

THE WALL STREET JOURNAL.

Published: 12 April 2011

Asia Deal Journal: A new tack in China for equity firms

BEIJING -- For years, private-equity funds have been searching for the best way to invest into China. Now they're looking for ways to get Chinese money out.

In one of the first moves of its kind, RIT Capital Partners PLC -- an investment firm chaired by Jacob Rothschild -- together with local Chinese investment company Creat Group and investment advisory firm Quercus Ventures at the end of March said they plan to raise \$750 million in yuan from domestic Chinese investors to invest in overseas companies.

Their efforts to raise funds and get deals done will be a test of how easily private equity will be able to regularly use Chinese money in international markets, something that isn't yet assured of success.

With China growing increasingly wealthy -- and much of the developed world still suffering the effects of the global financial crisis -- fund managers are starting to look toward China as not just an investment destination, but a potential source of funding for deals elsewhere in the world.

Already China has become a major investor internationally, with firms demonstrating a voracious demand for overseas resources and individuals snapping up real estate around the globe. Much of that gets greenlighted by Beijing because it is in the country's strategic interests, or comes from savings amassed overseas.

But China still maintains strict capital controls that make it difficult for the yuan to be changed into foreign currency to make a financial investment. Investment in foreign stock markets can be done only through funds that have a quota to convert a certain amount of foreign exchange for the purpose.

"Regulators like the concept [of outward private equity], particularly when it involves helping Chinese firms go" abroad, says Ying White, a partner at law firm Akin Gump Strauss Hauer & Feld LLP in Beijing. "But there's a lot of issues that need to be worked out."

Ms. White says that China's current system for regulating Chinese purchases abroad is geared toward regulators approving each outward investment deal by deal.

That is fine for major firms that make only the occasional strategic purchase, but might prove problematic for a private-equity fund looking to make multiple deals a year. And given the often slow pace of approval, requiring the sign-off of multiple government agencies, there is always the risk of missing a window of opportunity for competitive deals.

So far the early movers are trying to demonstrate that their funds will benefit China's broader interests. J. Rothschild Creat Partners -- the name of the venture between RIT and Creat -- is aiming to invest in foreign firms that have growth opportunities in China, and holds open the potential for Chinese firms to invest alongside them.

That is a similar approach to A Capital, a European-backed fund involved in arranging China-based Fosun International Ltd.'s stake in resort-chain Club Mediterranee SA of France last year.

A Capital has signed a memorandum of understanding with the Beijing municipal government to set up a yuan-denominated fund to invest overseas. The plan is for the fund to sometimes invest alongside firms introduced to it by the Beijing government that are looking to expand abroad.



For the early movers, such political support is likely to be key. RIT is hoping it has that covered. According to Quercus Chief Financial Officer Maxim Parr, the fund already has support from one of the key regulators, the National Development and Reform Commission, China's top economic decision-making body.

And Chairman Zheng Yuewen of Creat Group, which has 20 years of experience investing in China, also heads up the China International Chamber of Commerce for the Private Sector, a government-backed industry group geared to helping private Chinese firms expand overseas.

The fund hopes the chamber's members -- which include high-profile Chinese firms such as Lenovo Group Ltd., Zhejiang Geely Holding Group Co., Shimao Property Holdings Ltd. and Fosun -- will form a base of investors. It hopes to start raising funds in May.

It will initially focus on technology and clean-tech, the green economy, health care, natural resources, and luxury goods, areas where China has already demonstrated a demand for Western expertise and brands.
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