Emerging Markets Insight

SPECIAL REPORT

MICRO FIRMS ROCK CHINESE FILM INDUSTRY

CHINESE MOVIES ARE CURRENTLY GOING THROUGH THE "INDUSTRIAL" PHASE AND SMALL FIRMS ARE DRIVING THIS TREND, FROM MARKETING TO POST-PRODUCTION.

- WHAT SECRETS LIE BEHIND THAT MOVIE TICKET?
- PPL TAKES ITS PLACE IN FILM
- BAD ENOUGH TO BE SUCCESSFUL
- MAKEUP ARTISTS FOR MOVIES

BY MIRAE ASSET FINANCIAL GROUP
Q1 2014
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Earnings per share (EPS) of Indian companies in 2014 are expected to post a record high since 2010. In addition, India’s stock market is regaining global confidence on the back of the announcement made by the new President of India’s Central Bank to reform the nation’s financial sector.

The number of tweets reached 350,000 per minute in 2013, growing 2.5-fold compared to the number in 2012. Youtube also posted stunning growth, with the number of content video hours uploaded to Youtube each minute increasing from 30 hours in 2012 to 100 hours in 2013.

Brazilian stock market and prices of iron ore show a high correlation. They move up or down together. As prices of iron ore are expected to be stagnant between $110 and $120 per metric tonne due to the slowing Chinese economy, Brazil’s stock market might not rise for some time.

Developed nations with an older population such as the US and Germany have a relatively heavier weight of the health-care sector within their stock markets, while younger nations including China and Brazil still have ample room for growth in the future.
GLOBALIZATION AND GLOCALIZATION

With more than 50 books to his credit, Philip Kotler is widely acknowledged as one of the world's top experts on the power of marketing. He was recently interviewed by EMI and offered his thoughts on emerging markets as expressed in his latest book, *Market Your Way to Growth*.

PROFILE

Philip Kotler
Born in Chicago, Kotler is currently a professor of international marketing at Northwestern University in Evanston, Ill. He holds a Ph.D. in economics from MIT. In addition to his books, Kotler has written numerous journal articles and has consulted for companies such as IBM, AT&T, and Bank of America. He has been described as the founder of modern marketing management in *The Handbook of Management Thinking*. 
In your recently published book *Market Your Way to Growth*, you point out a “global redistribution of wealth” as one of the 9 megatrends that will offer new opportunities throughout this decade. You mentioned that economic power seems to keep moving towards emerging markets including emerging Asian countries such as China and India. How is this power shift affecting the market?

Countries in the Far East are growing at a higher rate than countries in the West. In addition, new multinational corporations (MNCs) are emerging from these rapidly developing Far East economies. The stories of these new MNCs are well described in a series of recently published books including *The Emerging Markets Century*, *The New Emerging Market Multinationals*, and *Brand Breakout: How Emerging Market Brands Will Go Global*. Taiwan’s Acer brand and China’s Lenovo brand of computers are doing relatively well in Asian markets compared to standard American computer brands. These emerging multinationals often have lower costs and equal or higher quality and will present formidable competition to the established multinationals.

“Glocalization” seems one of the insightful ideas we can learn from your book, especially for companies searching for growth opportunities amid tough economic circumstances. Does it mean we can find meaningful growth opportunities in the second- and third-tier cities within China or provincial cities in India? Can you describe some cases where a “Localization Strategy” is well applied and achieved successful results in the emerging markets?

“Glocalization” is the strategy of introducing well-known international brands into another country with appropriate local adaptations. McDonald’s is a good example where the company modifies its offerings to fit better local consumption preferences. Thus, many German consumers will order beer rather than Coke, and many Japanese consumers will order sake. As another example, Ikea “glocalizes” its product mix when it enters another country. A Swedish-size bed may be too big for the height of Chinese consumers or the available space in their home.

Whether a MNC should focus its attention on entering a nation’s top cities or the second- and third-tier cities is a separate strategic question. If the MNC realizes that it has come into China’s main cities too late to gain market share, there are plenty of other very large Chinese cities to enter. And these other cities should be entered with a glocalization strategy.

A business will surely be committing suicide if it does not enter the digital age.
approach coming out of careful research into the target audience’s buying behavior and preferences.

Online and related e-commerce market is showing rapid growth across the globe. How will recent development of IT technology or “Information Evolution” change business and marketing strategies among companies?

Online and e-commerce will have a gigantic effect on consumers, retailers, distributors and manufacturers. A business will surely be committing suicide if it does not enter the digital age. This is the age of Information and Communication Technology (ICT). Consider the information available to a client of Salesforce.com. They size up the opportunity for their clients by providing information about when they should make the next call and whether it should be by email, phone, text mail, or snail mail.

Consider the information available to consumer marketers who have access to the purchase profiles and digital streaming of millions of consumers allowing these companies to make personalized offerings to individuals. Everything is changing. Several types of retailers—music stores, book stores—are closing down because so many items can be ordered online without going to a store. A company such as P&G is putting between 25 and 35% of its promotion budget into the new digital media. Companies shunning digital beware!

Based on the megatrends, you suggested “creating a powerful brand” as one main growth strategy. Do you think the brand power of global companies will serve as a continuous growth engine in emerging markets?

Yes, as the upper middle class develops in emerging countries, they will show a preference for global MNC brands. The working class will continue to favor cheaper local brands.

Regarding the strategy of “International Expansion,” emerging countries can be seen as one of the markets where high growth is found. However, worries have arisen regarding increases in production costs in the emerging markets due to the rise of labor costs. Are there any other factors (which are more powerful to offset the cost risks) that we have to consider in order to continue to invest in the emerging markets?

Rising labor costs is a short-run curse and a long-run benefit. A company always has the option of moving its business to centers of lower cost. Africa will eventually get its growth by having the lowest production costs in the world. But businesses facing higher labor costs should be more patient.

First, they can adopt more modern equipment to increase factory productivity so that labor cost is a smaller percentage of total factory cost. Second, the higher wages, if not accompanied by inflation, will put more money into the hands of the working class and therefore lead to more consumer purchasing. As one consumerivist put it, “We have to pay people a living wage so that they can afford to buy enough to keep business in business.”

In the same context, China, where the government is implementing policies to strengthen the middle-income class, can be seen as a representative market with growth potential. If so, specifically, which industry or business do you think will experience higher growth?

The Great Recession starting in 2008 led China to realize that it had become overdependent on exports to fund its economic growth. When China’s GDP (gross domestic product) started to slip, China’s leaders realized that they must do a better job of creating home-based growth. After all, China has over 1 billion consumers. China realized that too much of its economic activity took place along its Pacific coast and in huge congested cities.

China is now developing new cities in the heartland that will keep many Chinese from moving into the crowded East Coast cities of China. Jobs will grow where the people live. As the people in China’s hinterland cities increase their income, they will spend it on...
basic products increasingly being manufactured in China by Chinese companies as well as foreign companies.

Focusing on China, Brazil, or some higher growth markets is one of the key strategies you suggest. As we are witnessing rapid increases in incomes within these countries, we can also expect corresponding growth in their consumption markets. What are the consumption characteristics of emerging markets? To build market share and achieve higher growth in these emerging markets, where does the marketing strategy of global consumer goods companies have to focus?

Companies need to be careful in analyzing the effect of high growth on consumer attitudes and behavior. A country’s economic growth is measured by GDP. High growth doesn’t mean that all the sectors are growing strong. Much depends on who has benefitted from the high growth. If the upper class and the rich benefitted the most, then retailers catering to those classes would benefit the most. It is even conceivable that the working class remains reluctant to spend very much if it doesn’t share in the income growth. My main point is that each manufacturer and retailer operating in these high-growth countries must carefully analyze the differential impact of the high growth on the different consumer classes.

The importance of brand power in terms of international expansion is highlighted several times within the book. What are the features of MNC brands that are becoming more popular in the emerging markets?

Multinational brands such as Starbucks, WalMart, BMW, Nike, Facebook, Dunkin Donuts, McDonald’s and Kentucky Fried Chicken, are well-established around the world. Their role is to give consumers confidence in their quality. This doesn’t mean that they take over the whole market in their category. Those multinational brands are higher in price. For example, McDonald’s is number 2, not number 1 in the Philippines because Jolly-Bee is number one, being less expensive and more flavored to the local tastes. Much depends on which consumer class a company is aiming. The rising middle class in China and in India are showing a preference for world-class brands. The poor are staying with low-priced local brands. Each company needs to define its target market and saturate its audience with a strong value proposition as to why it offers the best value for its given price.
MICRO FIRMS ROCK CHINESE FILM INDUSTRY

1. OVERVIEW
   WHAT SECRETS LIE BEHIND THAT MOVIE TICKET?

2. ADVERTISING
   PPL TAKES ITS PLACE IN FILM

3. MARKETING
   BAD ENOUGH TO BE SUCCESSFUL

4. SPECIAL EFFECT
   MAKEUP ARTISTS FOR MOVIES
In 2012, the film industry in China generated more than $272 million at the box office, replacing Japan, to make China the world’s second largest movie market. The wide range of participants in the industry, the number of stakeholders and the level of integration and innovation have far exceeded moviegoers’ imagination.

Liang Wei, founder of the movie marketing company Magilm Pictures, dresses like a typical IT professional and has a huge LCD screen and two Apple computers in his office. He claimed the company was an “Internet company” and firmly denied that he has “things to do with the industry.” He said this in order to set himself apart from those “old-fashioned and conservative industry people in their 50s and 60s.”

Recently, he told those so-called “big-shot” directors, “Don’t consider yourselves as experienced any more. Do you know that the average age of moviegoers is 22? It means your kids go to the cinema after school with their school bags. Do you understand the 90s generation?” The age structure of the audiences has been changing greatly. Experience is not that effective on the “Internet generation,” giving movie-marketing companies great opportunities to fill the void.

Back in 2009, when Magilm Pictures was founded, Liang Wei discovered that there were only one or two movies with a full marketing budget of over $1.6 million, but today there are dozens of them. The companies in this industry have also gone
through their “barbaric growth” phase; entering the “warlords era,” where each company has its own strength and focus.

Movie marketing is undergoing market segmentation and seeing the emergence of various subcontractors, such as promotion companies focusing on publicity for films, film placement companies focusing on finding the proper brand advertising channels, and companies that are hybrids of the two. These two types of marketing companies have one thing in common, which is that they are both resorting to new media to transform the relationship between movies and moviegoers, expanding the commercial potential.

“Tremble, movie industry, the time when the young generation will overthrow you has come.” Kodak announced this when it launched its 8mm film after World War II. Later, in the 1970s, Sony adopted a similar promotional approach when it unveiled its home-use VCR. Today, these ambitious challengers of movies have crashed, but the era of subversion they aspired to has arrived.

Newcomers are bringing a new gameplay. The Internet and big data are subverting the traditional movie industry, new marketing methods are on the rise, and a new fan-based economy and “subculture” are taking shape. All the traditional rules are being infiltrated by new forces, and traditional movie professionals who see movies as their “handiwork” are suffering a violent mental breakdown.

While the movie industry is rapidly maturing and growing, we are losing the humanistic values, ideas and artistic quality of its work. The “art” attributes of the movie continue to be weakened, yet its “commodity” characteristics have been strengthened to historic heights. Movies are facing an era of comprehensive industrialization.

Experience is not that effective on the “Internet generation,” giving movie-marketing companies great opportunities to fill the void.

Over the years, the first peak wave of domestic films has come to an end, but the monopoly of production, distribution and screens is basically stable. The most important change is that the soaring box office has pushed the gold-diggers in the industry to start a new round of ventures. These gold-diggers pay more attention to marketing, Internet use and big data; firms with fewer assets like public relations companies, advertising agencies, law firms and IT companies have become the new representatives of the industry.

The “Small” Times of the Film Industry Are Coming

These seemingly small-scale companies, mostly founded by the 80s generation, are driving the movie industry to undergo a profound fragmentation. When movies like Lost in Thailand, So Young, and Finding Mr. Right are taking over the box-office records in China, these “small” companies are revolutionizing the future of China’s movie industry.

Not only the marketing function but also the entire film production model has changed. “A Hundred Thousand Jokes” is a comic website, consisting of a series of animated “roast” clips, all of which were distributed via the Internet, winning a group of highly loyal fans. The producer of U17 hoped to adapt it into a big screen movie. They raised funds on Demohour, getting more than $32,000 as funding for shooting the movie only 18 days after the project was launched. Among the benefactors were netizens from Hong Kong, Taiwan and overseas. “Once this type of public fundraising model proves to be successful in the movie industry, many small production companies would become eligible for the game, competing with big production companies.” Dong Zhiling, co-founder of U17 believes that this Internet-oriented thinking would bring about the opportunity for change and evolution for the entire industry.

The business of film distribution has also been quickly “captured” by the Internet.
While the movie industry is rapidly maturing and growing, we are losing the humanistic values, ideas and artistic quality of its work.

While the previous generation of moviegoers were used to queuing up at a crowded cinema to get movie tickets, the new generation of moviegoers who value convenience and service have been captured by online ticketing websites and apps. Since Gewara launched its online ticketing service, 20% of Shanghai’s film tickets have been sold through Gewara. Gewara’s online movie ticket sales reached $75.2 million in 2012. Similar websites like mtime.com, wangpiao.cn, and meituan.com together constitute a sizable business for online ticketing. Online ticket sales in 2011 accounted for approximately 6.8% of the overall box office record; in 2012 its market share rose to 16.7%.

Marketing Based on Data

Zhang Xuejing, founder of Gewara, was previously engaged in the map navigation research and development business. When he discovered that movies were the most suitable business for adopting LBS (location-based services), there were hardly any mature companies in that area. Now, in addition to conventional ticketing websites, BAT (Baidu, Alibaba, Tencent) giants are charging into the market. The latest version of Baidu Map has added a ticketing feature. Taobao Movie and QQ Movie Ticket are not to be outdone, turning the online ticketing business into a “red ocean.” Nevertheless, there still seems to be opportunities in this market.

Next, the middle “distribution” link is gradually weakening with the rise of “marketing” in the industrial chain. In the earliest Chinese film market, distribution and marketing were tied together; however, they are not able to retain their leading role in the current round of market competition due to the nature of their monopoly, which had been granted by the system and their status as state-owned enterprises. Instead, the more flexible private companies which are closer to the consumers and have a better understanding of the market have the best entry point into the game.

“Currently, there are Huayi, which started as a production company, Enlight Media Group, which originated as a distribution company, and Wanda, which is known as a screening company. No sizable film company has yet emerged from a marketing company, but there will be one,” DreamWorks Chief Investment Officer Lv Zirui explained.

A lot of venture capitalists (VCs) are closely watching this emerging market. Three companies have already received investments from VCs. “Now they are all gambling. Nobody knows who will successfully grow and expand, but there surely are opportunities.” Lv Zirui went through the names of the companies within the industry, and all of those whose names are recognizable are in close touch with VCs and investment funds.

On the other hand, big data is disintegrating the rigid barriers in the traditional film industry. In the past, filmmakers could predict the market performance of a movie just by their experience and intuition, and the results always turned out to be close. But the fast-changing market today has already led a number of big-name producers to “miss the shot.” Only precision marketing based on data can quickly reap the market.

Before coming back to China last year, Li Zhan had worked for 10 years in an American company specializing in movie data research. He said that Hollywood has a sophisticated set of movie data surveillance tools and systems. Usually, a movie would spend 15% to 20% of its marketing budget on data research. Take a blockbuster with $100 million to $200 million in investment as an example. It would certainly spend millions on data research. “Film is an industry. So the experience-based prediction could be effective in the early stage, but the role of data would be increasingly important in the middle and later stages.”

An American movie would go through four to five rounds of screenings, and select 300 to 500 samples in 20 cities nationwide,
tracking audience viewing behavior and testing audience reactions through questionnaires. If the statistics in the first round of screening are not satisfactory, the movie director will make appropriate changes, or even re-shoot the movie to pass the second round of testing.

If the test results are still below standard after the fourth round of screen testing, that movie would not go to theatrical release but would go straight to DVD or be shown in niche cinemas. In these tests, not only excerpts from the movie, but also the trailer, TV commercials, title, posters and other promotional materials are tested. Fifteen versions of trailers are needed just for the first round of testing, and are gradually narrowed down to three to four versions in the final round.

As opposed to the complex and sophisticated process used by the Hollywood film industry, the “roughness” of the Chinese film industry is beyond Li Zhan’s imagination. There are quite a few directors who completely boycott the ideas of market research or use of data. For a long time, Li Zhan’s extensive experience from the United States was deemed totally inapplicable in China. In the last couple of years, as the movie-marketing function has come to the front, data has become an integral part of the movie marketing system. Almost all the movie marketing companies interviewed claim to be researching with “big data,” either with a data analysis team trained internally, or via outsourcing to external professionals. Entdigital is a “technical” company which came into being under this kind of market demand.

Entdigital, established last year, has already reached cooperation agreements with Huayi, Wanda and Enlight Media Group. This low-key company in the industry is doing something very advanced, i.e. forecasting a movie’s major audience, the number of fans of the main cast, and even the movie’s box office performance. The accuracy of the results is said to be above 90%.

The flooding business demands, the fast-growing Chinese market, combined with the overwhelming number of young people and the fast-developing new industrial chain for film, are leading to rapid changes in every area. In the eyes of many, this is also becoming a “small-time” industry composed of “vulgar” screenwriters, directors, bad taste and fast-ripened businesses.

Since Gewara launched its online ticketing service, 20% of Shanghai’s film tickets have been sold through Gewara.
PPL TAKES ITS PLACE IN FILMS

The fact that product placement has become an integral part of films signifies movies’ maturity as a commodity, attracting lots of gold-diggers.

By Zou Ling

Wang Yifei and his Herun Media is a pioneer that introduced Hollywood style PPL to China.
In China, movie marketing is beginning to diversify as the entire industrial chain matures.

"Let me finish the Shuhua milk before talking to you." When an Asian actor with a funny facial expression said that line, most of the audience laughed. This is one scene from Transformer 3. Of course, the cost was quite high—Yili paid nearly $1.6 million for this short line. Judging from the unprecedented attention it attracted afterwards, the deal was worth it.

Compared to traditional television and print advertisements, in-movie advertisements have become an increasingly cost-effective advertisement channel, and companies specializing in in-movie product placement have become a prominent part of the ever-stretching value chain of the movie industry.

In 2013, China's product placement market is expected to reach approximately $160 million—less than 1/15 the size of the American market six years ago. In 2006, the product placement market in the U.S. reached $3.3 billion. However, with the surging box office performance in China, gold-diggers in this field have started making moves. On Aug. 8, 2013, U-RIGHT MEDIA was listed on China's new tertiary board, making it the first placement marketing company in the stock market.

The Era of Entertainment Marketing

"In China, the era of entertainment marketing has just been unveiled," said Wang Yifei, general manager of Beijing Herun Media Ltd. Herun Media, a company dedicated to brand content marketing, successfully created the cooperation seen between Zoomlion Heavy Industry and Iron Man 3. The company also provided marketing services for a few Hollywood blockbusters, including The Avengers, Pacific Rim, and The Smurfs 2. Its 2012 revenue was over $16 million. In 2013, Wang completed some product placement deals with three or four Hollywood blockbusters. According to Wang, the blockbuster count next year will be up to 10, while for domestic movies the count of product placements will be 20. The company's revenue in 2014 should see a 100% increase compared to 2013.

In Hollywood, advertisement placement is usually inseparable from "bundled marketing." Bundled marketing refers to a campaign where the sponsoring brand creates product advertisements with movie elements. Take the cooperation between Zoomlion and Iron Man 3 as an example; besides the product placement in the movie, Zoomlion can use trailers and posters authorized by Iron Man 3 for its trade shows around the world because Zoomlion is the global exclusive partner of Iron Man 3; it can also create cinema advertisements out of movie elements and screen them in cinemas all around the world.

The fact that product placement has become an integral part of China's movie industry signifies the maturity of movies as a commodity in China. In Hollywood, 20% of movie revenue comes from the box office, while other revenues account for 80%, of which 20% comes from placement and bundled marketing. In China, the situation is reversed. Box office revenue accounts for 90%, while other revenues only account for 10%. According to Wang Yifei, Hollywood's movie industrial chain focuses on "post-movie marketing," with various revenue sources including joint publicity, copyright and derivative products, in addition to box office revenues. In China, movie marketing is beginning to diversify as the entire industrial chain matures.

As the first "well-digger" for placement marketing, Herun Media got involved in in-movie product placement just two years ago. Before that, Herun mainly acted as an agent for product placements in television series. Its first placement was for Kappa apparel in Who Takes Charge of My Youth. Kappa only provided costumes at that time and did not pay a sponsor fee. Now, product placement on television series has a comprehensive pricing system. Each television series consists of dozens of episodes, and generally, a television network would buy up the series before broadcasting. The business is B2B, so it is easy to estimate the ratings data for client's reference. Movies, on the other hand, are different. They are directly marketed to consumers, so it is hard to predict the box office before a movie's release. Even a seemingly great movie has every possibility of failing badly. In recent years, with the increasing number of large screens, many clients are demanding product placements in movies. What Herun does is help brands select movies that match their target customers; support the product's positioning, and have a release date that falls in the main promotional period of the brand.

A well-rounded brand placement process often starts at the script-writing stage. The placement agency will review all the props listed in the script or possible objects that could appear in the movie. For instance, in 007: Skyfall, audiences saw the stylish Bond with fine taste drinking Heineken beer. This cost Heineken as much as $60 million. Herun was asked by the producer of Small Times to be its agent for all product placements in the movie. Wang Yifei, however, found it "unfeasible" after reading the novel, since the glitz and materialism rendered in Small Times were molded through intensive appearances of luxury branded products. But international luxury brands would not invest in Chinese domestic films, while Chinese brands could not live up to the atmosphere or style that the movie is trying to create. In the end, Herun gave up on that movie. In Wang Yifei's opinion, the ideal situation is to get involved as early as the script-writing stage. If one starts contacting brands after the movie is finished, it leaves very limited options for the brand. In order to ensure that the brand will have a say in placements, Herun would even get...
While advertising conventionally on television is experiencing a downward trend, in-movie placement is quietly taking away advertisers’ budgets.

involved in early-stage investments as a good-faith deposit to “buy out” a say.

The second step is to carry out precise segmentation of a movie’s target audience, such as the “audience from third- or fourth-tier cities aged under 18,” or the “adult female audience from first-tier cities.” After the movie’s release schedule and cast are determined, the agency provides the brand with a comprehensive analysis report, taking into account multi-dimensional data related to the movie and coming up with an estimated audience number for its premiere. These data are crucial for the client, because they will directly affect the pricing for placement.

Ogilvy & Mather’s marketing director Ma Xiao Zhen said that in the advertising industry, clients attach great importance to data. For many, it’s “no data, no advertisement,” even given the unpredictable outcomes for movies. Ogilvy & Mather has developed a special Ogilvy brand entertainment assessment model (Ogilvy BEAM™). The abundance of advertisement channels has prompted Chinese advertisers to value advertising precision, and the application of data will become more and more common in this kind of agency.

Take the director Teng Huatao and his 2013 film *Up in the Wind,* for instance; “This is a simple and fresh movie, appealing to brands targeting urban and white-collar females,” suggested Wang Yifei. After identifying the type of brands, one also has to analyze Teng Huatao’s box-office performance history, the microblogging and social media audience for the principal actor and actress, and the demographical structure of their target audience, among other things, to arrive at weighted advertising effective-ness indicators for the brand.

The third and most critical step is to settle the placement plan with the producers. Wang Yifei now prefers to call it “brand content marketing,” rather than “product placement,” given that the better the movie is, the more subtle the “placement” has to be. Starting from *Tangshan Earthquake,* Wang has cooperated with director Feng Xiaogang in three of Feng’s movies, including *You Are the One 2* and *Personal Tailor.* He views Feng Xiaogang as definitely the “master” of product placement and the most skillful director in terms of “seamless integration” of content and brand.

Feng Xiaogang’s creative ideas to integrate brands into movies were manifested through the frequent appearance of the brand Zoomlion in the rescue scenes in *Tangshan Earthquake,* and the use of a DOOV phone by actress Shu Qi in *You Are the One 2.*

“Starting with Feng Xiaogang, Chinese movies have had a diversified revenue model that is not entirely dependent on box-office performance.” Wang Yifei revealed that, for *Personal Tailor,* which premiered in Beijing Dec. 17, revenue from these placements has basically helped recover most of the movie’s production costs.

Risky Business

But not all directors are as cooperative as Feng Xiaogang. The greatest uncertainty in a placement project lies in who the director is and in the movie’s release schedule. It is not uncommon that the deal eventually falls apart due to the director’s disagreement with the placement plan, even after the producer and the brand have already signed the agreement. The release schedule is also one of the biggest risks for in-movie placement. A movie is usually released one year after the shooting begins. If the director fails to wind up the film shooting within a certain period of time, or the brand cannot launch the product upon the movie’s release, both parties would be in great trouble.

For example, though the box office revenue of *Switch* was over $48 million, Herun took a loss as a result of paying for a default in the advertising placement contract; this was caused by a production delay of almost one year by the director. In view of this situation, the safest approach for advertising is to conduct branding, rather than pursuing any product, placements.

As for the fees for product placements, costs vary over a very wide range for different projects, from free of charge to tens of millions of dollars. One of the most expensive product placements recorded was for...
$50 million for the 007 series paid by Aston Martin, an automobile brand. Wang Yifei’s advice for clients in selecting a target movie is to avoid any film whose expected box office performance is less than $160 million. “Box office performance of less than [that] will bring hardly any value for product placement in the movie, because the audience size will be limited,” explained Wang. In contrast, when the production cost of a film becomes too high, say, above $32 million, the producers would accordingly attach more requirements and high expectations to the placement. A mere several hundred thousand dollars’ worth of placement creates no interest. It is in such a situation that there is an opportunity to discover a balance to reap the best value of spending. Proper marketing and placement in a movie would help achieve much better results than would traditional advertising channels.

Compared to the advertising investment in television broadcasts which could easily ask tens of millions of dollars, in-movie placement is still an underpriced practice. Insiders revealed that the price range for a product placement is usually around $160,000. For consumer products targeting young people, brands can advertise in cinemas by bundle-marketing with promotional posters in addition to in-movie placement. This strategy appeals to brands. Therefore, while advertising conventionally on television is experiencing a downward trend, in-movie placement is quietly taking away advertisers’ budgets.

**Between Brand and Movie**

Understandably, audiences’ strong dislike for “watching movies between commercials” is growing rapidly alongside the development of the industry. Director Feng Xiaogang had over 20 product placements in You Are the One 2, setting a record for product placements in domestic films but also inviting great controversy and criticism. Ma Xiaozhen said that more and more clients have started to realize the need for sophisticated skills in placing brands in movies and their ability to control the content. Compared to big-screen movies, “micro films” that are purely custom-made for brands are preferred for specific market communication. Last year, Ogilvy helped Nestle to produce a micro film Coffee Journey, visualizing Han Han’s travels in Europe, which received a lot of hits on Youku. Free video communications like this are more acceptable for audiences and clients.

“We are always the third party between the brand and the movie, a B2B industry,” Wang Yifei said, adding that, currently Herun has over 100 brand clients and the resources of all the top movie companies in China. It has become a large-platform provider. But the bottleneck lies in the fact that this is a sales-driven industry. All the essential resources are controlled by producers upstream and cinemas downstream, allowing limited room for growth.

Another major constraint lies in the difficulty of quantifying and testing the effect of product placements. The correlation between investment in product placements and good sales performance for a placed product cannot be measured. But risks like this do not stop savvy advertisers from investing their limited budgets into movies as a channel. With the decline of conventional media, a lower HUT (homes using TV) rate and an aging television audience, the mainstream social activity of young people is still going into crowded cinemas to enjoy a movie, which might be viewed as a type of prolonged commercial. After all, what cheaper entertainment can one find in China today?
Traditional film production, marketing, and distribution value chains are changing. Movie-marketing companies adopting Internet use are now in the driver’s seat, influencing box-office performance for even inferior movies.

By Zou Lin

Just two months before the release of *Switch*, Zhu Weijie watched the roundly criticized 2013 blockbuster. He is the general manager of the marketing agency Wishart Communication Co., Ltd., which was responsible for the promotion and sales of the movie.

He was extremely disappointed after watching the movie and predicted the expected box-office performance would be under $10 million. However, when he met the movie’s hopeful director, his promise belied his thought: “I will try to make a record of more than $20 million or $30 million.” In the end, however, the result was a shocking $49 million worth of ticket sales.

“Sometimes, marketing can change the fate of a movie,” Zhu said. Born in early 1980s, Zhu Weijie is a typical representative of this emerging industry—young (usually born in the 1980s), having a media background, patronizing movie release conferences, and resourceful in the media and entertainment fields. Players in the industry also include In Entertainment, the marketing agency for *Love Is Not Blind*, and Max Times, the agency which made *So Young* a hit. Along with the rise of small- and medium-budget movies which reaped success through marketing, these “unsung heroes” behind the scenes are emerging.

Insiders revealed that two movie-mar-
marketing companies, Wishart and Magilm Pictures, have already secured millions of dollars in investments from their Round A Financing. Lv Zirui, investment director of Media DreamWorks, a subsidiary of Zhejiang Daily Media Group, said that movie marketing may well be the next important focus of venture capital investment. It is also currently an opportunity for easy involvement by investment capital.

The Movie Alchemist
How important a role is marketing playing in the whole industrial chain? According to statistics by EntGroup, the total spending by Chinese movie companies on marketing in 2012 reached $384 million, a 20% growth year-on-year, and this number is expected to hit $454 million this year. There is still, however, huge room for growth compared to that in Hollywood, where a movie’s marketing budget usually accounts for 10% to 20% of the production cost.

Just a few years ago, the concept of “movie marketing” was not even heard of in China; thus any budget for marketing these days would not exceed 5% of the production cost. This means that compared to the mature and sophisticated system for promotion and marketing in Hollywood, Chinese movie marketing is actually a blue ocean industry.

It is against this background that Zhu Weijie successfully carried out the marketing of Switch. Controversy over this case has been endless, and people are asking whether “marketing for inferior movies,” a way of maximizing the movie’s shortcomings, would eventually bring down China’s fledgling film industry. Zhu, however, argues that he is faithfully playing an indispensable role in the movie industry chain.

After taking over the promotion and marketing project for Switch, Zhu first analyzed some historical data. He discovered that Future X-Cops, another film starring the same lead actor, Andy Lau, only recorded $9.6 million at the box office. “Future X-Cops at least had a decent screenplay. How could you sell more than $9.6 million for Switch at the box office?” To “reverse” the likely dismal box-office performance, Zhu took the following three actions.

The first was to change the positioning by repackaging Switch from “super cool sensational and fascinating blockbuster” to a “Chinese version of Mission Impossible or a secret agent film like the 007 series.” Andy Lau is the Chinese version of Tom Cruise while Chiling Lin is the Chinese version of
the Bond girl. This is just simplifying and reinforcing some concepts.”

The second step was to penetrate distribution channels. Before the release of Switch, Zhu collected a lot of data by sitting through microblogs and the Baidu Index, along with an analysis of movie star influence level. He came to the conclusion that the focus of the marketing for the movie should be downward toward the second- or third-tier cities.

“When we found that the movie’s reputation plunged sharply in first-tier cities, we basically gave up on those cities,” Lead actor Andy Lau did not even have a roadshow in Guangzhou, but instead went to Chengdu. Zhu geared all the publicity strategy toward second- and third-tier cities, because audiences there are not influenced by social media outlets Weibo, Mtime or Douban. Once local newspapers report that one particular film features particular stars and a good cast, the film should have a smooth entry into theaters. Statistics on the movie’s performance proved Zhu’s “penetrating downward” strategy to be successful. The sharp drop in box office performance in the first-tier cities was steadily offset by the gain in the second- and third-tier cities.

The third and most important step was the so-called “marketing on the negativity.” After watching the movie, Zhu understood that “word-of-mouth recommendations” just would not work for this movie. When Switch premiered, Zhu was sitting in his office earnestly scanning the microblog site Weibo, which steadily worsened his mood. “There was an avalanche of bad reviews online.” But, thanks to the screening by 48% of cinephiles scanning the microblog site Weibo, Zhu soon found this strategy was effective. In the next few days when Switch was showing, there were hundreds of thousands of critics online using similar “sarcastic style.” Other than the critics that Zhu had published for marketing purposes, the rest of the posts were all spontaneous “satires” by other netizens. The phenomenon of “sarcastic Switch” soon became a “hot topic” on Weibo. Zhu’s marketing of the negativity became the major contributor for the over $32 million box-office record for Switch during the first four days of the movie’s release.

It only took four days for Switch to reach that number at the box office; however, it recorded only an additional $14.4 million in sales over the next week and a half. Looking this over, Zhu believes that the so-called “marketing on the negativity” can only delay the “aging” of a film and that the pre-release marketing strategy was more important.

For instance, before the release of Switch, Zhu Weijie insisted that the movie company should not unveil the entire film to the media, but only a half-hour cut, which helped to guarantee that there were no “bad reviews” by media critics. At the same time, he also pressed for holding numerous press conferences with appearances by stars from the cast. All this ensured the 48% cinema occupancy achieved on the first day. Otherwise, there would not have been hundreds of thousands of negative reviews, making “marketing on the negativity” possible.

But earning this box-office record for an “inferior movie” did not bring much joy of success to Zhu. Instead, he was infused with a sense of guilt, and was in a debate with a colleague on the topic of “whether we are like a quack medicine seller.”

### Internet And Big Data

Building on his fame from the successful marketing for Switch, Zhu was given enough projects to work on till the end of the year. But now he has the same worries as all the other movie marketing companies: Unlike the mature market in Hollywood, the so-called “industrialization” of the Chinese film industry has just taken off and is characterized by disorder and chaos. The most depressing aspect is that the quality of a movie’s script, shooting and production basically dictate the fate of the movie’s release performance. But many investors or producers now count on movie marketing to change the fate of a movie’s box-office performance.

“For movies like Switch, if you spent $130,000 or $160,000 more to acquire a script, the box office might be performing at $48 million higher,” Zhu concluded afterwards. Unfortunately, this is precisely a matter that no movie marketing company has any say in.

From Love Is Not Blind and Lost in Thailand, online promotion has gradually become the “standard procedure” in movie marketing. The threshold requirement for practicing movie marketing has also been lowered alongside the rise in new media marketing. However, this implies there is no quick route to successful movie marketing by relying on eye-catching “publicity stunts” or success stories using social media marketing. In fact, it is fairly easy to enter the field of movie marketing, but rather difficult to grow into a large-scale business.

Zhang Wenbo, who designed the marketing plan for Love Is Not Blind, created the first movie marketing company In Entertainment, but he realized that companies of this nature would always face a bot-
tleneck in expansion and growth. This intrigued him enough to give up his entrepreneurial practice and take up the position of vice president of New Classic Media.

“New media marketing for movies and television spans over six areas, i.e. advertising, public relations, IT, media, film and television, and marketing, which is extremely demanding from the standpoint of having a comprehensive professional capability,” said Liang Wei, who is in charge of Magilm Pictures. “Nowadays,” Liang added, “you have to research big data and algorithms, or else you will soon be obsolete.”

The company just announced that it got tens of millions of investment from Cowin Capital. Liang said that receiving outside investment is a milestone for movie marketing companies. It also signifies that movie marketing companies have arrived at the watershed: Companies backed by such investment capital will quickly move towards professionalism and segmentation, and mergers and consolidation will accelerate within the industry. For many movie-marketing companies, the biggest pressure might be that they are too small in scale to have much revenue or profit. They only occupy one particular spot in the industry chain, and furthermore, replication of others’ success is hardly likely to happen.

Recently, Liang Wei was promoting An Ideal City, adapted from Han Han’s novel of the same name. He made a great effort to turn it a hot topic online and on a Weibo campaign. He even pushed up the Baidu Index to 35,000 points, higher than that for So Young before its release. Unfortunately the movie only made $656,000 at the box office in the first three days of release. Liang Wei, who once was hailed for his successful marketing of Let the Bullets Fly, could not help but feel frustrated by this result. His peer Zhu Weijie explained that the theme of the movie appeals only to a small segment. In addition, Han Han could not promote the movie as hard as another peer, Guo Jingming, did. It seems that standard new media marketing is proving weak in turning around the fate of a movie.

“In the future, companies which have the power to revolutionize the movie industry will be few, definitely those that understand the ins-and-outs of movies and are able to adapt to Internet use, or even those specialized in working with big data. It is all because the “9 generation” of the 90s has grown up with the Internet,” said Liang Wei.
Wang Lei and Wang Xuan, who used to be competitors, became co-founders.

“MAKEUP ARTISTS” FOR MOVIES

Chinese special effects (VFX) companies dream about becoming the Industrial Light & Magic of the Orient. The outsourcing business model is helping Beijing Phenom Films Technology Co., Ltd. (Phenom Films) become more competitive in the VFX market.

By Huang Wenziao
Since the merger was completed in March, Phenom Films has earned over $3.2 million in revenue.

Design may not have the power to alter life completely, but Phenom Films can straight away brighten the colors and effects of the movies directed by Feng Xiaogang. Deep inside the northeast corner of Beijing’s 798 factory/art district, there is a building where director Feng Xiaogang’s film Personal Tailor was in intense post-production earlier this year. Phenom Films is quietly hidden among a handful of art galleries, separated only by a red wall from the big black chimney of the old factory. Several large blue characters written on the corner of the roadside wall read “Design changes life.” The “one-stop for the entire process of post-production” company completed a merger with four other companies in March, 2013. Its predecessor handled most of the blockbusters by the Huayi Brothers.

Phenom Films is better defined, not simply as a VFX company but as an exception in the highly segmented post-production capital chain. It focuses on being an outsourcing company. Currently, there are only a handful of companies that are able to perform the entire process of post-production for movies, and Phenom Films is the biggest.

The company announced its establishment in June at the Shanghai International Film Festival, a result of the merger of four movie post-production companies. The four included Beijing Miracle Film & TV Co. Ltd which specialized in making movie clips and special effects, Eclipse Studio which specialized in VFX, and Lollol Media and Lollol Film & TV which specialized in digital dimming and intermediate film. Since the merger was completed in March, Phenom Films has earned over $3.2 million in revenue, over 60% of which came from the special effects business.

According to a survey by EntGroup, the post-production market in China’s film industry in 2012 amounted to approximately $99 million. Of that figure, $59.5 million was from the special effects business. This revenue was derived mainly from 34 domestic films with medium-sized or above budgets totaling $379 million. For these films, the average spending on post-production was about $2.88 million, 60% going toward special effects.

Dreaming of ILM

2012 was a fruitful year for Phenom Films. Among the Class A movies (the blockbusters), Phenom Films was responsible for 70% of the special effects in Painted Skin II and 90% for Back to 1942. Apart from movies completed overseas, the rest
Phenom Films has won enough Golden Horse Awards and Hong Kong Film Awards for Best Visual Effects to form a row inside a glass cabinet.

of the Class A domestic film special effects production was almost all shared between Phenom Films and CFG Post-Production Base.

This company situated deep in the 798 complex is performing artistic work in a precise way. Phenom Films has won enough Golden Horse Awards and Hong Kong Film Awards for Best Visual Effects to form a row inside a glass cabinet. Films like The Message, Detective Dee and The Mystery of the Phantom Flame, The Flying Swords of Dragon Gate, and Back to 1942 are some of the success stories. These technical awards may not be familiar to the general public. So, what kind of movies can win awards for Best Visual Effects? If the standards used by the Oscars for its Best Visual Effects Award are worth referencing, outside a glass cabinet. Films like 2012 and then visit the website of Industrial Light & Magic. Due to the number of high level of preserved artistry, skill and fidelity of a film, enough to deliver to viewers the illusion of not being able to see the difference between the genuine and the false. If this is still too abstract, one can watch the American action/adventure movie 2012 and then visit the website of Industrial Light & Magic, Hollywood’s top VFX company, which claims to set the standard for visual effects around the world.

It seems that Phenom Films is heading toward becoming the Chinese version of Industrial Light & Magic. Due to the number of scenes and their difficulty, there is no fixed pricing mechanism in China or Hollywood for special effects production. "The level of difficulty for making water and fire is surely different from making a cup," said Wang Xuan, deputy general manager of Phenom Films. Take Painted Skin II as an example; the budget for its post-production was around $1.92 million, out of which Phenom Films took nearly $1.44 million, for VFX, toning, dimming and editing. The $1.92 million budget did not even cover the cost of converting 2D to 3D, which added $1.28 million to $1.6 million to the budget.

"In the best year of Chinese movies with huge production costs, the release of five or six Class A movies can be defined as a bountiful year. There are fewer than 15 movie directors in China who can manage directing Class A movies." Wang Xuan went through a roster of directors dedicated to the Class A movie market who have cooperated with Phenom Films. And this company can provide outsourced post-production services to two to three Class A movies a year. Though 2013 was a poor year for film industry production, Phenom Films was able to complete eight Class B movies.

What is the gap between Chinese VFX companies and Industrial Light & Magic, the originator of Hollywood’s VFX industry? Wang Lei, Phenom Films’ deputy general manager in charge of technical production, frowned and pondered question this for a while before answering: time and experience. "In the VFX field, experience brings a great advantage. The development of this industry depends on the number of projects and the expansion of teams," explained Wang. "Movies are very complicated. Say, if you ask whether we can produce for 2012. The answer is yes and no. If we were given two years for producing 2012, we might well be able to produce. But if the production cycle is only a year, we really can’t. This industry is a complex consisting of talent, equipment, time and money."

No Set Rules

There are no set rules in VFX, while editing has many rules. In Phenom Films’ film editing team, Xiao Yang is an undisputable Class A editor. He has handled quite a few movies by director Feng Xiaogang. Other editors are Tu Yiran for Design of Death, Yang Hongyu for Expert Detective Heng Te Zhang; Tian lei for American Dreams in China and Zhangjia for Go LaLa Go. The price for film editing is basically clearly defined. Wang Xuan said that the market price for a Class A editor is $96,000 to $112,000 per film; $48,000 to $80,000 per film for a Class B editor, and $16,000 to $48,000 for a Class C editor. Of course, it is very likely that a movie’s editing is done cooperatively by several editors. The final editing fee for a film can easily be calculated according to the categories of editors assigned to the job.

VFX can be perceived by the audience through the “dazzling stunts,” and editing can be felt by the audience through the fluent flow of a movie. Dimming and toning, on the other hand, is a totally invisible post-production craft. Phenom Films accounts for 25% to 35% of the toning market. Wang Xuan said that Phenom Films performed toning for 45 out of over 200 movies released in 2012, including 3D movies like Painted Skin II and The Flying Swords of Dragon Gate. In this segmented market unseen by the general audience. Wang Xuan revealed that Phenom Films competitor Post Production Office Limited, owned by actor Nicholas Tse from Hong Kong, also...
recorded a productive year, taking 15% to 25% of the market.

The strategy of outsourcing services rather than working on segmented parts has shown its beneficial effects. Wang Xuan said that, though the trend of the international movie industry is toward greater segmentation, the Chinese prefer "full line work," letting one company handle the entire post-production. Phenom Films’ plan is to be a "large and versatile" company in the movie post-production business. After the merger, Wang Xuan compared Phenom Films to a gymnastics team. As a team, it has no equal rival in China, and its competition competes only in the “individual events.” As a “one line work” company, Phenom Films took care of all the movies directed by Feng Xiaogang since his work Tangshan Earthquake in 2008.

Will Phenom Films end up being "large but mediocre" if it gets stuck in every segmented market? Chang Hongsong, Wang Lei, Wang Xuan, and Pei Jialiang, who came in to take charge of the financial department, investing and financing, have teamed up to form the management team of Phenom Films. General Manager Chang Hongsong is the eldest, born in 1980. Wang Xuan smiled and replied that this “foursome marriage” originated from working on Painted Skin II, though it is not a forced matrimony. Though they recently “united,” the four have known each other for a long time. Wang Lei and Wang Xuan used to work for two companies that were direct competitors.

The all-1980s-generation management team is in charge of a multinational working force.

The all-1980s-generation management team is in charge of a multinational working force—there are Koreans in its toning team and Canadians on the VFX team, while undoubtedly most of the team members are Chinese, which is Phenom Films’ advantage, since the locals understand the local market the best.

"After all, we have a better understanding of clients’ needs in the domestic market, with no exaggeration and no downplaying. The most expensive domestic films are just $30 million in budget, which is considered as low- to medium-scale in the United States. How to wisely use this $30 million budget, how to collaborate well with other parts of production within your capacity, these are the things we are working on," said Wang Lei.
THE MOBILE BANKING TURF

Banks, telcos and tech companies are vying with each other to grab the lion’s share of the nascent m-banking space in India

By Raghu Mohan & Vishal Krishna
Illustrations by Dinesh Banduni

BANKS:
See m-banking as a cheaper means for transactions and linking up with customers

GADGET, APP MAKERS:
M-banking offers a brand new area with huge business potential

TELCOS:
See more revenue. Helps them evolve from being mere voice service providers
In January 2009, Barclays Plc did something that would soon become part of banking folklore. The UK bank decided to pair its OnePulse credit card, which also carries Transport of London’s Oyster ticket, with mobile phones sporting near-field communication (NFC) facilities. That essentially meant customers could do a three-in-one job with the plastic: access credit card facilities, travel on e-tickets, and tap to pay. OnePulse heralded the coming of age of mobile banking, or m-banking, globally.

Six months earlier, in July 2008, online startup Wonga had given m-banking a new dimension by introducing a loan app on the iPhone. In 15 minutes flat, the app would get a short-term loan of up to £1,000 credited to your account. Around the same time, in far-away Kenya, Vodafone-backed mobile operator Safaricom was experimenting with m-pesa, a money transfer and micro-financing service that works on mobile phones.

Cut to India—and the story is starkly different. The country has about 880 million mobile users—more than the 600 million lying outside the ambit of banks that vend through over 100,000 branches. But almost half of those without a bank account own a mobile phone, and m-banking is a cheap way to wire them all up: It costs banks just 2% of what they spend on branches and about 10% of the cost of automated teller machines (ATMs). You also get to use by tablet-sluggers, smartphonies, and GenYers (who consider it a stone-age practice to drop by at a branch).

Let’s look at the math. A semi-urban or rural branch costs from $64,000 to $73,000 per annum. It can be as high as $320,000 (for 2,000 sq. ft.) in a city; an ATM costs $4,800 to $5,200 a unit plus rental—ranging from around $19,000 a year (100 sq. ft) in a mall to just over $5,000 a year in Kakinada, Andhra Pradesh. A branch transaction costs anywhere between 80 cents and $1.05; in an ATM, about 32 cents. What is common is

**As of now, m-banking is expensive to the consumer, profitable to the hawker.**

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**Indian Banking**

As of now, m-banking is expensive to the consumer, profitable to the hawker.
the tech backbone—no matter what system a bank uses to service branches or alternative channels—and that variable costs such as staffing, power, rentals and marketing cannot duck inflation.

The Boston Consulting Group projects that fees from m-banking will exceed $4.5 billion by 2015. Another study by industry body Assocham and consultancy Deloitte predicted that annual m-wallet and retail transactions will hit $410 billion; that’s a potential pool of $8 billion—of which $5 billion will be in direct fees (when someone uses a mobile to make a purchase or person-to-person payment) and $3 billion in indirect fees (usage of voice, network and other services over the mobile).

A larger game plan is still under the radar: a unified payment architecture to hook up banks, telcos, business correspondents, the postal department, credit cards, ATMs, point-of-sale units, and the Internet. Further, you have the National Payments Corporation of India (NPCI), with all retail payment systems under its canopy. A series of legislations and reports also cover the field: the Information Technology Act (2008); the draft framework for mobile governance; the report of the inter-ministerial group on a framework for delivery of banking services via mobiles with linkage to Aadhaar; along with a triad of policies to drive a national agenda for ICTE (information and communications, technology and electronics).

Even the new Reserve Bank of India (RBI) governor, Raghuram Rajan, wants to tap the mobile. “We will set up a technical committee to examine the feasibility of encrypted SMS-based funds transfer using an application to run on any type of handset, get banks and mobile companies to cooperate…,” he told the media after taking charge. “It can be a game changer both in the financial sector as well as for mobile companies.”

A little less than 1% of bank customers now use m-banking. The RBI said over 53 million use m-banking in India; volumes are $960 million. It does not mean there is no money to be made or already being made.

### THE BANK BOUQUET

Mobile banking in India is largely limited to providing the following services on customers’ smartphones:

#### Interactive Voice Response (IVR)
Customer calls a number to hear a stored message followed by menu options. It’s largely to make inquiries, and costly as it involves a voice call.

#### SMS
Send an SMS in a prescribed format to a pre-specified number to know about balance, check status and check book requests, and transaction history; or fund transfers, bill payments and share trading.

#### Wireless Access Protocol (WAP)
You hook into the WAP site run by the bank from the phone just like Web users access a portal and access several services of the bank.

#### Standard Mobile Applications
Download the app to the cellphone and access bank services. A key weakness: Each OS has its own set of customizations.
For instance, you pay Vodafone’s m-pesa $1.28 per $80 for the m-wallet; $2.90 to remit to a bank account. The cost at 1.6% and 3.6% of the transaction works out to be much higher than at a branch or an ATM. As of now, m-banking is expensive to the consumer, profitable to the hawker. And just how the pie is carved out between the bank, telco and the distributor is a puzzle.

Nitin Chugh, head of digital banking at HDFC Bank, said that 2% of his customers transact by mobile, but he expects it to equal net banking transactions in four years. “It is just like the Web... it needs time to evolve.” Srinivas Nidugondi, head of mobile financial solutions at mobile solutions firm Mahindra Comviva said, “There is growing evidence that those who use m-banking do not use Internet banking.”

Whose Call Is It?
“You have a sharp divide between what an iPhone and Android wallet with an e-wad of cards can do in a mall and what basic phones with prepaid or no cards at all can offer to the less affluent parts of the world,” said Arindam Mukherjee, manager of regional sales (BFSI) at Cisco (India & Saarc). Added Ritika Basu, director of program management at digital agency SapientNitro: “The tech-savvy urban dweller would look for functionality beyond simple remittances. The unbanked will look for ease of transacting over simpler ways (like SMS).” You can’t be all things to all comers and still have the luxury of a gated residency.

On that note, it’s easy to fathom why Munish Dayal, partner, Barings Private Equity, said he has been told that “m-banking will be the next big wave for the past 15 years. But I am yet to see a good model to put money on it.” Or when Piyush Singh, managing director of Accenture’s financial services, quips: “When bank CEOs say they don’t want to be the first-mover in m-banking, well, there’s no such thing. You have to be in it or you will be finished.” If nobody’s got it right, blame it on the blurred lines. M-banking is a partnership exercise of sorts. For a Google Wallet, for instance,
Citibank provided the cards, MasterCard the network, First Data processed, Sprint offered the mobile network, and Google gave handsets. "It was a partnership of equals, though some were more equal than others with Google seeking to own the customer’s information and, so, the relationship," explained Mukherjee.

In m-banking, you don’t have to “own” a product, bankers will tell you. It’s evident when they sell for a third-party—it’s the customer relationship that matters. But who "owns" the customer? "Nobody owns as such. It’s a bouquet of partnerships," said Suresh Sethi, head, m-pesa at Vodafone (India). HDFC Bank’s Chugh is categorical: "It is the bank for the banking relationship; the telco for the mobile connection." Shrihari Bhat, managing director of FIS Asia PSG, added, "The answer could be different for different countries." For K.V.S. Manian, group head of consumer banking at Kotak Mahindra Bank, "All of this is true in a given context.”

According to the RBI, to the extent that m-banking customers have recourse to the Banking Ombudsman, the matter may appear to be settled. Not really. Assume a telco and a bank decide to terminate a relationship, what is the former to tell the customers? Said Pradeep Sampath, COO-MMPL, an arm of Tata Teleservices, "It depends on the engagement with the bank and how this is defined between partners. There is no readily available definition for this.”

In India, m-banking follows a bank-led model; the telco relays the service to the customer. When Axis Bank said it’s allied with Airtel Money, it’s an extension of a channel. You visit Airtel Money-Axis Bank outlets to open an Airtel Money Super Account, a no-frills account to deposit cash or withdraw from the outlets and remit funds to other users. But m-wallets work only on a given telco’s network, inter-operability is a no-no.

"If the closed m-wallet is made open, it can give it a leg up," said Accenture’s Singh. "You have to link it to the larger payment ecosystem, retailers and across telcos to get volumes. Or you will have islands," said Jose Thattil, head of sales and marketing, ElectraCard Services, an e-payment solutions company. "One way is to link it to a physical plastic so that you can access a larger base of merchants and pay for more
“With smartphones, banks can’t ignore apps as a means of financial inclusion.”

goods and services,” added Vikas Verma, head, MasterCard (South Asia).

An aside: You can’t help but contrast it with number portability. It’s unlike the telco-driven model where you go to an outlet, pay cash and get e-credits stored on the mobile.

You can use it anyway you want or swap it for cash (at the outlet) or “cash out” as it’s known. That’s how it works with m-pesa or G-Cash of Global Telecom in the Philippines. But the runaway success of m-banking in Kenya has led to it being seen as coterminal with or being confused with the telco-led model. The jury is out on what works best—bank or telco-led models or a mishmash of the two. But already there are a series of concerns.

**Identity Crisis?**

“Banks worry telcos want to be banks; telcos worry banks want to become telcos,” said Mukherjee. “Neither is right.” He explained that the RBI does not have enough regulatory authority over mobile payment firms. “Entry into the banking space has to be on open, transparent and contestable criteria. It may not be prudent to allow mobile operators privileged access to banking through the mobile route,” former RBI governor Duvvuri Subbarao noted.

Telcos argue that the m-banking license is given by the RBI, not telecom watchdog Telecom Regulatory Authority of India and that they have no interest in becoming banks. The m-wallet is funded by cash or by a credit card, and as in prepaid plastic, funds have to be kept in a bank’s escrow account. “We can’t use it for our treasury business. There’s a misconception that telcos are interested in such floats,” said Sriram Jagannathan, CEO, Airtel MCommerce.

But there is a subplot. “You can cash out at a telco’s outlet [if it is a business correspondent] only [up to] $160,” said Manian of Kotak. It’s his way of saying that e-cash may well be a substitute for cash as we now know of it; you cannot predict how regulations evolve.

In the Philippines, Global Telecom’s G-Cash and G-Xchange can be cashed in or cashed out (technically a deposit function) at its outlets; some companies even use it to
pay salaries and bonuses. It does not offer saving or lending functions as yet. But m-pesa is a virtual bank. “Cash out is capped at $160. Over time, this can go up. To an extent, you are not using a banking channel—and however limited it may be now—banks will have to keep their eyes open. “Who’s seen tomorrow?” said Manian. But the debate appears to be settled at the central bank. RBI deputy governor K.C. Chakrabarty put it eloquently: “Just as you cannot have tele-medicine without a doctor, you cannot have mobile banking without a bank.”

**WHAT TELCOS WANT**
- A business correspondent can be appointed only within a 30-km radius of a bank branch
- This limit needs to be relaxed to meet the objectives of financial inclusion and higher serviceability
- Alternatively, the 30-km radius rule should be extended to 100 km to create meaningful rural penetration
- Currently, as a prepaid wallet issuer, telcos are unable to offer “cash outs.” Enabling low-value cash outs from the wallet will enable telcos to offer an end-to-end proposition to the customer
- Transaction limits on the wallet are $90 per transaction with a monthly limit of $400. The limits should be raised

**WHERE BANKING IS HEADED**
- People are becoming more mobile—and banks are paying for it
- This year, 590 million mobile phone users globally will use their device for banking purposes. In 2017, that number will exceed 1 billion
- Worldwide, banks will spend $118 billion on technology and mobile banking in 2013
- 81 of the top 100 US financial institutions currently offer some form of mobile banking
- 48% of customers would like mobile banking tailored to location and their personal shopping habits
- Younger consumers are more demanding: of the 26-34 age group, 49% will change banks for a better mobile experience
- In 2016, there will be 448 million mobile payment users in a market worth $617 billion
- US mobile commerce sales will reach $86.9 billion by 2016
- By 2017, worldwide purchase volume over mobile devices will reach $1 trillion

Source: The 7th Annual Mobile Banking and Commerce Summit in Miami
“Irrespective of the model, the key is how well products are designed, how much additional value to customers and merchants is being given… .”

Suresh Sethi
Head, m-pesa, Vodafone (India)

“Nobody owns (the customer) as such. It’s a bouquet of partnerships”

-added that banks have to learn about innovation from the likes of Amazon, Flipkart, Google, Twitter, Facebook, Nintendo Wii or a Microsoft Xbox. The question, he said, is: Can banking in India become the ultimate customer experience?

That calls for linking m-banking with retailers or malls. “The next stage is digital wallets. The mobile will be the store for payments, identification and loyalty, basically one that will convert the wallet in the back pocket to the front... onto the mobile,” said Nidugondi. You can then not only do “remote” deals like book a movie or a train ticket, but also pay for “proximity transactions” with NFC or a QR code. Even real-time offers can be pushed with the use of location-based services. “The use of geo-fencing (a GPS-aided program that defines geographic boundaries) as a strategy can help banks and retailers push context-aware and segmented offers to consumers. You can enhance consumer stickiness,” he added.

“What you have is something that allows you to access a bank’s portal from the mobile or via an app. It is a cut-paste of what you see on the Web. M-banking is much more than that,” said Accenture’s Singh. He isn’t impressed with apps per se. “My son is 6 years old now. By 11, he too will develop an app.”

Generations X and Y have made apps for writers, SMEs and even painters, but not many for e-commerce platforms; they are just the staging rooms that guide you to a website where the final order is placed through secure gateways. “With smartphones, banks can’t ignore apps as a means of financial inclusion,” said Nikhil Sama, founder of app maker Snaplion.

For an app to be developed for a bank, you first have to tackle the security of phone and banking data and “meet the bank’s technology needs because all these projects are large”, added Sama. But there are issues. For one, hackers have moved to phones now. “Today’s malware is very intelligent; it lies dormant and gets active when there is a piece of important information to steal,” said Mohan Sundaram of Red Force Labs, a software security firm. Banks may ring-fence back-end servers and gateways, but your network gateway can be broken into.

“The loss of a device with payment information is the most common reason for not
“When bank CEOs say they don’t want to be the first-mover in m-banking, well, there’s no such thing. You have to be in it or you will be finished.”

Trying m-wallet. Smartphone users are more concerned about it, and they are more likely to be keen on m-wallets than basic phone users (63%),” said Nitish Asthana, executive director at First Data Corporation. According to consultancy EY, smartphones get exchanged or resold every eight to 12 months and with that go customer data which is monetized in the gray market.

That said, can startups pull off a banking app? “It involves a lot of integration of software and hardware, large teams and contracts that last for lengthy periods,” said Alok Mittal, MD, Canaan Partners India, a venture capital firm. Only the top five Indian software services firms can do this. “In the US, you have apps that track usage of your debit card and send reports on how to become intelligent with spending money,” said Mittal. AdNear, a location-based advertisement, maps you on call tower signal codes and pinpoints the location when you use an app. The rate is 5 to 10 cents per impression, and the revenue is shared in a 60:40 ratio with the ad network.

And such apps are challenged by state-of-the-art browsers and standalone mobile app platforms. “It is only a matter of time before you get an Android, iOS or Windows-compatible app,” said Kedar Sohoni, president of Informate Mobile Intelligence, which maps mobile behavior. He debunks the notion that smartphones are for the elite. A smartphone, he said, uses an identifiable open OS supported by third-party apps written by a notable developer community. They can be installed and removed, and they can be created for the device’s OS and application programming interfaces (APIs, a set of tools and rules for developing software programs).

Alternatively, developers must be able to access APIs through a discrete layer such as a Java platform. The OS must back a multi-tasking environment and a user interface to multiple apps simultaneously. “But a few years down the road, smartphones will penetrate across all social strata and even a feature phone will have the capability of today’s smartphone,” added Sohoni.

**Fellow Travelers**

Make no mistake, this is not just about banks and telcos. The European Financial Review (March 2013) said by 2015, over 900 million people may transact $1 trillion in m-payments. Enter big-time retailers and silicon. Walmart, Target, and Best Buy have joined hands to create their version of an m-wallet, the Merchant Customer Exchange, to gain a foothold in payments (combined, these retailers’ total customer spending is $1 trillion). So too Google Wallet and Apple Passbook. Then you have Facebook Credits with money transmitter licenses in more than 15 states in the US and Twitpay for Twitter-based fund-raising. It’s anybody’s guess as to how the entry of big retail into India and the rise of social networking will shape the topography even if it is the RBI that decides the rules on payments.

In the case of local banks, multiple systems have been built over a period of time; integration with the mobile leaves a lot to be desired. “Banks are ensuring the mobile channel has a focus for various bearers—client app, SMS, Unstructured Supplementary Service Data (USSD, a technology used for sending text, mostly real time); an integrated mobile middleware to interface various backend systems,” said Nidugondi. “State-run banks have been slow to launch comprehensive m-banking and while most have launched a mobile service, they have had limitations that restrict their utility,” said Bhat. Outsourcing to technology providers is also a strong trend. Over 800 banks and credit unions in the US (including more than a third of the 50 top banks) use Florida-based FIS’s outsourced m-banking offering. The fast pace of evolution of mobile and device platforms makes it unsustainable and disruptive for banks to manage on their own.

They have to reach out.

Said Ravi Jagannathan, vice-chairman of eMudhra and director of mobile wallet YPayCash, “If one were to look at the US, players from different industry segments have come together to create JVs and consortiums. ISIS has been formed with banks, card companies and telcos coming together.” But irrespective of the model, the key is how well products are designed, how much additional value to customers and merchants is being given by say, integrating shopping-related parameters to payment and, finally, having a revenue model at a unit level so that it is sustainable. “Square, m-pesa and PayPal attest to the fact that they have had sustainable margins at a unit level along with product features which have addressed either a customer or merchant need,” said Jagannathan.

But it is Accenture’s Singh who hit the nail on the head. “It is not about technology. Sooner or later, it will get created and adopted. Just what is the proposition that m-mobile presents to the customer? M-banking is just another channel. Can you service the customer across channels? That is the point.”
WE ALWAYS LOOK FOR WAYS TO SURPRISE

Hermès Middle East and South Asia managing director Luc Hennard believes India is as much of an inspiration as it is a market for the luxury brand.

Interview by Smita Tripathi

PROFILE

Luc Hennard
He joined Hermès as managing director of the Benelux-Scandinavia region in 2003 and then moved on to become managing director of northern and eastern Europe. He took up his current position in September of 2012, and now manages a region covering West Asia, South Asia, India and Australia. Before joining the luxury brand, he dabbled in the food business for a decade, having started his career at Quick Restaurants in Brussels, followed by a four-year stint at Godiva Chocolates. He is currently based in Singapore.

In an email interview, Hennard expounded on Hermès’s Asia strategy, and how it intends to woo Indian customers.

“The Indian customer is very discerning, and not easily fooled or pleased.”
With the European and US luxury markets stagnating, are Asian markets now at the forefront of the luxury sector?

The Asian markets have been comparatively more resilient during the last few years, and even if we see some changes now, we’re still optimistic about them. Their potential is good, and future growth will come from these markets. If we look at Southeast Asia and the Middle East, they have achieved very good performance despite the downturn in the last few years; Indonesia, Thailand and Malaysia, for example, have had good growth. Even if India is not performing as strongly as the others, we can still see a positive trend here. I firmly believe in the potential of Asian markets because of their steady economic growth, the general all-round stability and the rising middle class.

These countries are seeing the emergence of a strong upper middle class which is not only the critical target segment for long-term growth and loyalty, but is also big as far as local purchases of luxury goods go. Despite the adverse global economic conditions, the economies of these countries are likely to continue to grow.

How is the luxury customer in Asia and the Middle East different from the luxury consumer in Europe or the US?

As in Europe or in the US, luxury consumers in Asia and the Middle East will have a separate profile. Besides, the motivation to buy luxury goods will also be different. The Asian luxury market is evolving and the taste for luxury has changed. While some are looking for branded luxury goods, driven by social differentiation and status, others have a more conservative approach, including how they value a product as "luxury." But the luxury consumer in emerging markets has become more demanding and sophisticated—a more mature consumer. Also, in these markets, we have seen the highest growth rate of connoisseur consumers as they transition from emerging status, which is a good thing for us.

What has Hermès done differently to cater specifically to Asian tastes?

Nothing more than what we are now doing elsewhere in the world. Of course, there is “The luxury consumer in emerging markets has become more demanding and sophisticated—a more mature consumer.”
the essence of Hermès itself—exceptional products through our different métiers. We also ensure that we always have the latest designs and colors, so our customers have the same choice that is available globally. Lastly, the entire product range that Hermès has on offer allows us to constantly surprise our customers and create a unique and authentic experience.

Who is an Hermès customer in India?
We’ve been in India for about five years now, first in Delhi and then two years ago in Mumbai, and in both markets we’ve seen a wonderful evolution of our customers. At first, our customers were those who were already familiar with Hermès, perhaps, from their travels abroad.

Today, we can say that the Indian consumer is very discerning and aware of what is available across the world. They are not easily fooled, or pleased. Which, I think, is quite an interesting challenge. We are constantly pushing ourselves to understand how we can not just meet their expectations but deliver something unexpected.

What was the response to the saree collection? Are there plans to revive it or launch any other product especially for the Asian market?
The saree collection was an Hermès tribute to Indian culture. It gave us the chance to come up with an exceptional offering. Using Hermès knowhow in silkscreen printing, we presented four styles in different colors that sold out completely from our Mumbai store. It was a novelty to try something like this, and customers appreciated the homage.

Being a limited edition, such a collection allows a customer to have a very intimate relationship with Hermès. Interestingly, while the saree was, of course, picked up by long-time Hermès buyers; for a few, it was their first Hermès product. Quite a wonderful way to start a journey with Hermès! And, in the future, we will continue in this direction.

What products work best for the Indian market?
Initially, it was iconic products like silk and leather that were most associated with Hermès. However, with time, we’ve seen people grow to experience the entire world of Hermès products on offer, from ready-to-wear for both men and women to watches and the home collection. It’s very exciting to see the market develop. A very interesting métier for us is watches, and Hermès has introduced particularly innovative movements in the past two years that have been of great interest to watch connoisseurs here. It’s an appreciation for absolute quality and perfection that brings people to Hermès.

Are there any plans to open more stores in India?
We have two beautiful stores in India, one in Delhi and one flagship store in Mumbai at Horniman Circle. We were the first brand to be directly on the street in a market that is dominated by hotel and mall-centric outlets. These stores perfectly express our positioning in India. We don’t have any expansion plans for the moment but we’re very attentive to further development.

Where do you see the Indian luxury market five years from now?
India is a challenging market, but also the most interesting. It is a young market with good potential, and like any new market it requires time for the client to develop a relationship with the brand. With foreign direct investment rules changing, the market will see an influx of international brands that will, in turn, create a more informed customer. For Hermès, India is as much of an inspiration as it is a market. It is an emerging luxury market and slowly but surely we are seeing success.
THE REBIRTH OF TEXTILES

A decade ago textiles was seen as a sunset industry. That didn’t prove to be the case, but to grab some of the big opportunities in the global market, much still needs to be done before Indonesia can boost its market share.

By Albert W. Nonto
Workers are threatening strikes and demanding higher wages. Other costs are increasing, including the cost of logistics as infrastructure becomes increasingly snarled. Yet major players in the textile business have set aside enough capital to take their operations to the next level.

They plan to modernize their factories as well as increase production capacity. These players see a silver lining in the business for the next five years or more. Scarcity of labor in China and changing tastes and lifestyles have led to higher demand for quality fashion, creating opportunity for Indonesia’s textiles business.

Anne Patricia Sutanto, vice president of Pan Brothers Tex, is upbeat. The garment industry has started to recover from its so-called “sunset” phase of a decade ago. Her company is working to increase production capacity from 40 million pieces per year to 70 million over the next five years with investment in seven new plants in addition to the existing 12 factories.

In terms of sales, the trend is clear. Orders have been increasing steadily, including from the new market of China. In total, the Asian market rose from taking 27% of production in 2011 to nearly 32% in 2012, and the growth shows no sign of slowing. Main markets in Asia such as Japan remain dominant but other countries such as Thailand, Malaysia and Vietnam are also demonstrating strong demand growth.

The emerging middle-class economy in China has become brand-minded, creating new opportunities. In addition to its traditional position as a market for around 30% of global output, China is increasingly demanding high-quality fashion, an area where Indonesia has strong credentials.

These trends create a situation in which there is strong momentum for growth in the garment industry, especially for branded fashion. While some concerns are beginning to surface about social instability in Indonesia, most brand owners retain a positive outlook on the country.

Growth in demand has been such that Pan Brothers has had to import material to boost production capacity. Synthetic fiber, nylon and polyester have had to be imported. In fact, said Anne, while Indonesia does produce these materials, output is no longer adequate to meet demand, especially in certain areas. The key is new investment in upstream business, she said. “We are open to any expression of interest,” said the woman who was born into the textile family of the Batik Keris Group.

While maintaining its international market to meet its commitments to international brand holders, Pan Brothers, as one of Indonesia’s largest garment players, is also working with the domestic market, launching its own international-quality brand. Starting with a small number of stores, Anne believes the new line will be accepted by Indonesian customers and later by the international market. “We want to expand to Vietnam and then to China,” she said.

Other integrated textiles producers such as The Nin King’s Argo Pantes Group and Century Textiles are also expanding, although there is concern that margins are shrinking. There is also a push into new export markets, with Vietnam being one popular choice for expansion.

Ricky Putra of Globalindo, the king of underwear with the brands GT Man, GT Man Sport, GT Kid, Ricssony and Bum Equipment, is looking to open a new plant in Vietnam. Kahatex Group, the largest integrated textile company in Indonesia, has also expanded outside Indonesia.

The stronger Asian market has produced another benefit, particularly for the garment industry. Operators are no longer solely producers for international brand orders, with the result that their bargaining positioning with the brand holders has become stronger. Iswardeni, corporate secretary at Pan Brother Tex, said that Indonesia now handles most international garment and material design trends. This gives Indonesia a bigger opportunity to lead the business in the future. “The garment business is not simply a money machine which demands heavy investment and which is labor-intensive, but it also needs a more artistic and creative
Indonesian Manufacturing

It’s widely acknowledged that Indonesia’s competitiveness needs to be improved by work on both regulatory aspects and, most importantly, infrastructure.

approach, and Indonesia has that,” said Iswardeni.

High-Level Lobbying
While existing markets are growing, finding new potential markets is also important. The European Union already takes around 30% of Indonesia’s output, but many believe there is still room for growth. The EU’s total population is equal to the US, and purchasing power is actually stronger. The key is to keep working hard to negotiate on tariffs and non-tariff barriers.

Ade Sudrajad, chairman of Indonesia’s Textiles Association (API), believes that Indonesian negotiators need to be tougher in order to reduce tariffs from the current average of between 10% and 15%. He argues that Indonesia should receive privileged treatment since it has become a market for European products such as machinery, automobiles and the financial sector. This should be brought to the negotiation table, Ade believes.

While Indonesia pioneered its textile business 30 years ago, growth has been steady but by no means exponential. Big buyers have tended to go elsewhere to make purchases. Vietnam has seen its textile business boom, now contributing about $19 billion in exports and backed by conducive tariffs. Many international buyers go to Sri Lanka, which is even more competitive since it can trade with European countries with zero tariffs.

The key for opening new market opportunities is a tough negotiation stance. In the European market, for example, Ade said there has been no real effort to boost business opportunities. Market share has been stagnant and he sees a need to define a clear agreement on tariffs.

“We have to be complementary with Europe because we also import loads of goods from there, so we have negotiation points that we can bring to the table, and this is the government’s job,” he said, adding that Indonesia would benefit from a new, detailed free-trade agreement with European countries.

“We have to chase them since at the start our counterparts may be reluctant to talk and refuse to meet us. On many occasions Indonesia has lost important momentum,” said Ade, who no longer operates in the textile business, having shifted to property ventures. Besides tariff issues, he said that Indonesian producers are at times forced to follow strict rules on raw materials and environmental issues such as eco-labeling.

Indonesia at the moment controls only about 1.8% of the global $750 billion textile business, leaving the vast bulk to big players like China. A newcomer like Vietnam has surpassed Indonesia with market share of about 3.6%, earning about $21 billion last year from textile exports. Indonesia made only $12 billion.

With 27 member countries in the European Union, Ade believes the potential exists to improve market share. If all parties do their job over the next five years, Indonesia should be able to increase its international market share to as high as 5%, worth about $30 billion. From the government’s side, effort is needed to concentrate on details of trade arrangements.

As a labor-intensive industry, textiles are always subject to political issues, which can impact heavily on the performance of a company. Wage issues are a major factor, with regional leaders striving to please workers by backing big wage increases, even though this can destroy company performance. Workers themselves have learned that they can exercise their power by mounting rallies and strikes that impact production. This, noted Ade, risks further damage to Indonesia’s competitive ability.

Shrinking Margins
Given the current mix of pressures on the industry, it is little wonder that many textile companies are seeking new environments where there is the possibility of boosting...
profit margins. While they are newcomers in the industry, Sri Lanka and Vietnam have been successful in attracting investors because of friendly tariff policies and relative political stability.

It’s widely acknowledged that Indonesia’s competitiveness needs to be improved by work on both regulatory aspects and, most importantly, infrastructure. Prospects are not entirely dim, though. “If we compare apples-to-apples, even with Vietnam or Bangladesh, Indonesia can still win the game,” said Pan Brothers’ Iswardeni.

In the short term, Vietnam may be more successful, but that success may be short-lived. “They have limited capacity in terms of workers and resources,” said Anne. In Sri Lanka there is concern over continuing security issues.

Both Anne and Ade added that in the spinning sector, Indonesia faces the problem of energy shortfalls and availability of resources. So far, Indonesia has been competitive in the sector, which is capital-intensive but simple to operate. For fabric mills that also produce spun yarns from raw materials, success depends on a benign combination of energy sector policy and import duties for those raw materials, while in the garment sector far more factors determine performance.

Anne still believes that it is a misperception that the sun is setting on the textile business. Everyone needs clothes, she noted, and Indonesia’s own domestic economy is improving. Over the past three years, she has seen an improvement in the government’s understanding of the sector, helping it to grow with better policies.

Meanwhile Indonesia is fighting head-to-head with three countries at the moment: Vietnam, China and Cambodia.

The Indonesian garment industry’s competitiveness must lie in innovation and technology, especially in secondary processes and in innovation with materials, especially polyester, she believes.

“We will win market share if we are innovative and creative, but at the moment and for the next five years, China will still be the largest garment maker. Of late, though, there are signs of labor scarcity in the sector,” said Anne. Pan Brothers intends to push into China itself in the near future, she noted.

The slowdown of production in China will at the same time create a new market for other countries.

She believes Indonesia is the best destination for investment in the industry, even compared to Vietnam. She accepts that there are risks over the next two to five years due to the political situation, but she stressed that the key to resolving any problems is transparency and effective communication with labor.

“We have to supply information about company performance and about our plans and their realization. I also believe that good intentions and good faith in doing business will also help to resolve this situation, particularly in dealing with workers.”

Even though margins are getting thinner, industry players seem to have faith in the sector. “There is no problem with thin margins as long as there is still growth in sales,” said Iswardeni.

As an industry that continues to contribute to economic growth and as a major employer of labor, the textile industry needs to be considered as an integral factor in the grand design of national industry.

Textiles and textile-related products need to be considered in energy policies. Investment in refineries would guarantee a supply of basic chemical products that can be used to produce derivatives.

At any oil refinery, 30% of crude oil can be processed into chemical products including polyethylene, nylon and many more. This is the task of government, because it deals with huge investment, according to Ade and Anne.

So far, they believe, Indonesia has been left behind in refinery development. “This is very important if we want to make our industry, including the textile industry, competitive. Everyone has to come to share the same perspective on this,” Anne said.
Brazilian Industry

COMPETING WITH MIAMI

Brazilian e-commerce is being boosted by international investment. The most recent area is baby products.

By Ana Luiza Leal

The best place to understand the Brazilian baby products market is an international airport in Brazil. Every day, many couples land, coming back from Miami with suitcases full of clothes, toys, strollers, baby bottles, car seats, baby monitors, and all kinds of gadgets. This is how the wealthiest are known to make their babies’ "layette." The common people—those Miamiless—have to make do with buying the same items in Brazil. The surprising thing is that even with all these people going abroad for shopping, the Brazilian market for baby products has nearly doubled over the past five years, reaching $533 million in annual sales.

But retail has not evolved at the same pace as parents shop: the variety of items available is still limited, prices are high, and there is no national chain of specialized stores. The industry leader is Alô Bebê, with an estimated revenue of $41 million and 19 stores. In the United States, a chain such as Babies "R" Us has over 200 stores selling thousands of items. Brazil is another world—which explains so many trips to Miami.

A race started a year ago to change this
The biggest bet was made by American private equity fund Carlyle that bought the two largest chains of toy stores in the country, PBKids and Ri Happy, for $246 million. The company has recently announced that it will invest $82 million to open 100 stores with the brand Ri Happy Baby. "We have to grow before our competitors do," said Ricardo Floh, Director for New Business of the company. And he does have reasons to worry. In recent years, large amounts of money have wildly invested in Brazilian online retailers. The German fund Rocket has bought stakes in clothing, furniture, and jewelry retailers. The American fund Tiger invested in Netshoes, specializing in sports. Companies that sell wine, crafts and even pet shops received investments. The baby products market and make some real money out of it.

### THREE NEWBIES IN THE FIGHT

The size of the Brazilian baby products market and the three companies fighting for leadership in online retail—all with famous partners.

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<tr>
<th>Largest online retailers</th>
<th>Bebê Store</th>
<th>Tricae</th>
<th>Baby.com.br</th>
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<td>2008</td>
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<td>2013</td>
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**Sales of clothes, food, hygiene products, and toys**

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<th>Bebê Store</th>
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<td>Revenue</td>
<td>80 million Reais</td>
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<td>Atomico Fund, Skype co-founder</td>
<td>Rocket German Fund, Dafiti owner</td>
<td>Accel Fund, former partner of Facebook</td>
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(1) Estimates Sources: Euromonitor and companies
market is the most recent on the list. Three online stores in this segment have received investment from large foreign funds. They have similar strategies: to provide, in a single place, a variety of new products to the Brazilian market. For example, strollers alone are available in 300 models (a “physical” store usually has 10 of them on display). The goal is to create a new Diapers.com, an American diapers and baby products store purchased by Amazon for $410 million in 2010.

Bebê Store is leading this race. It was launched in December 2009 by a couple with e-commerce experience: Leonardo Simões used to work at Buscapé, a price comparison web page, and Juliana Della Nina at Submarino. The company has received over $12.3 million in investment, a great part of it from the Atómico Fund of Skype co-founder Niklas Zennström. It is followed closely by Tricae, established in 2011 by German fund Rocket. Ranked in third is Baby.com.br, also established in 2011 by American entrepreneur Kimball Spencer-Thomas, who was studying for his MBA at Harvard when he decided to open a baby products store in Brazil. Baby.com.br received about $16.4 million, and one of its partners is Accel Partners fund, famous for having invested in Facebook before everyone else. “It’s exhausting for parents to go from one store to another when they have small kids,” said Simões of Bebê Store. For him, it’s easier to buy everything online and wait at home.

These companies face the same challenges as all Brazilian online stores: to make a profit. None of the three companies have succeeded yet; selling high-volume products such as diapers attracts attention to the web page but doesn’t make money. Therefore the hope is to increase interest in more sophisticated and profitable products. But until then, things can get more difficult. B2W and Walmart are expanding their product offerings in this segment. Alô Bebê launched a new version of its web page at the end of 2012, and Ri Happy Baby will launch its online store in early 2014. Another challenge common to them all is to convince parents to pay up to $1,200 for a stroller—more than double they would pay in Miami. And without the perk of going to the beach.

What’s behind the change of attitude is the fact that Brazil has become a more protectionist country in recent years.