

# Mi and iPhone's shadow

Beijing start-up Xiaomi has stormed China's smartphone market to be nearly neck and neck with Apple's iPhone. Now it's going global.

STORY DANIEL ALLEN

Whatever happens now, Lei Jun, billionaire founder of Chinese smartphone manufacturer Xiaomi (pronounced "shao-mee"), can always reflect on doing something amazing. In less than five years his company has gone from nothing to rivalling Apple in Chinese smartphone sales. Last year, Xiaomi sold more than 60 million handsets, generating US\$12 billion in revenue and more than tripling its sales from 2013 in the process.

Last year's figures were the latest milestone in Xiaomi's astonishing rise. Many Chinese champion the company as the "Apple of China". That's not just because of resemblances between their products. A talented self-promoter, Lei frequently appears in black shirts and denim jeans, a look reminiscent of Steve Jobs, and his product launches have a distinct Jobs' style.

But while the sales figures for Apple and Xiaomi smartphones in China may be almost neck and neck, the way the two companies do business could hardly be more different. While Apple hones its "premium brand" image, Xiaomi stacks 'em high and sells 'em cheap. >

Xiaomi CEO Lei Jun shows off the Mi Note smartphone, Xiaomi's answer to the Apple iPhone 6 Plus.

**"The Chinese device market is the most brutal battlefield in the world."**

PO HOU, DELOITTE CHINA



## FEATURE CHINA'S NEW TECH GIANT

"Xiaomi has pioneered a new business model in the Chinese mobile market," says leading mobile strategist Chetan Sharma. "The specifications of the company's handsets are competitive, but their prices substantially undercut other premium handset manufacturers." For Chinese consumers who want a high-end phone running Google's Android operating system, Xiaomi phones are an attractive option.

Xiaomi has sustained its cut-throat pricing by ditching traditional marketing and distribution channels. Instead, it sells all its handsets online, releasing a limited quantity of phones each week. This approach maintains demand, lets the company hold less inventory, and minimises risk. As component costs decline, Xiaomi can also increase production over time. Also keeping costs down is the way the business makes clever use of Chinese social media for marketing, says Po Hou, the national technology, media and telecommunications industry leader at Deloitte China.

Hou points to another source of strength, too: unlike many low-cost operators, Xiaomi has focused on crafting a strong experience for phone users. Xiaomi regards itself as a software company and has equipped its phones with its own rather Apple-flavoured version of Android, called MIUI. But it has kept that software open so that developers can continue to improve it.

### FOREIGN MARKETS

Soaring demand from newly wealthy consumers is driving the growth of several Chinese smartphone brands. Xiaomi faces competition from the likes of Huawei, Lenovo and Guangdong-based Oppo Electronics, which have all copied Xiaomi's online-focused business model to keep prices down.

So Xiaomi is looking to shift its handsets beyond China's borders. "With the Chinese economy slowing, companies with ambitious growth targets – such as Xiaomi – will need to expand their international presence to keep fuelling growth," explains Melissa Chau, senior research manager for IDC Asia Pacific. "This is especially true of Xiaomi, with its low profit margin on each handset sold."



Xiaomi now operates in Taiwan, Hong Kong and across South-East Asia, but moving into foreign retail brings its challenges for the company. "Xiaomi is now learning how to adapt to different Asian markets," says Chau. "In Singapore, for example, it has already had to cooperate with local telco operators. This adds extra costs and makes it more difficult to maintain price-driven sales."

India is currently Xiaomi's most important market outside of China. Just weeks after



Gartner researchers predict 395 million smartphones will be sold in China this year. Only about 20 per cent will be Samsung or Apple phones; most will be handsets from local players such as (from far left) Xiaomi, mobile phone giant Huawei and ZTE Corp.

the company began its Indian operations in July 2014, it became the country's fastest-growing smartphone brand.

The company wants to greatly expand its portfolio in India this year, with devices hitting the Indian market about two months after they launch in China. It is also setting up a research and development centre in Bengaluru [Bangalore] and is looking to purchase Indian start-ups.

But Xiaomi's Indian plans have already hit several snags. After initial problems with defective units, dissatisfied buyers bombarded the company's Facebook page with complaints. And Xiaomi also faces a patent dispute with Swedish communications firm Ericsson, which claims Xiaomi's phones infringe its own wireless technology. Xiaomi's phone sales have been partially suspended until the two firms can reach an agreement.

"Being a new company, Xiaomi doesn't have many patents," explains technology strategist Sharma. "This means intellectual property (IP) issues may be a significant hurdle for them. Xiaomi needs real technological capabilities protected by lots of patents."

To head off any further problems Xiaomi is doing its best to build up a healthy patent portfolio. During a recent product announcement, Lei explained that the company had already applied for more than 2300 patents, 665 of them outside of China – of which less than 150 have so far been granted. By comparison, Samsung has been granted nearly 12,000 invention patents in China alone.

### GETTING PRODUCTS OUT THERE

Distribution and branding are key challenges for Xiaomi as it moves into foreign fields. Currently it lacks the distribution channels to effectively challenge the big players in Asia, let alone Europe. However it's already selling its handsets in Brazil, and is making its first small steps into the US market this year, selling lower-priced accessories such as headphones and

**"Distribution is Xiaomi's biggest expansion headache."**

CHETAN SHARMA,  
TECHNOLOGY STRATEGIST



battery packs through its mi.com portal. Selling Xiaomi phones and tablets in the US isn't yet on the agenda, due to the "incredible amount of work" in localising hardware and software and getting the devices certified, the *Financial Times* reported in February.

If Xiaomi really wants to compete globally, most experts believe the company will need to create a global chain of stores like Apple's, and establish robust supply chains.

"Xiaomi's biggest challenge will be expanding its salesforce and getting phones on store shelves," claims Neil Mawston from Strategy Analytics. "There are millions of retail stores selling smartphones worldwide outside China, and it will take years to fill them up with Xiaomi products."

Sharma sees the same problem. "Distribution is Xiaomi's biggest expansion headache," he says. "In emerging markets the online channel only gets you so far ... Not everyone is connected, especially if you're targeting the budget end of the market. To maximise product access, the company is going to need an alternate strategy that will complement their online model."

This is not an impossible task. Rival Huawei has already established itself internationally and is partnering with US telcos to push its budget "MyTouch" smartphones there. >

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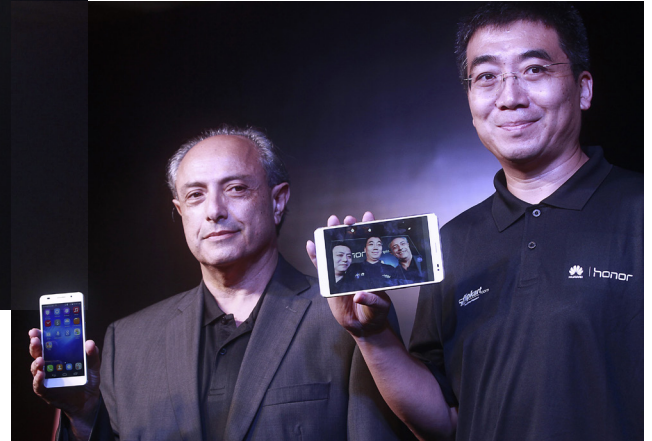




极致工艺



Lei Jun (left) is taking Xiaomi into India, but faces tough competition. Huawei India's Michael Adnani (below left) and Allen Wang launched the fast-selling Huawei Honor devices there last year.



Because such challenges require a huge and long-term financial commitment, many analysts believe Xiaomi should concentrate on the Chinese market a little longer before it embarks on serious overseas ventures.

“There is a real danger that the company will overreach itself,” says Chris Devonshire-Ellis, from Asia-based professional services firm Dezan Shira & Associates. He notes that the Asian markets which Xiaomi's vice-president of international, Hugo Barra, has talked about – Singapore, Hong Kong and Taiwan – are small and easily covered. “ASEAN alone has a population of 600 million,” he notes. “Selling a Chinese product in Hong Kong is one thing. Selling and distributing across Asia is quite another.”

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NEIL MAWSTON, STRATEGY ANALYTICS

### BUILDING THE RIGHT IMAGE

With some Chinese products still plagued by perceived quality or credibility issues, the success of any move overseas by Xiaomi will also depend on effective brand development. The company's phones often win good reviews, but its brand image doesn't yet match their capabilities. So far its image management is so undeveloped that even its online marketing and public relations contacts don't work, as INTHEBLACK discovered while writing this story.

“If Xiaomi wants to position itself as a company focusing on the mid to high-tier end of the market, it will certainly need to communicate better and look at other ways to market itself,” says IDC's Chau.

Devonshire-Ellis goes further, arguing that Xiaomi needs to develop “truly innovative products and services” if it is to shake off that “cheap Apple” tag.

To do this, Xiaomi could look to the Japanese and South Korean playbooks. By combining build quality and innovation with insightful marketing, companies such as Sony, Samsung and LG changed the negative way the world's consumers once viewed their products. Other Chinese brands, such as Lenovo, are already raising their international profile, partly by purchasing established brands such as ThinkPad and Motorola. Lenovo doesn't regard itself as a Chinese company at all, and makes concerted efforts to avoid appearing like one. Even its name doesn't sound Chinese.

Xiaomi has already taken note. In an effort to help out the linguistically challenged consumers of the world, it paid US\$3.6 million in April last year for the mi.com domain name. Many of the company's products now include “Mi” in their name.

As with the products, so with the personnel. Founder Lei plays a vital role in Xiaomi's marketing inside China, and was *Forbes Asia's* Businessman of the Year in 2014. But on the global stage he's a virtual unknown.

Sharma argues that regardless of whether Lei has modelled himself on Steve Jobs, global consumers should not be encouraged to see Xiaomi as an imitator. “Lei needs to be his own man,” says Sharma. “He needs to move the focus away from Apple and concentrate on his own personal philosophies.”

Like Lenovo, Xiaomi would also benefit from a more cosmopolitan management team. At Lenovo, for instance, Brazilians run Brazil, Europeans run Europe and Indians run India. In this respect, the 2013 hiring of Hugo Barra – Google's former vice-president for Android – showed the way ahead.

“Barra has definitely helped to strengthen Xiaomi's image in overseas markets,” says Sharma. “His drive to succeed in markets such as India continues to be a great asset for the company.”

### FUTURE FOCUS

With information on the company's expansion plans still sketchy, most investors are waiting on further developments before ploughing in any more cash. But just five years after its founding, Xiaomi seems full of potential. It wants to sell 100 million smartphones in 2015, a 67 per cent increase on 2014. Its ambition and drive are still there. If any Chinese company can maintain such spectacular growth, it's the Beijing-based start-up.

“The Chinese device market is the most brutal battlefield in the world,” says Deloitte's Hou. “It might be the world's largest market, but almost 100 per cent of people already have phones, and consumers are extremely picky. Local competitors are formidable and ruthless. Any company which can thrive in this kind of market should be feared by all.” ■