Greater China Private equity briefing

3Q 2021

October 2021

Building a better working world

This briefing offers you a roundup of the private equity deals and fundraising in the last quarter (3Q 2021). It also covers the trends that are shaping investment decisions today.

It distills the perspectives of the teams of subject-matter professionals in the region into pertinent insights to keep you ahead in navigating the private equity landscape.

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1 Executive summary

The private equity (PE) market in the Greater China region is compelling for investors looking to capitalize on the region's growth. Despite the global economic disruption, China posted a GDP growth of 2.3% in 2020. Moreover, its private capital sector has total assets under management (AUM) of US$1.3t, which is expected to expand further with proactive government efforts to strengthen regulatory frameworks and establish a formal financial system.

The Greater China region is becoming increasingly accessible to private investors:

- The introduction of Foreign Investment Law, Catalogue of Encouraged Industries, and the launching of various free trade zones provided attractive ways for foreign investors including PE to access the broader fast-growing industry sectors.
- Hong Kong's Limited Partnership Fund Ordinance adopted in Aug 2020 has facilitated the establishment of funds onshore in Hong Kong in the form of limited partnerships. This is expected to boost Hong Kong's standing as an asset management and PE investment centre in Asia. In addition, the Hong Kong SAR government has introduced the tax concession regime for carried interest in early 2021 to enhance attractiveness to PE investors.

However, while the PE opportunities abound, China's changing regulations on a few industries as well as the impact on Chinese companies to list on overseas stock exchanges are critical challenges industry players face.

In 3Q 2021, the region witnessed:

US$5.6b

capital commitments across 14 closed funds*

US$16.1b

capital deployed across 140 announced PE deals

US$4.8b

realized capital across 11 PE-backed exits

Thematic opportunities for PE include:

- 5G, AI, chips and cloud
- Pharma and HealthTech
- E-commerce, internet retail
- Advanced and green manufacturing

Notes: *Analysis includes PE funds which are closed, fully invested, liquidated or in the divestment phase. It includes funds with an investment mandate to deploy capital in the Greater China region.
Source: AVCJ, EY analysis

Key emerging themes impacting Greater China's PE landscape include:

1 The new regulations launched by Chinese Government has undermined business model of certain industries and suspended overseas listings by domestic companies.

In Jul 2021, the Cyberspace Administration of China (CAC) proposed draft rules calling all data-rich tech companies with over one million users to undergo security reviews before listing overseas. Chinese regulators' scrutiny and new legislation could be a headwind for companies attempting to list on overseas stock exchanges and will likely push more high-profile offerings onto domestic and Hong Kong-based exchanges. Concurrently, U.S. Securities and Exchange Commission ("SEC") has required Chinese issuers to disclose material risks related to their operations in China, further adding complexities and creating uncertainty over exit timelines.

Notably, the Hong Kong Exchange (HKEx) has outlined rules for IPOs by Special purpose acquisition companies ("SPACs") and Beijing opened new Stock Exchange ("Beijing Stock Exchange") to be a major base serving innovative small and medium sized enterprises. Both provide alternative exit opportunities to PE portfolio companies in the region.

2 Investors expected to shift focus to sectors less prone to regulatory impact and identify opportunities in the sectors that are aligned with China's regulations

Technological innovation is in the spotlight of the 14th Five-Year Plan (2021-25). Investors are expected to shift focus to the core technologies, covering key sectors such as semiconductors, 5G applications, the Internet of Things, and autonomous driving.

3 China's blueprint for national development is pushing Environmental, Social Responsibility and Corporate Governance ("ESG") into the mainstream investment focus

In 2020, China announced its climate targets to be carbon-neutral by 2060. According to BNP Paribas, to achieve the goal of economic transformation to sustainable development, an investment of approximately US$247-468b will be required each year, and 90% of the capital may be from the private sector.

4 Artificial intelligence/machine learning (AI/ML) and 5G expected to garner continued PE interest in the region

The ubiquity of mobile payment systems and the advent of advanced digital infrastructure have paved the way for companies focused on next-generation technologies such as 5G and AI/ML. According to GSMA Mobile Economy Report 2021, Greater China alone will account for nearly half of the total 5G connections (48%) by 2025, way ahead of the global average of 21%.

Stella Yuan
EY Greater China Private Equity Leader

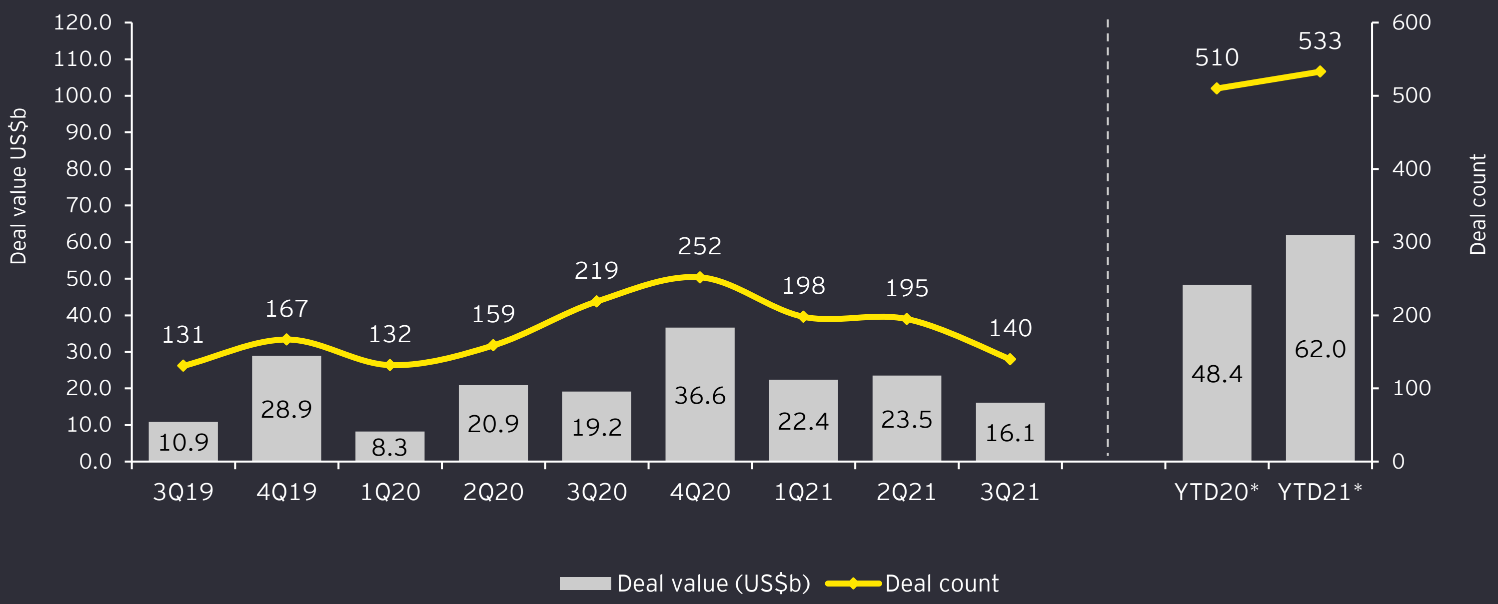
"During the 14th Five-Year Plan period, China will accelerate the establishment of a new development pattern of "dual circulation", where domestic and foreign markets can boost each other. We believe that China will further push forward opening up, which is compelling for PE looking to capture the growth of domestic demand and create value by technology and innovation. To attract international long-term capital, Hong Kong and Mainland China continue to innovate and have already been releasing a raft of favourable policies to strengthen their attractiveness as both PE fund hubs and investment destination.

Source: AVCJ, EY analysis

2 Investments

- PE invested US$62.0b across 533 deals throughout Greater China in YTD21*.
- Aggregate deal value[1] increased 28% from US$48.4b from YTD20*, while volume increased by 5% from 510 deals.
- The average deal size[1] witnessed an increase of 31% to US$175m in YTD21* from US$134m from an year ago.
- Technology remained the preferred sector for investments, garnering 49% of the total deal volume and 50% of the total deal value.[1]
- Many investors are now shifting focus to sectors that are less vulnerable to regulatory and policy changes, such as semiconductors, automation, sustainable products, etc.
- The region could witness increased investments in ESG-linked assets. The government is working towards increased sustainability efforts.
- Recently the China government committed to achieving complete carbon neutrality by 2060 and, in the 14th Five-Year Plan, it has set a target to reduce carbon dioxide intensity by 18%, thereby providing the private sector with significant opportunities to invest in clean energy and e-mobility.

Figure 1: PE investment activity



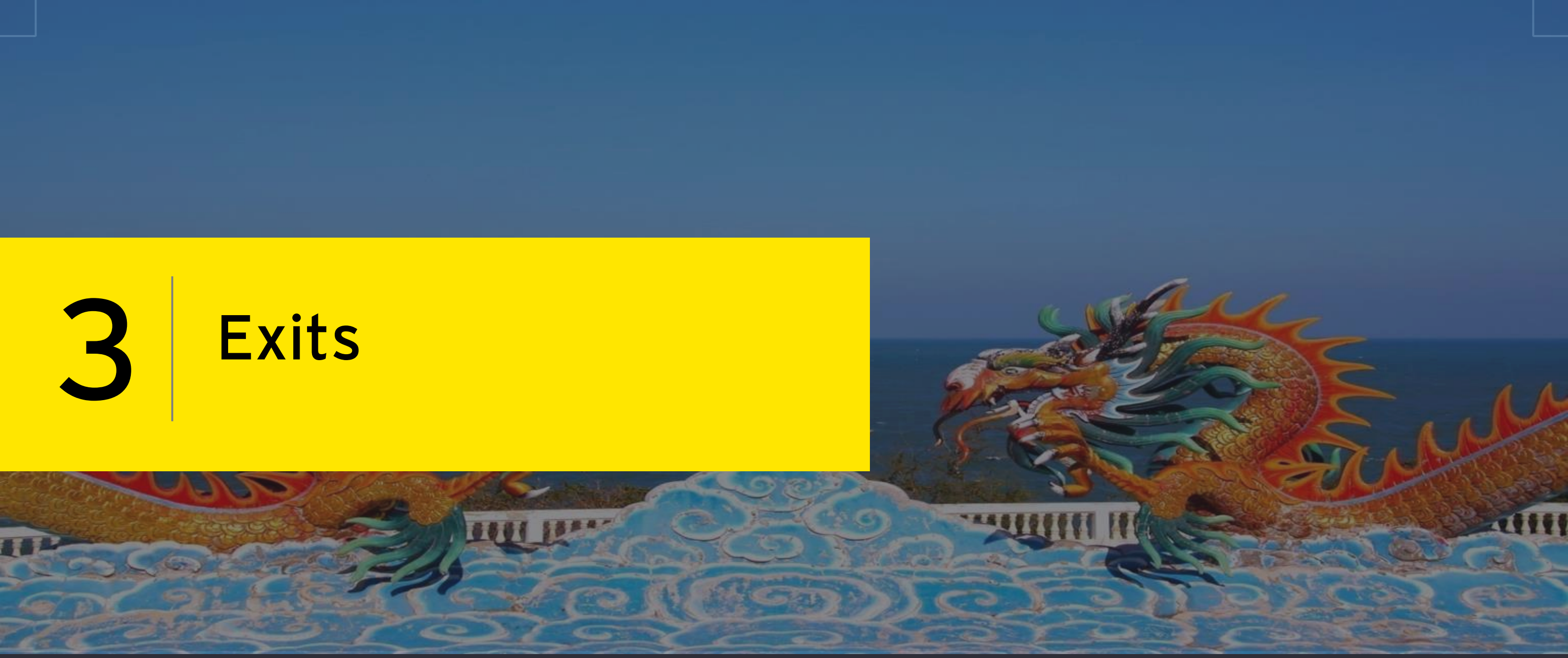
Note: [1]Deal value was disclosed for 354 of 533 announced PE transactions in YTD21; and 361 of 510 announced PE transactions in YTD20; *YTD21 refers to the period from Jan 21 – Sep 21, YTD20 refers to the period from Jan 20 – Sep 20.

Source: AVCJ, EY analysis

Table 1: Top PE investments announced in 3Q21 (by deal value)

Investment date	Company	Country	Sector	Value (US$m)	Investors
Jul 2021	SVOLT Energy Technology	China	Technology	1,586.1	IDG Capital Partners; Bank of China; China Renaissance Holdings; Country Garden VC*
Jul 2021	Suning.com	China	Consumer	1,363.3	Hainan Jilida Investment
Jul 2021	CICT Mobile Communication Technology	China	Technology	926.9	CCT Fund Management; CDB Capital; Guangzhou Yuexiu Financial; HuBei Science & Technology Investment; Unicom Capital*
Jul 2021	FTX Exchange	Hong Kong	Technology	900.0	Altimeter Capital; Coinbase; Insight Partners; Paradigm; Ribbit Capital; Sequoia Capital; Sino Global; Thoma Bravo*
Aug 2021	Beijing Zhendong Langdi Pharmaceutical	China	Healthcare	895.4	FountainVest Partners
Aug 2021	Suzhou Abogen Biosciences	China	Healthcare	700.0	5Y Capital; AIHC Capital; BioTrack Capital; Boyu Capital; Everbright; Gaorong Capital; Hillhouse Ventures*
Jul 2021	LeapMotor	China	Technology	694.6	CICC Capital Management Co.
Sep 2021	Hangzhou Youxing Technology Caocao Chuxing/Caocao Zhuanche)	China	Technology	588.9	ABC International; Dongwu Innovation; Suzhou High Speed Rail New City State-owned Assets Holding*
Sep 2021	Hangzhou Semiconductor Wafer	China	Technology	511.4	BOCOM International Assets Management; CCB International; China Cinda Asset Management; CICC*
Jul 2021	HeyTea	China	Consumer	500.0	BA Capital; Dayone Capital; Hillhouse Capital Management Group Ltd.; L Catterton Asia; Sequoia Capital China; Temasek; Tencent*

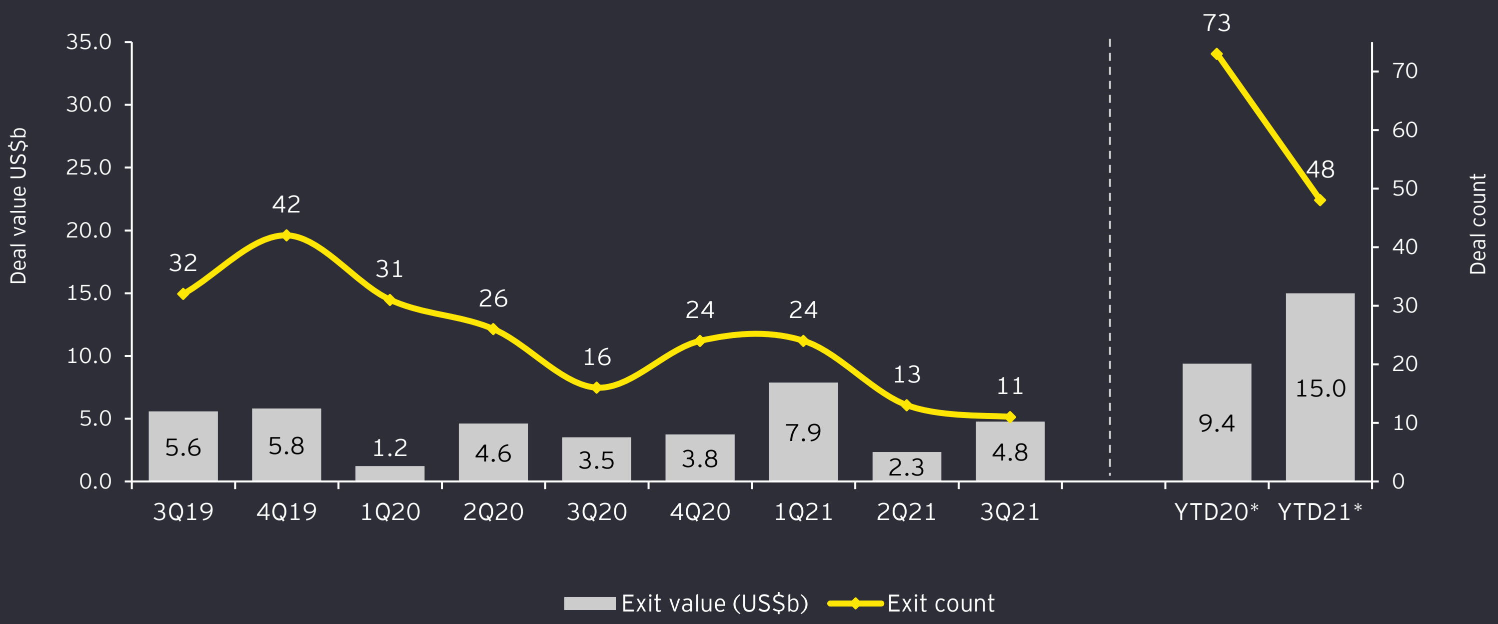
Note: *Includes co-investment from other PE firms.
Source: AVCJ, EY analysis



3 Exits

- PE exited 48 assets worth US$15.0b in YTD21* throughout the Greater China region.
- Aggregate exit value[1] increased 60% from US$9.4b to YTD20*, while volume fell by 34% from 73 deals.
- The average exit size[1] witnessed an increase of ~2.7x to US$417m in YTD21* from US$165m from an year ago.
- In the largest exit of YTD21*, RRJ Capital and Joy Orient Investments along with other investors, sold their US$2.1b stake in China Logistics Property Holdings Co. to JD.com.
- The technology and healthcare sectors offered remarkable opportunity to realise value and together garnered a share of 52% of exits volume during YTD21*.
- During YTD21*, sale to strategic acquirers dominated the exit activity (82% of total number of exits), followed by secondary sale.
- Cyberspace Administration of China have proposed new regulations that would require all data rich tech firms with over one million users seeking to list in overseas stock exchanges to undergo a cybersecurity review. This is expected to deter portfolio companies looking to exit via IPO route by listing on overseas stock exchanges
    - This move is expected to re-route the PE-backed IPO listing plans of some China-based portfolios to domestic stock exchanges.
- The uncertainty over exit timeline remains. Notably, the Hong Kong Exchange (HKEx) has outlined rules for IPOs by SPACs and Beijing opened new Stock Exchange to be a major base serving innovative small and medium sized enterprises. Both provide alternative exit opportunities to PE portfolio companies in the region.

Figure 2: PE exit activity



Note: [1]Exit value was disclosed for 36 of 48 announced PE transactions in YTD21, and 57 of 73 announced PE transactions in YTD20; *YTD21 refers to the period from Jan 21 - Sep 21, YTD20 refers to the period from Jan 20 - Sep 20.

Source: AVCJ, EY analysis

Table 2: Top PE-backed exits announced in 3Q21 (by deal value)

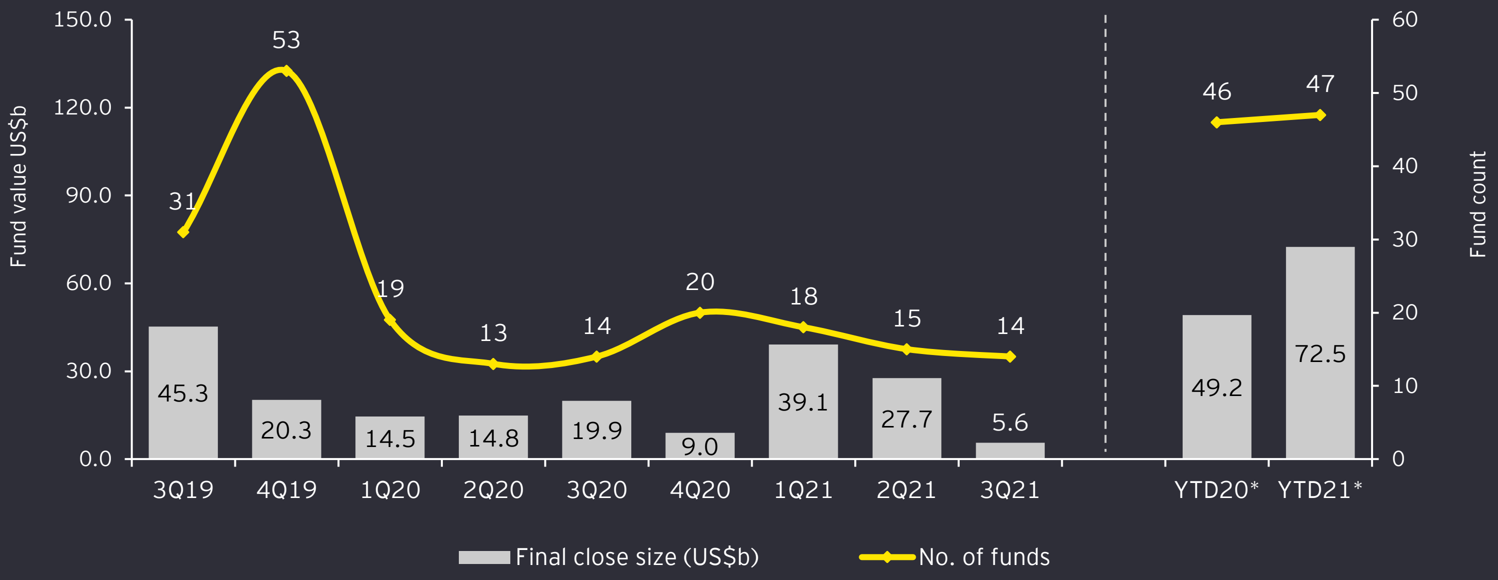
Exit date	Company	Country	Sector	Value (US$m)	Sellers	Type
Sep 2021	China Logistics Property Holdings	China	Mobility	2,105.8	RRJ Capital; Joy Orient Investments *	Trade sale
Aug 2021	Pico Technology	China	Technology	1,384.3	CCB International; CM Capital; Co-Stone Capital*	Trade sale
Aug 2021	Inner Mongolia Yitai Chemical	China	Advanced manufacturing	324.1	Juxin Taifu (Shenzhen) Fund Management	Trade sale
Aug 2021	Suchuang Gas	China	Power and utilities	316. 4	Prax Capital; Shanghai Dazhong Public Utilities	Trade sale
Jul 2021	Jiangsu Suote Electronic Material	China	Technology	192.5	Haitong Capital; Shenzhen Oriental Fortune Capital; V-Capital*	Trade sale
Jul 2021	Suzhou GCL New Energy Investment	China	Power and utilities	188.3	Sumin Investment	Trade sale
Jul 2021	Shanghai Xinjiangwancheng Investment Development	China	Financial services	136.4	Shanghai Dinghuitong Equity Investment Management	Trade sale
Aug 2021	DeepMotion (Beijing)	China	Technology	77.4	Redpoint China Ventures; Source Code Capital	Trade sale
Jul 2021	Shenzhen Ruiling Wireless Technology	China	Telecommunication	40.7	Shenzhen Capital Group; Shenzhen CCB Huaxun Equity Investment Fund Management	Trade sale

Note: *Includes other co-sellers.
Source: AVCJ, EY analysis

4 Fundraising

- Fundraising activity came roaring back in 2021, as economies reopened and healthcare crises started to stabilize.
- Greater China-focused funds raised an aggregate amount of US$72.5b across 47 funds during YTD21* as compared with US$49.2b across 46 funds in YTD20*.
- The average fund size increased 44% to US$1.5b in YTD21*from US$1.1b in YTD20*.
- The region witnessed the final close of 13 mega funds (more than US$1b) during YTD21* compared with seven mega funds in YTD20*.
  - US-based KKR achieved the final close of its KKR Asian Fund IV, with a close size of US$15.0b, and a mandate to invest in the APAC region.
  - China-based Boyu Capital achieved a final close of its Boyu Capital Fund V, with a final close size of US$6.0b.
- Regulatory developments in the PE space in the region ensure that Hong Kong SAR remain a leading jurisdictions for offshore funds to establish their regional platforms.
- In Feb 2021, Hong Kong set forth a legislative framework for granting concessionary tax treatment to carried interest received by or accrued to PE fund managers and their employees. This move would create the right conditions to encourage increased critical mass in the onshore PE funds industry, and to develop Hong Kong as a premier PE fund hub in the region.

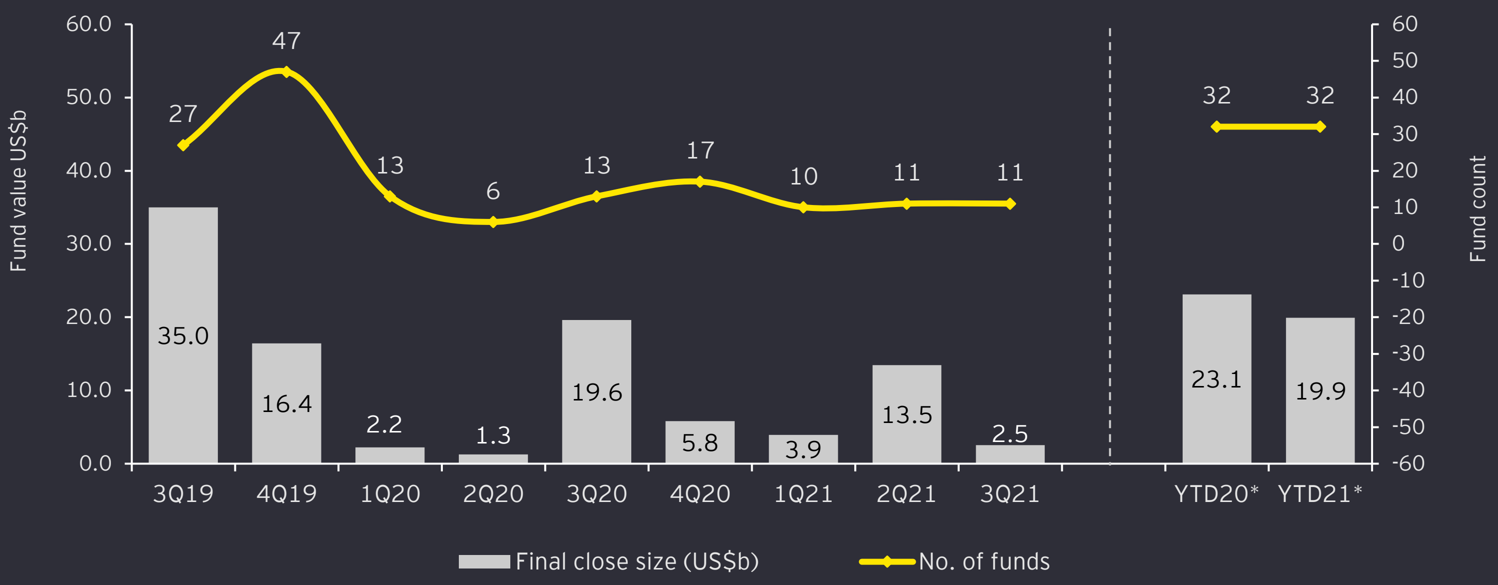
Figure 3: PE fundraising activity



Note: Analysis includes PE funds which are closed, fully invested, liquidated or in the divestment phase. It includes funds with an investment mandate to deploy capital in the Greater China region; *YTD21 refers to the period from Jan 21 - Sep 21, YTD20 refers to the period from Jan 20 - Sep 20.

Source: AVCJ, EY analysis

Figure 4: PE fundraising activity by Greater China-based fund managers



Note: Includes closed and liquidated funds, managed by Greater China-based fund managers with an investment mandate to deploy capital in the Greater China region.

Table 3: Top funds closed in 3Q21 (by final close size)

Fund name	Final close date	Manager	Final close size (US$m)	Industry focus
Apax Digital Fund II	Sep 2021	Apax Partners	1,750.0	Technology
Navis Asia Fund VIII	Jul 2021	Navis Capital Partners	900.0	Diversified
Dayone Capital Fund I	Aug 2021	Dayone Capital	630.0	Consumer
Guangxi New Hope Live Pig Guarantee and Supply Special Industrial Fund	Aug 2021	Guangdong New Hope New Agricultural Equity Investment Fund Management	615.2	Consumer
PAG Growth II	Jul 2021	PAG Capital	525.0	Diversified
Navis Asia Green Loop Fund	Jul 2021	Navis Capital Partners	450.0	Diversified
Ningbo Kangjun Zhongyuan Equity Investment Partnership	Sep 2021	Bayland Capital	216.9	Healthcare
Chongqing BOE Smart Private Equity Investment Fund Partnership	Sep 2021	Guoke BOE (Shanghai) Equity Investment Management	154.6	Technology
Taizhou Jinli New Energy Equity Investment Fund	Sep 2021	Jiangsu Jolmo Investment Management	146.1	Technology
Jining Huisheng Industrial Investment Partnership	Sep 2021	Hangzhou Huahong Guotai Investment Management	77.5	Power and utilities

Note: *YTD21 refers to the period from Jan 21 - Sep 21, YTD20 refers to the period from Jan 20 - Sep 20.
Source: AVCJ, EY analysis

5 How PE could evolve in Greater China amidst the new regulatory changes?

In the past few months, several regulations have been passed by Chinese regulatory bodies to govern the economy, including placing restrictions on certain industries such as private education, conducting cybersecurity reviews of China-based companies to be listed on overseas stock exchanges, and launching antitrust scrutiny of investments made by internet giants. PE have responded by realigning their strategies and aligning their investment mandate to the policy changes.

Despite the challenges and uncertainties presented from the pandemic and regulatory scrutiny, as a key part of China's "dual circulation" strategy, China will further push forward opening-up and focus on quality growth, which still favour PE assets in the region for higher quality growth, better governance structures, and value enhancing opportunities.

The introduction of Foreign Investment Law, Catalogue of Encouraged Industries, and the launching of various free trade zones provided attractive ways for foreign investors including PEs to access broader and fast-growing industry sectors.

- New sectors of focus emerge:
  - In Apr 2021, both the China Securities Regulatory Commission (CSRC) and the Shanghai Stock Exchange released guidelines to emphasise their interest in attracting companies with 'hard technology' and helping them go public. Hard technologies mainly include areas such as new materials, new energy, aerospace, biotechnology, advanced manufacturing, and integrated circuits.
  - Within Catalogue of Encouraged Industries, China allowed foreign investments in new sectors such as AI, 5G technologies, blockchain, and automation services, thereby opening the door for more foreign PE investment to spur its economic growth.
- New regulations aim to improve transparency and trust for limited partners (LPs) while investing in PE funds or deals:
  - With the enforcement of a Merger Clearance Review in PE/VC deals, State Administration for Market Regulation (SAMR) now requires the transacting parties acquiring a minority stake to file a declaration for merger clearance review in accordance with the law.
  - CSRC recently stressed that PE in China should focus on its original purpose of supporting innovation and start-ups. CSRC is expected to crack down on fake funds that are promoted to the general public, tighten scrutiny of fundraising and probity within PE funds, and generally exercise firmer control of the industry.
- Expanded implementation Of Qualified Foreign Limited Partnership (QFLP) might heat up foreign equity investments in China:
  - In May 2021, the Shanghai government improved its QFLP scheme to encourage QFLPs to manage domestic Renminbi funds, to invest in shares of unlisted domestic companies, and to participate in private placements by listed companies.
- Hong Kong to emerge as an attractive PE hub:
  - Hong Kong's Limited Partnership Fund Ordinance adopted in Aug 2020 has facilitated the establishment of funds onshore in Hong Kong in the form of limited partnerships. Hong Kong has introduced the tax concession regime for carried interest in early 2021 to enhance attractiveness to PE investors. These are expected to boost Hong Kong's standing as an asset management and PE investment centre in Asia.
  - Due to suspension of domestic companies in US, Hong Kong stock exchange will replace US as the primary listing choice. Hong Kong has also propose listings by SPACs which provide an alternative exit route for PE backed portfolio.

Source: EY analysis

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