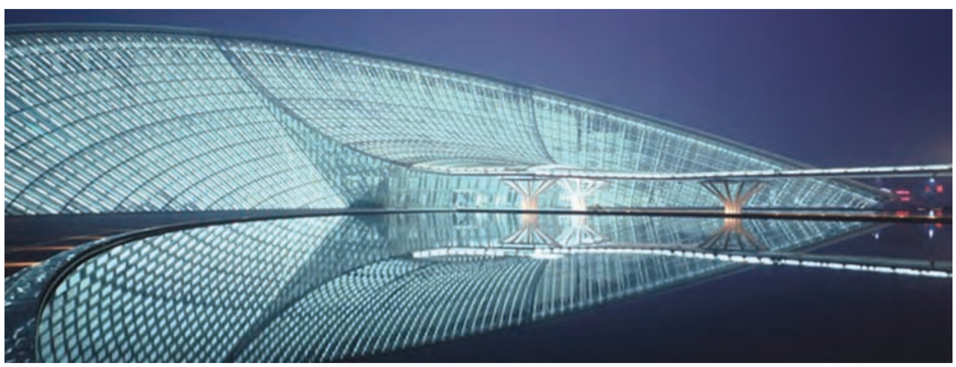
MidMarket in China

PRE-OLYMPIC UPDATE



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中道资本顾问

Tianjin and ACG on International Private Equity for Chinese Companies

By Patrick Hurley

Droves of Chinese growth company executives eager to attract Western private equity and strategic corporate investment made their way to Tianjin in early June to network with and pitch their stories to early adopters eying opportunities in China.

The second annual China International Private Equity Forum (CIPEF) drew nearly 6,000 people from across China, the U.S. and Europe to participate in programs such as the Association for Corporate Growth (ACG) Capital Connection and panels put together by ACG, the co-host of the event.

ACG panelist Peter Chen from Bain & Company shared with Chinese entrepreneurs that getting his investment committee up to speed on Chinese business practices is perhaps his biggest challenge.

Andy Rice from The Jordan Company, long an active investor in China, said that some of the best Chinese partners are companies that were not actively looking for capital but were sought out because they fit well with the needs of U.S. portfolio companies. These companies are receptive because their savvy owners see the benefits of beefing up management and systems to compete more effectively to service big multinational companies with high standards.

Jonathan Kotler from CCMP Capital Asia noted that 70 percent of his firm's value is in the nonfinancial aspects of helping drive portfolio company growth. He has found that third-tier cities are where reasonably priced deals are best sourced.

Seasoned U.S.-China hands including Gary Riley, CEO of MidMark Capital's portfolio company Energy Conversion Systems, has moved several businesses to China. He has dealt with the hurdles of ramping up a workforce for dramatically increased levels of production. Riley outlined creative ways that Western investors can support Chinese companies and protect their own flanks.

Tony Wong from 3i suggested that bridging Western standards with local Chinese practice could pay big rewards for investors who can put themselves in the Chinese entrepreneur's shoes when faced with inconvenient timelines and government approval needs.Oliver Ewald from Audax Group remarked that Chinese executives in private enterprise respond exceptionally well to incentive programs common in the United States. Heavyweights in China's financial reform such as Xianglong Dai, chairman of the National Council for Social Security Fund, and Xiaoling Wu, deputy director of the Financial & Economic Affairs Council of National People's Congress, also weighed in with insightful and inspiring comments about the need for and multitude benefits to flow from the development of private equity.

CIPEF grew out of ACG's effort to forge an alliance in China to serve the needs of ACG's nearly 13,000 members in North America and Europe. They increasingly find themselves with challenges and opportunities that require more knowledge of China and the ability to navigate on the ground there. It is no surprise that many of ACG's corporate members have done business in China for some time and that adventurous private equity firms are finding the natural evolution of sourcing portfolio companies can often lead to attractive direct investment in Chinese companies with opportunities ranging from greenfield investments and acquisitions, to minority interest purchases.

Several of the private equity players active in China commented about the lack of an established community of investment bankers and other intermediaries to serve up screened deals that can efficiently be reviewed and processed. The role of intermediaries in China is markedly different from the Western custom of the auction market and the often-transactional relationship model for advisers to issuers and the buy-side or sell-side.

Outbound acquisitions by Chinese companies were a hot topic as a result of the realization by Chinese executives of where the ultimate margins are most attractive. Several years of rapid growth for successful private companies has positioned them to be able to pursue acquisitions abroad.

There is a perception on the part of Chinese would-be buyers that U.S. intermediaries representing sellers are difficult to deal with because of the auction process. So much of what is common practice in the Western market for M&A is diametrically opposed to the approach of getting to know principals before engaging to do business.

The efficiency offering memorandums, chilly bidding guidelines, financing reps before even meeting seller management, and marking-up purchase agreements is a rude awakening for any first timer.

Private equity in China is taking hold for basic industry as well as telecom and so many other technology areas that have garnered the support of the venture crowd from Hong Kong. It was only a year ago that China created a limited partnership law and began to think about the motivation of the institutional funding sources that will fill the coffers of RMB-denominated funds to compliment the dollar-based funds that have been aimed at this growing and dynamic market.

While there is a long way to go, the Chinese have a sense of what needs to be done and ACG is committed to helping to pave the way.

Partick Hurley is Chairman of CIPEF. He can be reached at phurley@mmadvisors.com. For more on the China International Private Equity Forum and the Association for Corporate Growth, visit www.pe-fund.com and www.acg.org.