

# Largest IM Platform In China – Tencent's QQ

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## ABSTRACT

*This case illustrates how Mainland China based Tencent Holdings Ltd., through focusing on its core competencies, has rapidly evolved into a technology powerhouse in the global Instant Messaging market. In just over a decade, the company has influenced and changed the communication methods and life-style of hundreds of millions of Chinese in China and around the world. Staying true to its core competencies, such as intense attention to innovation, efficiency, and customer responsiveness, the company successfully expanded its marketplace footprint from a locally-sighted, straight-forward telecommunications service provider into a complex, internet value-added service provider with a global reach. This case includes an introduction to the instant messaging industry, followed by a profile of the company. Also, an extensive analysis of Tencent's core competencies is presented, along with a summary of the company's path towards internationalization.*

**Keywords:** China; IM Market; Core Competence; Internationalization; Strategy

## INTRODUCTION TO INSTANT MESSAGING

Instant messaging (IM) is popularly known as online chat; many think of it as interactive email, where emails are sent and instantly received. It consists of numerous computer- and network-based technologies that provide for and facilitates real-time, person-to-person text messaging. Much of the technology underlying an IM tool is unbeknownst to the user, however, the user's *experience* is heavily depended on the user-interface and features of IM software being used. Today, IM is no longer a simple text-based chat gizmo; it now transports a variety of information formats (image, audio, video, etc.) and has evolved into an integrated *information platform* that includes advanced communication, information, entertainment, search, e-commerce, office collaboration features and even comes with enterprise-level customer service support.

IM is a product with high customer loyalty--known as *stickiness* in the software industry. Customer attrition is minimal once one begins using a specific instant messaging software / provider. In 2008, 46.3% of Chinese IM users have 2-6 years experience and 40.7% have more than 6 years of experience—amounting to 87% being considered *highly experienced*, thus locked-in, Chinese-speaking customers. Moreover, the most repeatedly used software functions by IM users are *text chat* (84.7%), *group chat* (66.4%), *document transmission* (65.8%), *audio chat* (49.9%), and *video chat* (46.1%). From this usage profile, we can see that the majority of users are presently locked into only the basic functions of IM. In addition, the positioning of IM as a web portal *platform* of is increasing prominently with the recent adoption of advanced email, blog and news related functions which have gained increasing popularity among users. (Internet world stats, 2008)

## COMPANY PROFILE

Tencent Holdings Limited, established in November 1998, is now one of the largest comprehensive internet service providers (ISP) in China serving over 400 million customers in the country. In the past decade, Tencent has been relentless in developing high value added products and services for its customers; such products include IM software, online games, portal site and other associated *value-add* products. The mission of the company is to enhance the quality of life through internet value added services.

Tencent has adopted “one-stop online service platform” as its strategic mantra by establishing four major services, namely: QQ IM, QQ Net, QQ Game and Paipai Net (the largest online C2C store in China). In terms of satisfying users’ needs in information transmission and knowledge acquisition, Tencent has added QQ Net, QQ IM, QQ Mail, and SOSO. In a determined effort to satisfy customers’ growing demand for group communication and resources sharing, Tencent launched QZone - now the biggest individual space in China--which has synergy with the frequently visited forums, chatting rooms and QQ groups. When it comes to meeting users’ demands in character shows and entertainment, Tencent owns successful virtual character products like QQ Show, QQ Pat、QQ Game and QQ Music/Radio/Live, it also provides wireless value-added services for mobile phone users. In respect of satisfying users’ transactions demand, Paipai Net, an e-commerce platform for C2C, is integrated with the community platform. By mid-2009, registered users of Tencent’s instant messaging QQ passed 1.06 billion, among which were more than 480 million active users and 100 million concurrent users. The concurrent users of QQ Game reached 86.63 million. The QQ Net became the number one comprehensive portal in page view. The Paipai Net became the second largest electronic commercial transaction platform.

Tencent’s marketing approach includes forward orientation, independent innovation and national brands creation. Normally, about 60% of Tencent’s personnel are working in an R&D capacity. The company has a considerable number of patents in instant messaging, e-commerce, online payment, searching engine, information security and games. In 2007, Tencent invested more than 100 million (US dollars) to establish China’s first Internet academy. The Tencent Academy, located in three major Chinese cities, nurtures independent innovation in core-Internet technologies. Innovation efforts have penetrated deeply into its development, operation, sales and other processes. Innovation is helping to drive its leadership in its core businesses.

Tencent’s vision is to be among the most respected global Internet companies. In line with this vision, the company has deemed social responsibility a priority and has been engaged in enhancing network civilization and welfare undertakings for many years. In 2006, Tencent set up the Tencent Charitable Foundation, which is the first charitable foundation established by a Chinese-run Internet enterprise. Tencent also established the Gongyi Net to help with adolescent education, poverty-stricken areas development, vulnerable group assistance and disaster relief and anti-poverty work. Recently, Tencent has also established several public welfare programs. Tencent dedicates itself to the harmonious society and to becoming an excellent corporate citizen. (Tencent, 1998)

By January 2010, the value of Tencent reached nearly US\$40 billion, which easily surpassed the market-value of both Yahoo and eBay (US\$20.34 billion and US\$28.17 billion respectively). In this industry, only Google with US\$145.12 billion surpassing Tencent ranking Tencent 2nd in NASDAQ network shares as summarized in Table 1. (Return From Tencent, 2007)

**Table 1: Milestones In Tencent’s History**

<b>Time</b>	<b>Event</b>
Nov .1998	Company formed
Feb .1999	Launched instant messaging service – QQ
Aug .2000	Launched mobile and telecommunication value-added services
Jun .2001	Launched Internet value-added services
Mar .2002	IM Registered Member exceed 100 million
Sep .2003	Launched QQ Game portal
Dec .2003	Launched portal website – www.QQ.com
Jun .2004	Listed on the main board of Hong Kong Stock Exchange (SEHK: 0700)
May .2005	Launched Qzone blog service
Oct .2005	Launched first self-developed MMOG
Mar .2006	Launched C2C platform Paipai.com and online payment solution Tenpay
Jul .2006	QQ.com became the most popular portal website in China
Mar .2008	Qzone active user accounts broke 100 million
Jun .2008	Became a constituent of Hong Kong's Hang Seng Index
Sep.2009	Launched self-developed search engine SOSO
Mar. 2010	QQ IM peak simultaneous online user accounts broke 100 million.

Source: <http://www.qq.com/>

## PRIMARY BUSINESS

Tencent's business-line includes these three broad product segments:

- Internet Value-Added Services (Internet VAS),
- Mobile and Telecommunication Value-Added Services (Mobile & Telecom VAS), and
- Online Advertising Services (Advertising)

Following the firm's "one-stop online living" strategy, the company further divides the Internet VAS segment into two smaller business lines: interactive entertainment service, and, e-commerce. As is typical in these industries, Tencent offers selected free of charge services in addition to its for-pay services. In just five years, Tencent has transitioned its focus from being primarily a mobile-telecommunications company to an Internet services company. The financial importance of Internet Services to the revenue stream increased markedly during the past 5 years and has doubled its contribution over the period from 38% to over 75% of the mix (Luk, 2010). Notably, while the relative contribution of mobile have reduced, the absolute contribution to revenues for mobile has increased 3-fold over this same period; the mobile business is still contributing. Nevertheless, over the same period, absolute revenues from Internet services have increased 20-fold. A number of renowned services provided by Tencent as well as the positions they hold in the Chinese internet market will be discussed below. Table 2 is the revenues contributed by each segment.

**Table 2: Financial Performance By Segment**

	Year ended 31 December 2009 ('000 RMB)					
Year	2004	2005	2006	2007	2008	2009
<b>Revenues</b>	1,143,533	1,426,395	2,800,441	3,820,923	7,154,544	12,439,960
<b>Internet value-added services</b>	439,041	786,680	1,825,343	2,531,728	4,914,974	9,530,711
<b>Mobile and telecommunications value-added services</b>	641,190	517,265	700,114	807,645	1,398,984	1,905,599
<b>Online advertising</b>	54,801	112,826	266,684	493,018	826,049	962,171
<b>Others</b>	8,501	9,624	8,300	6,532	14,537	41,479

Source: the annual report 2009 of Tencent

## CORE COMPETENCE ANALYSIS

In an effort to maintain and sustain its growth in the IM market, Tencent has been relentless in building its competence in innovation, efficient management and responsiveness to customers.

### Innovation

Information Technology (IT) is an innovation-driven industry; R&D capability is always a lively concern for management. Ma Huateng, the founder and CEO of Tencent, holds the opinion that the competition among online service providers will be fought within the battle ground of technological innovation. Accordingly, Tencent is ardent in aggressively developing and maintaining its R&D capability. Every year, Tencent will release several new versions of QQ and TM; since 2000, more than 265 different versions of QQ and TM have been released. In 2009, the source code of QQ2009 is completely rewritten, providing brand new services to customers. In addition, customers can also find the trend of new services in QQlab. (lab.qq.com). The company website is designed for introducing new concept and new product of Tencent.

Tencent is the only local internet service company that has built up a research institute. Since being established in January 2007, Tencent Research has shaped its strategy in three aspects: (a) engaging in basic and applied research, and enriching the next generation internet services; (b) advancing the technologies by tightly cooperating with colleges and universities in China, and; (c) recruiting and cultivating talents on Internet technology

research. The establishment of the institute cost more than 100million RMB and it ensure the structural arrangement of R&D to be relatively independent from the operation of Tencent. In July 2008, Tencent has more than 100 patents; however, by July 2009, it has more than 400 patents registered meaning 300 patents were approved in a single year. This impressive number ensures Tencent’s leading position in innovation among Chinese internet companies.

### Efficient Management

Tencent’s management efficiency was flatteringly demonstrated by its dynamic approach to maintaining a history of financial stability since its inception. As summarized in Table 3, in Apr 2000, IDG and PCCW each held 20% of Tencent’s share with US\$1.1 million investment. In June 2001, MIH group bought the 20% share from PCCW, and 13% share from IDG. In June 2002, MIH group bought 13.5% share from the Tencent initiative members. In 2003, the MIH group and Tencent initiative members rearrange the structure into 50-50. In June 2004, Tencent was listed in Hong Kong. The IPO results in the dilution of stock shares. MIH group and Tencent initiative members both hold 37.5% of the company. Also in 2004, the ABSA bank was introduced as a new Tencent’s shareholder.

**Table 3: Changes In Capital Structure From 2000 To 2009**

Year	Founder	IDG	PCCW	MIH	ABSA bank
2000	60%	20%	20%		
2001	60%	7%		33%	
2002	46.30%	7.20%		46.50%	
2003	50%			50%	
2004	37.5%			37.50%	
2008	11.85%			35.08%	10.30%
2009	11.66%			34.93%	10.25%

Source: the annual report 2009 of Tencent

Another dimension of Tencent’s management efficiency is its unwavering attention to hiring and maintaining a talented workforce. Ma Huateng says “for Tencent, business and capital are the most important things, business can be re-discovered and replaced, capital can be gathered or adjusted; however, talented people can never be easily substituted. Therefore, they are our most precious asset.” Tencent has developed its recruiting strategy in 2008, named “Great platform, Great Accomplishment”. The strategy is said to provide an open-ended salary structure for exceptional employees with no salary cap in place. During the hiring process, an individual’s values and responsiveness to customers’ need are closely evaluated. Tencent recruits people whose are both capable and willing to satisfy the needs of customers and to fully appreciate the value of each customer. In order to attract top technology students, Tencent holds competition for university and college students. The winners of the Tencent Innovation Contest (TIC) each receive a cash prize, free QQ membership, an internship at the company, and special opportunity to personally meet the top managers of the company, including CEO/Founder Huateng.

### Responsiveness To Customers

Listening and responding to customer needs is commonly-known to maintaining customer and software-user loyalty. Therefore, Tencent has managed to achieve its strong reputation for customer responsiveness by separating its business into various levels and accurate positioning.

#### 1. Separation of Business Levels

Tencent has successfully separated its business into two parts namely basic and value added services. *Basic Services* is widely applied to QQ IM as it attracts the huge group of users with high viscosity. *Value-Added Services* contains all the profiting services. The customers have various needs thus requiring different service levels to satisfy their demands. The needs of the internet users can be categorized into the following 3 groups: (1) the need is about the acquire and transmit of information, which can be satisfied by the basic internet service, (2) the need for

communication in group and the share of resource, and (3) the need to show individuality and to participate in interactive entertainment. By separating its business into 2 levels, Tencent is successful in satisfying its users with high dependency on the QQ platform.

2. Accurate Positioning

Tencent's users are typically young and energetic with age between 10 and 30 as its main target group. Products such as QQshow, QQgame, mobileQQ are clearly designed for young people. The QQ penguin trademark in Figure 1 and the visual identity design of Tencent services are obviously cute and focused on the interest of young people. Although the users between 10 and 30 may not be the richest, they spend lots of time on the internet and more willing to spend a small amount of money on things like QQshow and QQ game. If Tencent were to set its target on business or older users, the services would not have attracted so many users; also, the viscosity can never be as high as it is now. (Einhorn, Lee, & Aley, 2010)



**Figure 1: QQ Penguin Trademark**

**TENCENT’S INTERNATIONALIZATION**

**Im QQ**

To implement internationalization, Tencent launched its first English website, ImQQ.com, along with the English version of Tencent QQ for Windows Vista. Moreover, iPhone users can also download and use QQ on the phone. Allowing free download and installation enables Tencent to attract more international customers.

The website also did some adjustment to meet the style and taste of European and American users. Unlike most Chinese websites, ImQQ.com is simplified to an extent that gives the users a fresh and energetic impression and its strategy is summarized in Table 4. (International ambition of Tencent, 2009)

**Table 4: Im QQ Strategies**

Market Entry Strategy	Acculturation Strategy	Strategy to Attract Customers
<ul style="list-style-type: none"> <li>Free download to expand the user base</li> <li>Various versions for different users</li> </ul>	<ul style="list-style-type: none"> <li>“IM QQ” imitate Apple’s “I’M a MAC”, as well as Microsoft’s “I’M a PC”.</li> <li>The style of QQ English version is very simple which is in line with the aesthetic ideas of Europeans and Americans.</li> </ul>	<ul style="list-style-type: none"> <li>Emphasis that QQ is the world's most popular instant messaging software and has the world's largest online user base.</li> <li>QQ's slogan is “to contact with more than 300 million people online”</li> </ul>

Source: <http://www.tudou.com/programs/view/uGCYWknpG2o>.

## **QQ Game In US**

In February 2008, Tencent entered and launched QQ games the U.S market through partnership with AOL (American On-Line). QQ as a third-party provides the interactive services between friends among AOL Instant Messenger users. That position avoided direct competition with Windows Live Messenger, Yahoo Messenger and other mainstream instant messengers abroad. Three steps Tencent took to make the online games become international:

1. To stabilize domestic service. Tencent form a solid base in China as the starting point of internationalization as it provides technology, human resource as well as capital.
2. To internationalize games platform. By allying and purchasing leading companies abroad, Tencent tried to expand its game platform to overseas market. For example, Tencent purchase Foxmail and an Indian mobile game provider.
3. To develop international service content. Tencent developed an international version of the QQ game platform and actively look for partners to achieve Internationalization.

## **Steps In India**

In July 2008, Tencent signed a licensing and franchising agreement with MIH India as its first move into the Indian market. The agreement allows MIH to use some of Tencent's software applications and trademarks in India for seven years, while Tencent can buy up to 50% of MIH's equity via an option contract. This moving into India is an operative model for Tencent expansion into other developing countries in Asian so that it can take up market shares easier and build up competitive advantage.

Reasons that Tencent chose to forge into the Indian market are summarized as follows:

- The internet market in India is developing rapidly and the mode of development is similar with China. So it is helpful for Tencent to expand in India.
- Although there are a number of companies engaged in India's instant messaging market, their market share is not particularly large. This makes Tencent see the opportunity to enter the Indian market.
- Naspers Limited has shares in both MIH India and MIH China; meanwhile, MIH China is one of Tencent's major shareholders. Because of potential benefits, Tencent decided to expand its business in India.
- Like China, India is a populated country with a large number of Internet users. It is reported that currently India has 60 million Internet users and the growth rate is as high as 7.8% annually, the highest in the world. More importantly 65% of Internet users use instant communication tool. This is a good opportunity for Tencent to enter India's internet business using its outstanding IM software. (Trial in the Indian market-analysis on the internationalization of Tencent, 2008)

## **Taking Initiative In Vietnamese Market**

The characteristics of the Vietnamese Internet market are structurally similar to that of China. The potential user-base in both countries have a similar socio-economic structure (a prominent gap between the rich and the poor) as is well known in China. There are 20 million Internet-users in Vietnam, which equates to 25% of the total population. This ratio is similar to that of China and the market development and maturity of Vietnam is similar to China a few years ago. Therefore, Tencent bought over VinaGame and Tencent offers this company instant messaging software (QQ) and some recreational games. In 2007, VinaGame upgraded QQ and changed its name to Zing Chat and the penguin trademark was replaced by two ducks. By 2009, Zing Chat defeated Yahoo messenger in Vietnamese market and became the most popular instant messaging software with most users in Vietnam.

## **Developing Russian Market**

In 2010, Tencent took a significant step forward in its internationalization strategy by announcing a long-term strategic relationship with Digital Sky Technologies Limited (DST), a Russian network company. The two

companies announced that Tencent would invest US\$300 million which is Tencent's largest acquisition to date. (Tencent would invest DST 300 million dollars, 2010)

In the Russian market, the penetration rate of Internet and broadband is still relatively low; therefore, its potential for growth is fairly huge. Acquiring DST and moving into the Russian market follow the long term strategy of Tencent which is cooperating with local Internet companies to explore and capture the market potential. Tencent has a good start in the Russian market and will need some time to test its performance. (The Emerging Online Giant, 2010)

## CONCLUSIONS

Tencent's prosperity originates from its attention to its core capabilities and the execution of its aggressive strategies, as evident by its unqualified success in the Internet Messaging (IM) space. QQ IM has accumulated 400 million customers with strong brand loyalty which has further evolved into an intricate interpersonal relationship with millions of Chinese. Through this past decade of development, Tencent has been unwavering in its effort to reinforce its core competence of innovation, management efficiency and responsiveness to customers. Moreover, its aggressive international expansion has further strengthened its position as the largest IM platform in China with a global market ambition. The company continues to enjoy its prospects for exponential growth by way of continued expansion within China and by opportunistic international acquisition.

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**NOTES**