartet* (2011), which had more than 100 million online viewers in 2011. [85] This trend seems to have intensified after the merger. In 2013, five of the Youku Tudou’s produced shows were in the top 10 of the group’s most viewed content. This decision to produce and promote content made financial sense for YT since, in most cases, in-house production significantly reduced

the costs associated with content acquisition, given that an in-house feature film can be produced for as little as RMB1 million (c. US\$167,000). [86] Following the same strategy, YT renamed its production house ‘Heyi’.

After the merger, Tudou and Youku’s websites still existed independently with a certain level of brand fragmentation, which in time could have created a brand identification and validation issues. While Tudou and Youku and remained complementary, the group renamed its operations Heyi (literally meaning ‘unify’) to promote the production of its own content with a common brand. [87] In that regard, the company tried to regroup its distinct target audiences: Tudou.com had positioned itself in the ‘fashion’ and ‘youth’ target while Youku was more of a ‘mainstream’ online-video provider. [88] In 2013, Heyi started to coproduce prime content with global companies such as Canal+. Heyi coproduced *Outcast* (2014) with Nicolas Cage for an estimated budget of US\$25 million. [89][90]

The group also chose to turn toward prosumer video creators through its ‘New Revenue Sharing Program’ launched in June 2013. The program gave young talented video creators the opportunity to be paid for producing high quality UGC, sometimes in the range of US\$3,500 to US\$10,000 per month. The operation has been successful so far and YT has entered agreements with c. 600 selected partners. [91] The decision of YT to screen a blend of exclusive mainstream films, regional and in-house productions, along with prosumer content allowed the group to control the cost of its acquisitions, while simultaneously ensuring that it still operated legitimately, continued to attract large online audiences, and even own and manage the rights of its own original content.

Since 2008, Tudou has organised the Tudou Video Festival, an online independent film festival to attract and build loyalty with young urban audiences. In 2013, for the festival’s 6th edition, the website registered 18,000 entries (almost twice as many as Sundance) and had 230 million online viewers. The festival also moved across several cities and screens films during events at various locations including Beijing, Shanghai and Guangzhou. [92] The festival started collaborating with Sundance from 2011 and acts as a large catalyst to identify and nurture local emerging talents. [93][94] Some of the participants have been able to find their audience and reached up to 1 billion viewers. [95] YT also finances original content from local filmmakers, separately from the festival, sometimes propelling them to fame while knitting a long-term working relationship with them and retaining the copyright of their work. Besides becoming a central part of the online creative corporations, IP seems to be combined with the promotion of emerging talent as a vehicle of soft power both locally and abroad.

### Product placement and advertising standards

The new directions taken by YT in terms of content production have not only allowed the group to reduce its cost of purchasing content, it has also contributed to increase its advertising revenues and to build a distinctive and unique social and corporate image. Large corporations such as General Motors started advertising on Tudou before the merger and sometimes contributed financially to produce original content for the Chinese market such as *Miss Puff* (2011) an online animation series that targets the young female audience. [96] In this Beijing-based animation, one of the protagonists owns a GMC car, which was a good product placement opportunity for the car manufacturer. Additionally, YT has been competing domestically for audiences and advertising revenues against national and provincial television networks, which are usually quite fragmented. The most popular TV shows typically capture 2-3% of the national audience so there is scope for YT to build larger audiences than the local or national TV networks. [97]

The Chinese TV network is still state-owned and suffers from significant levels of bureaucracy, which YT tends to be free from as a private enterprise mostly co-financed by US and Chinese transnational capital. Government restrictions have also led young Chinese to migrate from their TV to online platforms to access Western and on-demand content. [98] When online regulations come into place and allow online-viewing channels to compete directly with the television networks, it is expected that an even larger part of the audience will move online. YT has another advantage compared to the local TV networks: on Youku's website there is about one minute of advertising per hour, compared with 12 minutes on Chinese TV, which gives YT considerable space to operate and increase its advertising revenues.

Appealing to the advertisers and providing them with a good service seems to have been at the core of both Youku's and Tudou's strategies even before the merger. In 2010, Youku was the first online-video website in China to use third party auditing of all its videos. Youku partnered with CR-Nielsen, a Chinese joint venture between Nielsen and ChinaRank, to systematically and independently monitor the ads and transfer the data directly to the relevant advertisers. [99] Based on transparency, credibility combined with its IPO, gave Youku a distinct advantage in attracting advertisers to its platform. It was also part of the group strategy in negotiating its transition from a pirate platform to a legitimate business. At the same time, Youku did not simply look to comply with State-led and transnational IPR regulations, but it positioned itself as a pioneer company that demanded urgent standardisation of ad-tracking criteria, for ad effectiveness, and for transparent ad-tracking systems to be implemented. [100]

In a similar way, Tudou challenged the Silicon Valley-based Alexa ranking criteria as a set of data, which can

sometimes be inexact and potentially misleading. In particular, Tudou challenged the concept of the 'click' largely promoted by Silicon Valley-based dot-coms, which may have lost some of its initial significance, and instead focused on new criteria such as time spent on the website, unique visitors, and user "stickiness." [101] YT has been challenging Internet practices both at home and abroad in order to reshape a fast changing online landscape for what appears to be better practices, but first and foremost to remain a market leader and a Chinese creative champion spreading soft power abroad. This series of tactics should now serve the overarching Alibaba brand after the takeover is complete. Beyond the transition of YT from a pirate platform to a legitimate business, which values the concept of copyright, these changes also illustrate the transformation of the company's original business culture. YT and Heyi have essentially developed a corporatist, IP centric business model and culture, similar to Hollywood, which also operates as a soft power vehicle for China.

### Consolidation of the online creative champions

The political-economic agenda of the media industries (traditional and online) and that of the government are to create corporate brands primarily as soft power expansion political tools internationally and, to some degree, as a way to attract additional revenue streams from both local and foreign markets. This strategy is more effectively applied if there are only a handful of Chinese players to promote internationally and it makes the sector easier for the government to control. This has meant that the film and particularly the online sectors have had to consolidate rapidly.

The concentration of the online sector is exemplified by the recent takeovers of PPS and Iqiyi by Tencent, Youku and Tudou's merger, and more recently with Alibaba's purchase of a 18.6% stake in YT in 2014 and the successful offer to purchase the remaining control of the company in October this year. [102][103] These series of consolidations seems to show the government's intention of increasing its supervisory role over the online economy. The rationalisation of the sector is reflected at a political level and coincides with the merger of official departments, for instance GAPP and SARFT merged into SAPPRFT in 2013.

The government has regulated and controlled the sector to balance the number of companies operating in it. It has avoided situations of monopolies and at the same time it has consolidated the ecosystem so that the champion brands can economically survive in it. Supporting online brands and creative champions while avoiding monopolies comes from the imperative to create more jobs, and develop the sector in a sustainable and harmonious fashion. These measures also have an underlying political motivation as they make the sector easier to control. Additionally, they make it easier to promote and diffuse a handful of strong emergent brand names from China and to spread their soft power



globally. This corporate framework also contributes to identify and promote local emerging talent online. This could be a long-term soft power strategy if these talents are nurtured and grow as creative ambassadors.

## Conclusions

Since the beginning of the Chinese reforms, particularly in the 70s and after the WTO accession in 2001, macro political-economic transformations have influenced the evolution of the media sector in China. This is particularly true of the online media sector which has gone through successive phases of formalisation and rationalisation with an increasing emphasis on the corporate development of IP and talent.

The sector has received a lot of attention worldwide, with successive IPOs, and posed new challenges to both Hollywood and the Silicon Valley companies. Local talent, Chinese standards and brands have been promoted in a corporate fashion that shows a different business culture emerging within China. The series of carefully planned strategic changes and tactics of adaptation by the Chinese government also mirror the growing trend of corporate culture.

After the promotion of Confucianism and national pride, could China's next move be described as a development towards a corporatist system whereby emerging creative talent could be identified, selected and nurtured by the corporate political-economic systems in place?

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