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IPTV Leads the New Way for Local Color TV Industry

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On Jan. 13, 2010, Chinese Premier Wen Jiabao chaired the executive meeting of the State Council, which has clearly identified the strategy of accelerating the integration of the telecom network, broadcasting & TV network and Internet. On Jan. 14, 2010, Zhu Hong, the spokesperson of the State Administration of Radio, Film and Television (SARFT), said China would strengthen the development of new media, focusing on the CMMB TV and IPTV.

TCL, a leading TV maker in China, announced it would launch the true "IPTV" on March 31, 2009, and it would stop the production of TV sets above 40 inches other than IPTV on November 11 of the same year. One month later, Changhong, another major TV maker in China, announced its decision to stop producing non-IPTV flat panel TVs above 32 inches. In addition, Konka declared in a high profile that it would produce 3.50 million IPTV sets in 2010, more than 50.0% of its total shipment of flat panel TV sets.

China's color TV industry is generally con-

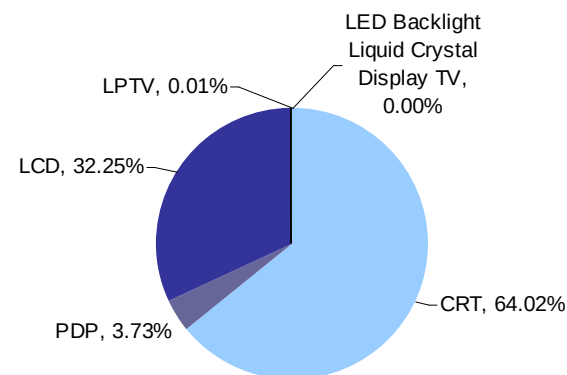
sidered a sunset industry, because the industry lacks the core technology, the poor bargaining power with the upstream and the downstream sectors. Color TV enterprises have staggered over the most recent ten years.

In 2009, while many industries were caught in the crisis due to the financial tsunami that has swept the entire world, the color TV, in particular that in China, seemed to have found out a new way of development. After the publishing of the "three-into-one network integration" policy, the product in which Chinese color TV enterprises own their core technologies, IPTV, has become a hot topic. It can be predicted that once the "three-into-one network integration" succeeds, the development of IPTV and relevant industries will embrace an upcoming revolution.

I. Color TV Industry Will Embrace Long-term Optimistic Prospect

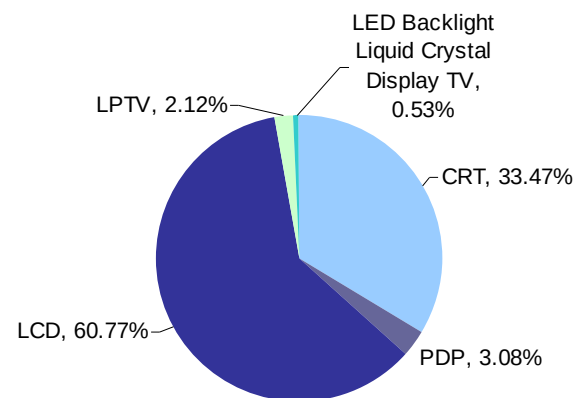
In 2009, the color TV industry made a

Chart 1 Comparison of Market Share of Products in 2008



Source: AVC

Chart 2 Comparison of Market Share of Products in 2009



Source: AVC

long stride due to the vigorous drive of the policy, and this year is thus called the "first year of the era of color TV industry" by many industry insiders.

1. Product Mix in Color TV Market is Changing

The market shares of different types of color TV products experienced substantial changes in 2008-2009. In 2008, the market was almost dominated by CRT color TVs with a share of 64.0%, followed by LCD color TVs at 32.3%. IPTV took up a share of almost zero. In 2009, LCD TVs emerged with a share of 60.8% of the market, snatching much shares from CRT color TVs, while IPTV expanded at a faster speed than before and succeeded in capturing a 2.1% market share.

2. Favorable Policies Have Driven the Continuous Development of the Industry

The central government has ear-

marked RMB2B in support of the "Old for New" policy to stimulate the replacement and upgrade in the urban home appliance market, and to drive color TV industry to evolve from CRT color TVs to flat panel TVs, apart from the policy of promoting the sales of home appliances in the rural areas. The "Old for New" policy has delivered the most obvious effect on promoting the development of home appliance industry. Launching of the "three-into-one" network integration policy has paved the way for the further development of color TV industry.

3. The "three-into-one" Network Integration: On January 13, 2010, Premier Wen Jiabao chaired the executive meeting of the State Council, which has decided to accelerate the integration of the telecom network, broadcasting & TV network and Internet. The move is intended to realize the interconnection and resource sharing among three networks and provide users with enriched

1. Promoting Home Appliance in Rural Areas:

Date of Implementation	Scope of Implementation	Maximum Product Price (RMB)	Subsidy Standard	
2007.12.1	Shandong, Henan and Sichuan	2,000	13.0% of sales price	
2008.12.1	14 provinces (autonomous regions, municipalities and cities under separate planning)	2,000	13.0% of sales price	
2009.2.1	Rural population nationwide	2,000	13.0% of sales price	
2009.5.14	Rural population nationwide	3,500	13.0% of sales price	
2010.1.1	Rural population nationwide + staff of State-owned farms and forest farms	7,000	13.0% of sales price for product priced RMB3,500 and below	Fixed subsidy of RMB455 for the product priced at RMB3,500-RMB 7,000 each

Source: Zero2IPO Capital

2. Old for New:

Date of Implementation	2009.6.1
Content	The "Old for New" pilot program was implemented for five types of home appliance products, including TV set, refrigerator (including ice lockers), washing machine, air-conditioner and computer in Beijing, Tianjin, Shanghai, Jiangsu, Zhejiang, Shandong, Guangdong, Fuzhou and Changsha. Subsidy: 10.0% of the sales price of new home appliances, but no more than RMB400 for each TV set, RMB300 for each refrigerator (including ice locker), RMB250 for each washing machine, RMB350 for each air-conditioner and RMB400 for each computer.
Beneficiary Industries	Color TV, washing machine, refrigerator and air-conditioner
Relevant Data	The central government earmarked RMB2B to subsidize the "Old for New" program of home appliance replacement at the standard of 10.0% of the sales price. This move is expected to stimulate an RMB20B demand for home appliance replacement.

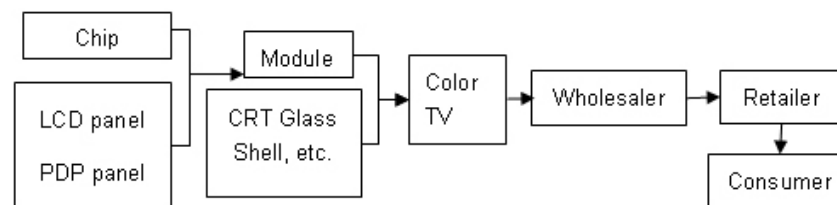
Source: Research Department of CITIC Securities

services like voice, data, radio and TV. It is also designed to innovate industrial form and promote the application of mobile multi media radio & TV, mobile phone TV, digital TV and Internet access services by making the most out of the favorable condition created by the integration of three networks. The central government will provide the financial, fiscal and taxation supports for product development, network construction and business application of the "three-into-one" network integration program as well as their promotion in rural areas. Traditionally in China, the cabled TV network is operated by the radio & TV sector, and the Internet is carried by the telecom sector. Failure to realize the interconnection of both networks has somewhat hindered the development of IPTV. However, the "three-into-one" integration policy will strongly boost the development of IPTV. Once the integration succeeds, the IPTV will undoubtedly develop at a fast speed.

II. Color TV Products Are Ready for New Landscape:

1. CRT color TVs: Products remain at the stage of stagnation, and the industry competition is not very fierce. Since 2009,

Industry Chain



the sale of color TV sets has started falling quickly, with a trend to exit from the industry.

2. PDP color TVs or plasma display panel TVs: Before 2009, PDP color TVs and LCD color TVs battled for the market and attempted to defeat the rival to become the "king" in the future development of the industry. However, the sale situation in 2009 proved that PDP color TVs are difficult to represent the future trend, and remain at the verge of disappearance after years of existence. At present, only a few products from Changhong and Panasonic are available in the market.

3. LCD color TV or liquid crystal display color TV: It is the mainstream product at present. In early 2009, it was generally believed that LCD color TVs and CRT color TVs would evenly split the market. However, LCD color TVs snatched 70.0% of the market share in the year, realizing a considerable growth in both production and

sale annually. The industry underestimated the development of LCD color TVs, resulting into the tight supply of panels from the upstream industry, and adding more pressures to the already weak bargaining power of color TV manufacturers with the upstream suppliers. At the same time, due to the excessively high price of LCD products, color TV manufacturers will not significantly adjust the terminal price even if the upstream suppliers increase the price, and their bargaining power with the downstream will also be limited. LCD color TV products have got caught in a dilemma while their sales have considerably expanded.

4. LED color TV or LED backlight liquid crystal display TV: It represents one of the future development trends. Currently, both LED TVs and LCD TVs sold on the market adopt LCD panels, and contain no substantial changes and breakthroughs in technology. Thus, they fall into the same category of product. The difference is that LED TVs can be thinner and more stylish with the introduction of the backlight source.

5. IPTV or Internet TV: It is also one of the future development trends. IPTV covers LCD, LED and all the TV sets that may be used as the terminal in future, and

innovates in contents. In reality, IPTV can also be understood as the LCD and LED TVs that own special functions and contents. As an innovative product of the TV industry in 2009, IPTV represents an all-new technology that transmits digital signals via the broadband Ethernet network, uses the broadband cabled TV network, and integrates such technologies as the Internet, multimedia and communication to provide home users with a wide range of interactive services, including digital TV. With the extensive penetration of the Internet, people have come to favor the Internet as an open platform, and the netizens are usually aged at 18-35. Thus, the Internet is attracting more attention from young TV audience. IPTV is just the terminator of traditional TV functions by giving users more options and allowing them to select by themselves rather than receiving passively. As a result, the monthly sale of IPTV sets had surged to about 100,000 units at the end of 2009 from rough 10,000 units in early 2009 when it was just formally launched.

For an extended period of time, the domestic TV brands have lost their ground in face of foreign competitors. They have not only lost the positions in the first- and second-tier cities, but also the traditional competitive markets in the third- and

fourth-tier cities. It has been an extensive topic among the industry on how China's color TV industry can make a breakthrough and how Chinese brands can realize sustainable development. It is generally believed that the future directions of China's color TV industry will be the LED TV and IPTV.

At present, the core technologies for both LCD color TVs, the mainstream product on the market, and LED color TVs, one of the future development trends, are not in the hands of Chinese color TV manufacturers. As a consequence, Chinese color TV enterprises suffer from thin profits and weak bargaining power with the up stream and the downstream and technical homogeneity, lagging behind foreign competitors and being passively involved in the process.

The story in IPTV arena is quite different. It features the reform in broadcasting contents as the key feature, and the chip technology for the homemade color TVs has already been owned by domestic enterprises. In addition, SARFT imposes strict control over the IPTV content platform, and has not issued business licenses to foreign investors so far. Thus, Chinese color TV enterprises outperform foreign rivals in both production and sale.

Under such context, it can be judged that IPTV will provide support for the domestic color TV enterprises to win the race.

III. IPTV Will Become Next - generation Mainstream Product

IPTV is a business that uses broadband network as the carrier and AV multimedia as the form, features interaction and personalization, and provides broadband terminal users with universal paid services. However, the service provided by IPTV is still free. IPTV production enterprises are making efforts to build the concrete provision platform in order to provide users with sound services, including online high-definition film watching, film download, sound information system and Internet access function.

With the continuous growth of the global Internet user base and the young age of Internet users, people prefer to choose the open and free Internet platform, rather than the TV system featuring closed network. The traditional TV is a mass communication media controlled by a TV operator, without interaction with audience, meaning the audience will have no choice but to accept the contents broadcast by TV operator. However, audiences now have increasingly

strong interest to select programs by themselves, rather than accepting the contents passively, so they prefer the products that allow them more freedom. The birth of IPTV just meets the strong demand of people for participation and independence.

On March 31, 2009, TCL announced it has mastered the core technology for IPTV and successfully developed IPTV products, and soon launched the true IPTV. At the end of 2009, the major domestic color TV brands expanded into the IPTV field, and stated the Internet function would become a standardized configuration of future flat-panel TVs. TCL and Changhong both announced they would stop producing non-IPTV large-screen TV sets, and Konka, Skyworth and other enterprises stepped up the promotion for IPTV. So far, all leading color TV manufacturers in China have launched the products with part of IPTV functions. MiTV of TCL features the online upgrade function, free from the restriction of existing product functions, and the functions to be released in future will be directly added to the IPTV sets that the users have purchased via online upgrade. To address the shortage of content resources, some famous Chinese color TV enterprises are joining hands to build IPTV content platform, which is bound to provide users with rich film & TV, information and

entertainment contents. Although IPTV is a new product, it has been quickly accepted and has grown rapidly, which is mainly because of the following characteristics:

1. The audiences are young and highly aware of IPTV, thereby creating the foundation for rapid penetration;

2. The price increase of just RMB200-RMB500 provides a relatively high price-performance ratio;

3. The integration of three networks will provide the policy support for the development of IPTV;

4. At the end of 2009, SARFT closed a number of BT download websites, BTChina.net, VeryCD.com and other famous download websites. These moves will be the very blessing for IPTV operators that own the genuine resources. At present, the homemade IPTV sets are all the products that domestic enterprises have developed in-house and owned the core technologies, so the domestic enterprises

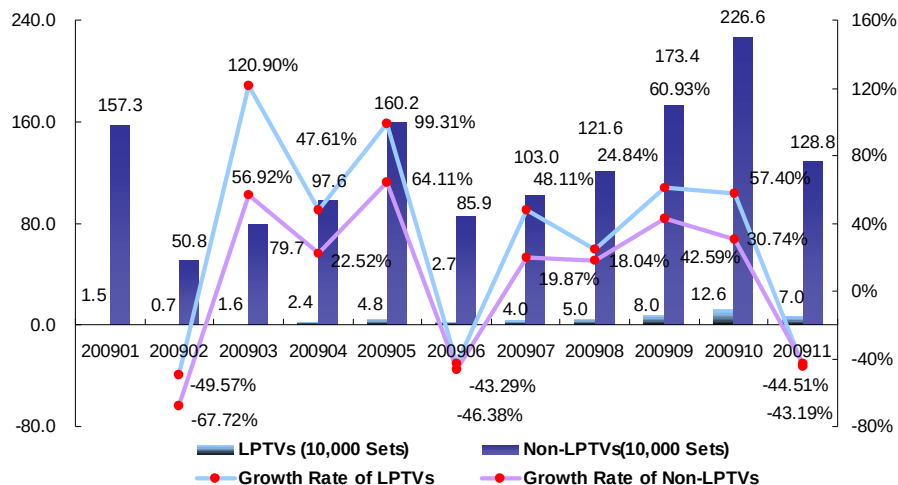
Brand	Pros	Cons
TCL MiTV	Having universal Internet functions like online film & TV download, online watching, game experiencing and karaoke, supporting online upgrade and allowing functions to increase without limit.	High price and less rich contents
Skyworth Coocaa	Mainly offering home karaoke function and introducing automatic on-demand function through voice.	Fewer functions and failure to upgrade in future after purchase
Hisense TLM47V88GP	Light and thin touch-type keys	Failure to upgrade
Changhong Lejiao Web TV	Mainly focusing on online education, and owning the 3G wireless network configuration.	Failure to upgrade
Haier MoCard	Browsing information and downloading film resources from the Internet.	Needing to buy specific Mo-cards to access different functions

far outperform foreign rivals in the IPTV business.

5. Foreign companies will be excluded in the short term. Foreign color TV brands are also coveting the big cake of IPTV. However, SARFT has made public the notice on the strict control over IPTV contents, and has not issued the policy concerning the promotion of IPTV by foreign color TV brands in China. Thus, they have had no choice but to shift to other markets such as the United States, Japan and South Korea, and achieved very excellent sale. They are also prepared to seize this vast market once the Chinese government gives them green light.

Driven by the aforesaid factors, the IPTV

Chart 3 Month - on - month Comparison of Sale and Growth Rate of LPTVs in 2009



Source: AVC

segment outperformed the entire color TV industry in the first 11 months of 2009, and maintained the sale growth rate higher than that of the entire color TV industry. In addition, the IPTV segment had taken a 2.1% market share in 2009 from almost zero a year earlier. It is generally forecasted that the IPTV segment will grow by more than 50.0% in 2010, creating new breakthroughs for the color TV industry and forming a new media industrial chain.

Despite good momentum, IPTV will undoubtedly face barriers and uncertainties because it belongs to a segment of color TV industry and remains at the post-birth stage of the industry.

some preset video websites that cooperate with color TV manufacturers and their functions are still very simple.

2. The platforms are not mutually connected, and do not have the basic property of the P2P communication, thereby restricting the content provision.

3. Most IPTV sets are unable to be upgraded after delivery. The product functions are restricted by the functions when they leave the factory, and can not be enhanced through online upgrade.

4. Traditionally in China, the cabled TV net-

1. The true IPTV should own the independent content platform. However, building such a platform will be very expensive at the initial stage. At present, there are very few color TV enterprises that have their own content platforms and program resources. Instead, most IPTV sets can only browse

work is operated by the radio & TV sector, and Internet is carried by the telecom sector. Failure to realize the interconnection of both networks has hindered the development of IPTV. The policy of the "three-into-one" network integration can effectively address this issue, but the policy has just been published. It will still take some time before it makes a difference. The effect of the integration is difficult to judge now, and also faces certain risks.

5. Network rebuilding and upgrade. Judging from the network condition, China has basically built the broadband backbone network, but the current broadband access condition can not completely satisfy the need of IPTV. In order to provide high-quality video contents, it will be very necessary to rebuild and upgrade the current broadband access, which will entail a heavy investment.

6. Business mode and profitability mode. The charging mode for the access service still needs exploration and discussion. At the same time, efforts must be done to find the effective profitability mode and establish the reasonable tariff rate before the IPTV service is offered.

7. Competition constraint. The barriers to the development of the IPTV business

include the failure to break the TV pattern in the long term, the extremely strict management of TV contents, the rampant piracy, the penetration of Internet and the richness of resources.

China's color TV industry has entered a maturity stage after years of painstaking efforts. Backed up by such blessings in economy, policy and industry, the color TV industry will still maintain a momentum of long-term steady development. Until today, the product structure of China's color TV industry and the competitive landscape between domestic and foreign manufacturers have basically taken shape. The dominance of LCD as the mainstream product is difficult to be challenged, nor is the leadership of foreign products. With the robust development of China's Internet industry and the unremitting efforts of the local color TV enterprises, IPTV has come into the historical stage as a homemade color TV product that has core chip technology, uses the Internet to share resources and leverages the content provision of SAFRT. In the

hard to increase in the short term, IPTV has taken a firm step ahead based on the powerful boost from the state policy, industry orientation, customer requirement, technical support and other factors. Based on the core technology and unique position as content provider, IPTV sector will crowd out foreign brands, and thus provide a strategic option for the domestic color TV enterprises to regain the lost ground. However, IPTV, which remains in the infancy, still faces many uncertainties, constraints and operating risks. To achieve the long-run development and compete against foreign brands in the domestic color TV industry, it will be necessary for the domestic brands to build a good content platform, provide users with abundant genuine contents and more entertainment and interaction functions, and seek the most suitable business mode. However, as long as the target is clear and the direction is solid and correct, the result will be encouraging, and the hardships in the process will be nothing important. For the tomorrow of China's TV industry,



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