

**60 Minutes Episode: "The Cleantech Crash", shows how Silicon Valley Sends American technology to China Through Covert Pump-and-Dumps the same way it did with Russian mobsters**

**China is flooding Silicon Valley with cash.  
Here's what can go wrong.**



An employee is seen behind a glass wall with the logo of Alibaba at the company's headquarters on the outskirts of Hangzhou, Zhejiang province. (© Chance Chan / Reuters/REUTERS)

By [Elizabeth Dwoskin](#)

SAN FRANCISCO — Mountain View, Calif., start-up Quixey was the envy of many in Silicon Valley when the company announced a multimillion-dollar investment from one of China's largest and most powerful technology companies, Alibaba.

The \$110 million deal — parceled out over two funding rounds in 2013 and 2015 — was the latest evidence that deep-pocketed Chinese investors would pay premium prices to get a stake in the region's hottest young companies.

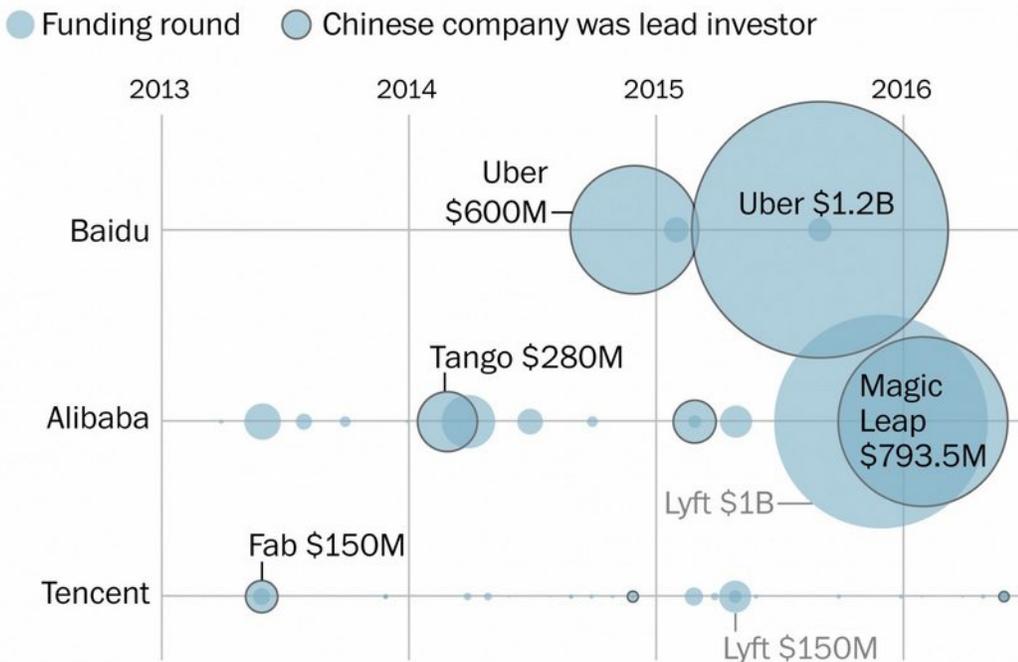
But then, something went very wrong: Alibaba stopped paying, according to people familiar with the matter. The start-up was left in the lurch, until Alibaba fired back with a hard bargain: We'll give you a loan and you must promise not to sue. After a few breathless months of negotiations, Quixey went through with the new deal. The company said Thursday it had borrowed \$30 million. Those funds came from Alibaba and others under terms that were worse than the original arrangement, the people said.

At the heart of the bitter, under-the-radar dispute between China’s online shopping powerhouse and Quixey, whose tech enables users to search within apps, is a culture clash — one that is emblematic of both the promises and the perils involved in Silicon Valley’s relationship with China. Experts say that relationship — always delicate, always mind-bogglingly complex — has reached a new inflection point, as unprecedented amounts of cash from China have poured into Silicon Valley.

The flood has had a profound effect on the region’s start-up boom. Over the past two years, Internet giants such as Alibaba, Baidu and Tencent — sometimes referred to as the Amazon, Google and Facebook of China — as well as dozens of private investors, family offices, local municipalities and state-owned enterprises have raced to capture a stake in the region’s cutting-edge technologies.

## China is flooding Silicon Valley with cash

In recent years, Chinese companies have invested heavily in U.S. start-ups. Here are some high-profile deals involving Baidu, Alibaba and Tencent, often referred to as the Google, Amazon and Facebook of China.



Source: CrunchBase

DARLA CAMERON/THE WASHINGTON POST

Investment from China into Silicon Valley, excluding real estate, topped \$6 billion by the end of the first half of 2016, with more than half of that spending taking place in the past 18 months, according to the Rhodium Group research firm. Investors have been spurred by China’s growing wealth over the past decade and a government push to develop innovative technologies — particularly in areas such as virtual reality and artificial intelligence, where China still lags.

“China realizes it needs a role model to follow as the country is transitioning from manufacturing to innovation,” said Shoucheng Zhang, a celebrated Stanford physicist who started a \$350 million venture capital firm two years ago to capitalize on the boom. “This is the new digital Silk Road.”

U.S. start-ups, for their part, are hungrier than ever for access to China's cash-rich companies and newly minted millionaires, especially in light of a tighter fundraising environment in Silicon Valley. Chinese investors also can open doors to China's billion-plus consumers for services and products that are facing a saturated market in the United States.

Such investments can alter the trajectory of a nascent company. "Start-up fundraising in Silicon Valley wouldn't function without Chinese money," said Chris Nicholson, chief executive of two-year-old artificial intelligence company Skymind.io, which has received funding from Tencent and other Chinese investors. Start-ups that have been rejected from the clubby venture capital world on Sand Hill Road can still get cash from China, he said. "It has changed the landscape."

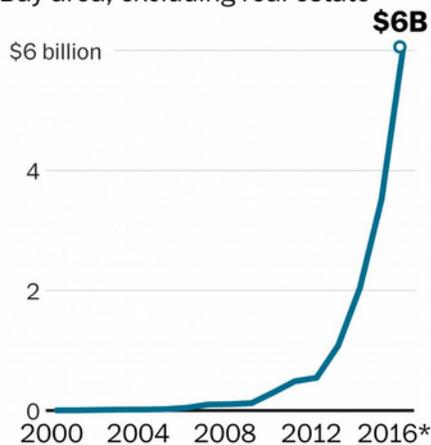
But there is also distrust on both sides. U.S. start-ups are wary of hardball tactics and the power that some Chinese players have come to exert. Some have raised concerns about their innovations being copied, which has been a long-standing concern for many U.S. corporations partnering with Chinese firms. As newcomers, Chinese investors don't want to be disrespected or treated as naive, or as so-called dumb money, according to executives who work closely with them.

In interviews, U.S. entrepreneurs said that Chinese investors often play by unfamiliar rules. Quixey learned that the hard way.

Shortly after the company got its first round of financing from Alibaba in 2013, Quixey began doing custom work for the Chinese conglomerate under a separate contract, building specialized technology that would enable Chinese consumers to search inside Chinese apps in Alibaba's operating system, YunOS. (Searching within apps is very different, technologically speaking, from searching on the Web; even Google has failed to crack the problem.) The deal stipulated that Alibaba and Quixey would share revenue from any profits Alibaba made off using the company's technology in China, according to people familiar with the matter who spoke on the condition of anonymity to talk freely about private events.

## Chinese capital has poured into U.S. tech firms

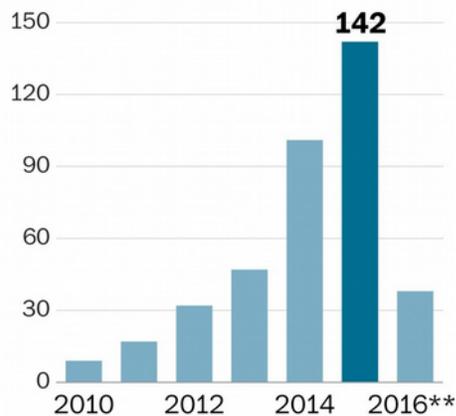
Cumulative Chinese direct investment in the San Francisco Bay area, excluding real estate



\* Through June 30.

Sources: CBInsights, Rhodium Group

Estimated number of tech deals involving Chinese investors



\*\*Through May 19.

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By early this year, a dispute had arisen. Alibaba claimed that the start-up had fallen behind on its deliverables; Quixey claimed that Alibaba owed the company tens of millions of dollars for work rendered for several months, the people said.

Meanwhile, the expected revenue from Alibaba's distribution in China never came, according to one of the people. Alibaba became frustrated that Quixey wasn't diversifying its revenue streams, another person said. At the same time, Alibaba went through a large organizational shake-up, and start-ups that attempted to work with the company, including Quixey, felt they were getting bounced around by a dizzying array of politics and priorities, several people close to the matter said. The problem was compounded by language barriers, they added.

Quixey considered suing Alibaba, but decided it wouldn't be worth it, the people said. Few start-ups can afford a costly lawsuit against their main customer and investor. The tumult led to missed revenue targets and the departure of key executives, while the company's founder stepped down as chief executive.

"We do, of course, value our relationship with Alibaba — they've been an integral partner and investor," said Quixey spokesman Scott Samson. He declined to comment further.

Alibaba declined to comment, citing a policy of not discussing current investments.

Quixey aside, many investors said the Silicon Valley-China relationship, while full of opportunity, is also rife with cultural misunderstandings. Many partnerships fall through as a result, said Jay Eum, managing director at TransLink Capital, a Palo Alto, Calif.-based early stage venture capital firm that specializes in helping start-ups work with Asian technology conglomerates. (Eum's firm is an investor in Quixey, but he said he was speaking generally.)

“While the promise of a China partnership is exciting and looks good on paper, the actual reality requires trade-offs,” Eum said.

In China, where there’s less rule of law, a powerful government relentlessly pushing for growth, and enormous competition among companies, brass-knuckled business tactics are more common, said Thilo Hanemann, an economist at the Rhodium Group.

“Sometimes these tactics are not misunderstandings but reflections of cultural norms of how business is conducted in China. The Chinese investor may ask for terms that would be considered overly aggressive in Silicon Valley, but these terms would be considered fair in China,” said Connie Chan, a partner with the venture capital firm Andreessen Horowitz who focuses on China.

It’s not uncommon, for example, for an investor to take ideas from one start-up and then turn around and invest in a rival, experts said.

Nicholson, the Skymind.io chief executive, said many U.S. start-ups cannot afford to walk away from a bad deal. “As a founder, your job is to keep your baby alive, so you can’t always afford to ask too many questions when someone comes along with terms that might not be perfect,” he said, while emphasizing that his own experiences with Chinese investors had been extremely positive.

Overall, entrepreneurs and investors said Chinese investment had opened many new doors. For CloudFlare, a Web performance and security start-up that had pulled out of China in 2011, an unusual partnership with Baidu in 2015 put the company’s technology in the hands of millions of Chinese consumers. For Artsy, an online art marketplace, investors from China helped the company grow its market in Hong Kong. Magic Leap, a virtual reality darling that received a large investment from Alibaba this year, was invited by Alibaba to give a keynote presentation in front of hundreds of Chinese engineers at the conglomerate’s Maker’s Fair in Shanghai.

Chinese investment in Silicon Valley stretches back at least three decades. But 2014 is considered a tipping point. That year, deals began to rev up in a big way: Chinese investors took part in 101 deals — more than triple from two years earlier, according to the research firm CBInsights. The actual number is likely to be larger since many investments aren’t made public.

Like the U.S. real estate industry and the bond market, Silicon Valley has been the target of growing classes of Chinese uber-rich who are looking for opportunities to grow their wealth outside the country. Recent instability has pushed money out of the country even more quickly, according to Rhodium.

Alibaba’s spending spree has included \$795.5 million in Magic Leap, \$500 million in the e-commerce site Jet.com, along with unspecified multimillion-dollar investments in Snapchat, ride-hailing service Lyft and e-commerce start-up Shoprunner. Last year, Baidu led a \$1.2 billion fundraising round in Uber and put the finishing touches on a glossy new Silicon Valley campus — a move intended to anchor the company’s growing number of investments in the region and attract engineering talent that is still hard to come by in China. Tencent, which owns WeChat, the most popular messaging application in China, has a quieter presence, investing small amounts in hundreds of companies and vetting technologies in the areas of gaming, mobile money and artificial intelligence.

“We’re looking at companies that provide strategic value to us — and building cool new technology for the China market,” said Alex Tze-Pin Cheng, general manager of Baidu U.S. Like other Chinese investors, Baidu has developed ties to the influential venture capitalists on nearby Sand Hill Road, Cheng said.

Fyusion founder Radu Rusu, whose recent deal will put his company’s 3-D photography technology on millions of Huawei smartphones, said the arrangement would be transformative for his 40-person start-up. Like other founders who had Chinese investors, he said it was remarkable how quickly a deal went down. “Definitely much faster than any U.S. company I’ve dealt with,” Rusu said. “They were very aggressive — like there’s no time to waste.”

In the near term, Quixey and Alibaba are patching up their disagreements. The start-up has built new technology to search within apps and is talking to a fresh set of potential customers and partners, people familiar with the matter said.

Quixey is no longer building technology for Alibaba.

Elizabeth Dwoskin is The Washington Post's Silicon Valley Correspondent.

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