China GPs emphasize consumer sector opportunities
AVCJ
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Policy volatility in China has prompted many investors to eschew consumer-facing business models in favour of B2B plays like deep-tech, but sector specialists still see opportunity, the Hong Kong Venture Capital & Private Equity Association's (HKVCA) Asia forum heard.

"Compared to other sectors, consumer has been far less impacted by policy changes. With the government promoting common prosperity, some consumer services that improve life quality are encouraged - and then the anti-monopoly actions have brought better market diversity," said Robert Chang, a co-founder and managing director at GenBridge Capital.

"The pressure comes from macros, like the slowdown in the economy and uncertainty regarding the COVID situation. These have led to operational issues for some players."

Private equity investment in China's consumer sector reached USD 8.3bn last year, nearly twice the combined total for 2019 and 2020, AVCJ Research's records show. Emerging domestic consumer brands, which have gained traction by leveraging technology in marketing and distribution, attracted considerable interest.

At the same time, the line between consumer and technology is increasingly blurred. One clear trend within the technology sector, as regulators cracked down on consumer-facing business models from financial technology to education, is a transition towards enterprise-facing opportunities.

Early and growth-stage investment in technology excluding content or services fell to USD 7.1bn in the second half of 2021 from USD 13.1bn in the first half. Over the same period, sector-wide deployment fell from USD 23.7bn to USD 19.3bn, as investors re-focused on areas like hard-tech and deep-tech.

Wendy Zhu, a managing director at AlpInvest Partners, observed a slowdown in IPOs - and in IPO pricing - could make late-stage growth investment less attractive. This would likely take some of the heat out of the consumer sector.

Chang added that valuations in the technology-facing consumer space have already experienced substantial declines. This is a consequence of traditional technology, telecom, and media (TMT) investors turning their attention to B2B models.

"Competition is much less intense than before, and we are seeing more rational expectation on the founder side. It will be a great investment window this year and next year because we can negotiate some good deals," he said.

It is widely expected that hard-tech and deep-tech start-ups will pursue domestic rather than offshore listings, given the sensitive nature of their intellectual property. This may give impetus to renminbi-denominated fundraising, but it isn't reflected in the data. Local currency fundraising continued a multi-year decline in 2021, while commitments to US dollar vehicles increased.

Nevertheless, Richard Nie, a partner at King & Wood Mallesons, claimed to be seeing more activity.

“One of our clients, a US VC firm active in China for the last 25 years, has always resisted the idea of raising a renminbi fund because they were not willing to deal with the very different domestic LPs," he said. "But last year they seriously considered the idea ... They feel like they must do this as a strategic move because of the policy changes."

Family offices to mix caution with courage in 2022
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Justin Niessner
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Conservatism in a post-pandemic world must be redefined to include flexibility and exposure to progressive industries, the Hong Kong Venture Capital & Private Equity Association's (HKVCA) Asia forum heard.

John McLean, a managing director and head of global asset managers Asia Pacific at Citi, who spoke as part of a panel representing family offices, flagged pending interest rate hikes as among the most likely market disruptors in the coming year.

This concern is tempered, however, by expectations that China's latest regulatory crackdowns and recent pandemic-related pressures on international logistics will prove short-lived phenomena.

"We see that that trend [less capital flowing into China] has well and truly troughed and maybe moving back the other way within a 12-month window. Sure, there's a desire on the part of the market to see a little bit more certainty there, but we're talking within 6-12 month timeframes, not 3-5 year timeframes," McLean said.

"I think supply chain-induced challenges exist around some consumer sectors. Although it does appear that Omicron will be a phenomenon everywhere, we hope that it will pass quite quickly, and we'll see those supply chain blockages unblock very quickly. You can see some quite sharp, short rotations in different sectors."

Patrick Tsang, CEO of Chow Tai Fook Enterprises, and Tony Yeung, CEO of Peterson Group, agreed that investors should avoid valuing assets based on the frequently used comparables and underwriting metrics of recent years. Both family offices are active across private asset classes.

Yeung, whose family established Peterson Group in 1959, said travel restrictions in Hong Kong were making it difficult to maintain a global portfolio and access talent. Nevertheless, the plan is to continue pressing for more non-Asia exposure, eschewing Europe for North America, which is seen as a more cohesive regulatory environment in terms of COVID-19 restrictions.

Chow Tai Fook Enter prises, controlled by Hong Kong's Cheng family, owners of the eponymous jewellery chain, plans to target opportunities this year across upstream mobility tech, healthcare, and special situations. There is also significant interest in cleantech, including hydrogen energy.

"In the past couple of years, we've seen some very aggressive valuations, aggressive methodologies in terms of beating your competition, winning market share, and we are beginning to see cracks in those industries," Tsang said.

"Just burning cash and giving lots of rebates may or may not be the way to go. The super-aggressive competitive strategies may not work. Sometimes the more realistic goals we need to think about."

Anthony Chan, CEO of Isola Capital Group, emphasised the need for diversification but noted that his firm was pulling back from smaller markets where it did not have access to partners on the ground. Isola, a multi-family platform, plans to establish more relationships with GPs in large geographies with a tech-focused strategy. This includes building out an in-house blockchain team.

"Historically, some people might think it's conservative to be more focused on a core portfolio and even fixed income, even though it hasn't generated much return for years. I think we live in a world now where you have to be diversified across asset classes, strategies, vintages if you have a program to deploy across certain major currencies, and just have good geographic separation," Chan said.

"We live in a world where very clearly there's the US or North American side, and there's the China side, particularly for technology-driven sectors."

LPs rely on managers to navigate China's regulatory headwinds
Private Equity International
Alex Lynn
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Chinese private equity firms are tweaking their sector focus to help legislate against regulatory uncertainty.

Mason: Investors must be "careful" about rushing into new sectors

Private equity investors are relying on their managers to help navigate China's unique regulatory environment, a conference has heard.

Appearing virtually at the Hong Kong Venture Capital & Private Equity Association's Asia Private Equity Forum on 12 January, Eric Mason, managing director at the $17.3 billion Church Pension Fund, said it trusted GPs to execute within the confines of government policies.

"We leave it more to our managers to navigate and to assess what policies are going to be catalysts for investments, [and which ones] are going to be restrictions or headwinds for investments," Mason said.

"Obviously, we've seen a big switch from ecommerce, data-oriented businesses in China that come under pressure for social responsibility and data security and national security. It's a natural trend. I think you're seeing this in some form or fashion in the US and Europe as well – people are trying to understand the size and scope and power of large, data-focused companies."

Sectors popular among Chinese private equity investors, such as education and consumer tech, have been subject to a spate of regulatory actions over the past six months as Beijing clamps down on national data security. This uncertainty has dented investor appetites for the market and prompted some managers to rethink their sector focus.

On a separate panel at the conference, Hongwei Chen, partner at Hong Kong-based Forebright Capital, said: "For some of the segments, we have seen some of the larger funds who used to bet relatively aggressively on consumer internet companies [have] now started backing aggressively enterprise and semiconductor companies as well."

According to ThomsonReuters and PwC, consumer appetites had soared prior to the regulatory crackdown, attracting $65.5 billion of private equity investment in the year to 30 June 2021, compared with $39.7 billion in the preceding 12-month period.

Challenge posed by China: Hongwei Chen, partner at Forebright Capital (bottom left) and Leon Meng, founding managing partner at Ascendent Capital Partners (bottom centre) were among the speakers

"A lot of our managers… see that there are other policies that are tailwinds for investing," Mason said. "It may involve renewable energy, electric vehicles, autonomous vehicles, elements of AI, hard-tech, semiconductors. [For] these policies which are encouraging more investments, I think we have to be careful about rushing too much into any one of these because they sound like they could be the next generation of very sensitive industries, as far as I'm concerned."

Other firms – such as Hong Kong-based Ascendent Capital – are seeking greater control over their investments to help navigate potential shocks. Leon Meng, founding managing partner of the mid-market firm, said at the conference that it expects buyouts to account for 50 percent of its portfolio in future, up from 30 percent at present.

"In the last 15 years we've seen many policy resets, but every time it's one to two years," he said. "This time shocked everyone because of the suddenness and also the magnitude of scale.

"The fact that we're sector-agnostic allows us to not put all the eggs in one sector, one industry. And… I think what's important is due focus on downside protection, due focus on cashflows, due focus on risk-adjusted returns, and having a structured mechanism… [providing] flexibility in exit."