

Hong Kong Venture Capital and Private Equity Industry Backing Asian Business into the Future.

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Despite the exciting growth of domestic private equity markets in Australia, Korea, PRC, Japan and India over the past five years, Hong Kong is still home to the largest available pool of capital for private equity investment in the Asia Pacific region. As with many other financial institutions in the region, Hong Kong still remains the place of choice for regional head offices of private equity firms. As of June 2003, there were 176 Hong Kong based funds with Capital Under Management of US\$26.6 billion. These funds employed approximately 700 investment professionals based in Hong Kong*. Historically, over 90% of investments made by Hong Kong based private equity firms were invested in Australia, Singapore, India, PRC, Korea and Japan.

Over the past ten years, the industry throughout the Asia Pacific region has grown to a total of approximately \$100 billion funds under management, a ten-fold increase over this period. It has grown from the one asset class (ie development capital) to the full range of private equity covering buyouts, technology, development capital, mezzanine and distressed debt. This has been due to the restructuring post the financial crash of 1997, the rapid recovery of the Asian economies and the many positive reforms made to Asian capital markets since 1997. Clearly these reforms need to continue in order to further allow capital markets to become more efficient and transparent. Providing we do not see a return to the pre-1997 days of uncontrolled and wasteful bank lending, the private equity business in Asia can look forward with growing confidence that it does indeed have a significant role to play as a provider of new investment funds to the region.

Initially the industry was concentrated in Hong Kong and Singapore with investments made throughout the Asia Pacific region. The past five years has seen a sharp rise in the number of large leveraged buyout transactions completed in Australia, Korea, and Japan. Domestic banks in these markets have embraced the concept of non-recourse lending to financial buyers on terms and conditions in line with international practice. In addition we have seen some large development capital and technology related transactions in India and the PRC. As a result of this activity, strong domestic funds have emerged in these countries and now present solid competition to the regional funds, the majority of which are based in Hong Kong.

The evolution of private equity in these five large economies has been the turning point for private equity in the Asia Pacific region. The industry has shown that financial buyers can compete with corporate buyers in competitive auction processes. Best practices and processes from European and US private equity markets have been successfully imported into Asia. There is now a firm belief among firms that the private equity business has a long way to grow in the Asia Pacific region.

Furthermore, recent exits of large MBO's in Korea, Japan and Australia are finally demonstrating that private equity firms can make excellent returns in Asia Pacific. Shinsei Bank in Japan, Koram Bank in Korea and Pacific Brands in Australia are recent examples of multi- billion dollar disposals by private equity firms. This is also true of development capital deals in the PRC and India where excellent returns have been made. This has resulted in a better environment for fundraising for Asia Pacific Funds. At this time last year, investment from the US and Europe into Asia Pacific Funds had slowed to a trickle, however it has increased sharply since the end of last year and is now buoyant. US and European pension funds are reassessing their appetite for Asian Pacific Private Equity and domestic life companies, particularly in Australia and Japan, are committing more allocation to private equity. Should this trend of increased supply of institutional money continue, growth in the private equity industry is all but assured.

In summary the future of Private Equity in Asia Pacific looks promising. Hong Kong as the main hub in Asia, is well placed to take a leading role in this dynamic growth. The challenge for Hong Kong will be in maintaining its leadership in the region as the industry evolves with the markets, which it will invariably do. As markets grow or regulations change in Australia, Korea, Japan, India and the PRC, there will be the danger that the larger private equity firms will relocate to one of their most active markets. Thus I believe that Hong Kong private equity firms need to develop their investment sourcing and investment capabilities for the huge PRC market and take a leading role in the growing private equity market in China. This presents a huge opportunity for Hong Kong based private equity firms as the industry in the PRC has only just started and is set for take-off. Only by developing a strong domestic business into China and at the same time maintaining its regional hub status, can HK retain its leading position in Asia Pacific Private Equity.

* Source - AVCJ