Piracy hurting China's own industries

By JOE McDONALD, AP Business Writer
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BEIJING - Kingsoft Corp.'s English-Chinese dictionary program is used on most of China's 60 million PCs. That's the good news. The bad news: Kingsoft doesn't make any money from it, because 90 percent of those copies are pirated.

One by one, the Beijing-based software maker has seen its sales of such popular products destroyed after black market producers flooded the market with cheap copies.

Today, Kingsoft's 600 programmers focus on making what it hopes can't be copied — online games and business and anti-virus programs that have to be linked to its own computers in order to function.

"Piracy has had a big impact on us, making it so we can't get powerful and compete with Microsoft," said Ren Jian, a former Microsoft manager who is Kingsoft's chief operating officer.

Kingsoft is far from alone. Rampant Chinese piracy of music, movies and software that raises howls of protest from the United States, Europe and elsewhere is hitting China's fledgling creative industries hardest of all. Robbed of sales in their key home market, companies are short of money to develop new products to compete with foreign rivals.

Losses to piracy are especially damaging at a time when communist leaders want China to transform itself from the world's low-cost factory into an "innovation society" that makes its own profitable technology and brand names.

China has long been the world's leading source of illegally copied music, movies, designer clothes and other goods. U.S. officials say its exports cost legitimate producers worldwide up to $50 billion a year in lost potential sales.

At home, sidewalk vendors sell unlicensed DVDs of Chinese movies for as little as 50 cents. Software makers say more than 80 percent of programs used on China's PCs are pirated.
Few brands are immune. A government list released this month of recent major piracy cases included a gang that sold $300,000 worth of fake Wuliangye, a popular Chinese liquor. Another trafficked in counterfeit upmarket Chunghua cigarettes.

Sporting goods maker Li Ning Co., which has ambitions to expand abroad, says it sees copies of its shoes and athletic clothes in markets alongside Nike and Adidas counterfeits.

Kingssoft, the software maker, aspired to be the "Microsoft of China," but was forced by piracy to stop selling games, a media player and other mass-market programs. Ren, the COO, says the consumer logic is simple: A pirated copy of Kingsoft's Chinese-English dictionary costs one-tenth the $12 price of the real thing.

The onslaught has forced Kingsoft to narrow its product range, with two-thirds of its programmers now working on online role-playing games that players access on Kingsoft's computers for a monthly fee — part of a thriving Chinese market for online games.

President Hu Jintao called attention to piracy's cost to China in a May 27 speech to Communist Party officials. Enforcement "is an urgent need for ... enhancing the country's core competitiveness," Hu said.

"We should strengthen our law enforcement and lawfully and severely crack down on and effectively curb law-breaking and criminal acts of violating intellectual property rights," he said.

The government has tried to undercut the black market for software by ordering computer makers this year to sell PCs only with legitimate operating systems already installed. Officials have been told to remove pirated software from government computers. Commerce Minister Bo Xilai said in March that process was under way, but he set no deadline for compliance.

And Chinese companies are fighting back in court. The government says they are responsible for 90 percent of lawsuits filed against Chinese copyright and trademark violators.

Yet trade groups and foreign governments say that despite repeated crackdowns, China's output of pirated goods is rising steadily, along with its rapid economic growth.

A report in May by the American Chamber of Commerce in China said that 43 percent of 76 U.S. companies surveyed said they have seen an increase in the amount of counterfeiting of their products, while 55 percent said the amount has stayed the same. Only 7 percent saw a decrease.

Losses to piracy have made film studios and music companies reluctant to finance new releases at a time when they might be cashing in on rising foreign interest in Chinese pop culture.

Chinese musicians say piracy makes producing new CDs so unprofitable that they are treated as just promotional material for concerts, which provide performers' real income.

Web sites that carry unlicensed copies of CDs often give away the music for free and make money from advertising. That takes advantage of a provision in Chinese law — one that trade groups are lobbying Beijing to change — that requires pirated goods to be sold before violators can be prosecuted.
Chengdu Xiangsha Music Co., in the southwestern city of Chengdu, got out of its main business of distributing CDs and promoting new performers in 2003 when it saw that losses to piracy "would be huge," said general manager Liu Jiming.

Now Xiangsha focuses on supplying music to Web sites and mobile phone companies, Liu said.

"Things are much better now," he said. "But we are still bothered by illegal downloads and online linking."

Losses to software piracy are especially damaging to China's plans.

Beijing wants to see the industry flourish, both to create jobs and to reduce reliance on foreign software, which communist leaders consider a strategic weakness. China has scores of small software companies and its universities produce thousands of programmers every year.

But battered by piracy, software developers are switching from selling products under their own brand names to working as subcontractors for U.S., Indian and other foreign companies — just the anonymous status that Chinese leaders don't want. Most Chinese software companies — such as DHC, Sinocom Software Group Ltd., Broaden Gate Systems Inc. and UFSOft Corp. — focus on subcontracting for foreign clients instead of selling to the general public.

A report this month by the Business Software Alliance, a U.S.-based industry group, said 86 percent of software used in China last year was pirated — one of the world's highest rates — though it said that was an improvement over 2004's figure of 90 percent.

Even though China is the world's No. 2 PC market, "the legal market for software is relatively small, because of the large piracy rate," said Jeff Hardee, the BSA's vice president for Asia.

"When the piracy rate is as high as it is, it's hard for (Chinese) producers to develop a market, while the foreign developers have the whole world market," he said.

In a separate report in December, BSA argued that China could see its information technology industries triple in size and create 1.8 million new jobs if its piracy rate were cut by just 10 percentage points over the next four years.

"China could potentially gain more than any other country," the report said.

Ren says the problem is not lack of official enforcement but Chinese consumers, whom he complains don't see that they are supporting innovation when they pay for legitimate goods.

"Ordinary Chinese people don't see anything wrong with buying pirated goods," he said. "We need to change people's attitudes. That is going to take time."
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