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Hot News

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With the constant development and expansion of local VC/PE investment institutions as a whole, some leading VC/PE institutions, having accumulated successful experiences in the domestic operation, also start to consider "globalization" to further expand their business scopes and step into the next development stage.

Zero2IPO Research Center, famous VC/PE research institution in Great China, observes that an increasing number of local VC/PE institutions also develop towards an "all-round type" and start to establish USD funds, becoming investment institutions that can implement a strategy of "walking on two legs". This represents an important step of local VCs/PEs towards "globalization". We hereby released the Guidelines on Establishment of Foreign Currency Funds by Local VC/PE Institutions 2011, detailing fundraising and launch of foreign currency funds for local VC/PE institutions in terms of selection of overseas LPs, establishment of fund structures, conditions and registration processes for launch of different offshore funds as well as taxation related to foreign currency funds, and putting forward problems in the establishment of offshore foreign currency funds by local VC/PE institutions and some suggestions for future development.

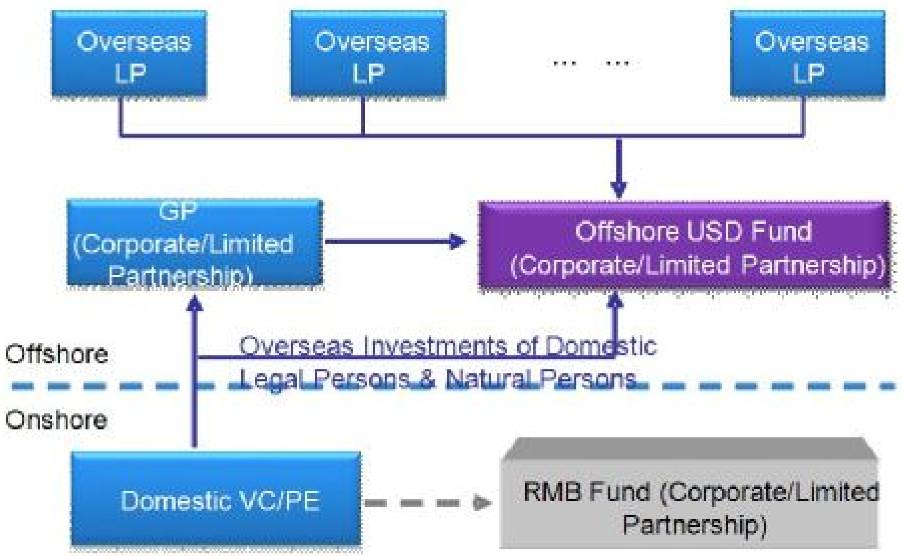
Kunwu Jiuding Capital Co., Ltd. (hereinafter as "Jiuding Capital") is a local VC/PE institution that founded USD fund in relatively early periods and sought for "overseas development". On November 18, 2010, Jiuding Capital announced that it completed the fundraising of

Table 1 Comparison of Domestic VC/PE-established USD Funds (Part)

Fund Initiator/Management Company	Fund Name	Fundraising Phrase	Fund Scale (US$M)	Establishment Date	Financing Completion Date
Kunwu Jiuding Capital	Jiuding China Growth Fund	Completed	120	2009.12	2010.1
Fortune Venture Capital	Fortune Venture Capital USD Fund	Completed	100	2010.06	2010.12
Citics Private Equity Funds Management	CPECHINA Fund	Completed	800	2010.08	2011.Q1
OFC Investment Management	OFC Investment Management USD Fund	Under fundraising	100	2010.05	-
Cowin Capital	Cowin Capital USD Fund	Planned to conduct fundraising	-	2011.02	-
Kaixin Investment	-	Planned to conduct fundraising	-	-	-

Source: Zero2IPO Research Center

Figure 1 Establishment Structure of USD Funds by Domestic VCs/PEs



Source: Zero2IPO Research Center

the first USD fund - Jiuding China Growth Fund, with the total scale of US$120.00M. Vertex Management is the cornerstone investor of the fund, and others include many globally well-known institutional investors, such as Sovereign Wealth Funds, Allianz Group (famous insurance company in the world), BMW Family Funds and Partners Group (one of the largest PEFOFs in the world).

Fortune VC, which is a local VC institution advancing aggressively in recent years, also successfully completed the fundraising of its first USD fund in the end of 2010 with the scale of US$100.00M. Fortune VC, as one of the leading representatives among the local VCs, has always been "observing programs from the perspective of foreign capital, implementing programs by means of domestic capital", also receiving high acknowledgement from LPs. It smoothly accomplished the fundraising of its first USD fund with its LPs including internationally known PEFOF and overseas individual investors.

In addition, local VC/PE institutions that have formed their brands such as Oriental Fortune Capital and Co-Win Capital also plan and prepare to establish USD fund. However, up to now, the establishment of USD fund by local VC/PE is still in the "infancy stage" without the formation of the first echelon. (See Table 1)

At present, the local institutions that have successfully raised USD funds, or are raising USD funds, or have included USD funds into their plans are all leading ones in the domestic VC/PE industry. They have already accumulated rich experiences and achieved excellent performances in RMB funds and their management teams have ideas, ambitions and long-term strategic plans. The starting points of their establishment of USD funds can be summarized into the following aspects:

1. Orientation towards internationalization.

Enterprise internationalization refers to the gradual evolution of enterprises to develop from domestic to international markets. Local VC/PE institutions that have completed the fundraising of USD funds, or are raising USD funds, or plan to raise USD funds should consider, at a strategic level, formulating the future development direction towards the global market. Although the development of this industry in the country is still earlier than the countries like Britain and the US, an investment institution that has an ambitious team and aims at sustainable development needs to lay a solid foundation now for future internationalization from a strategic perspective.

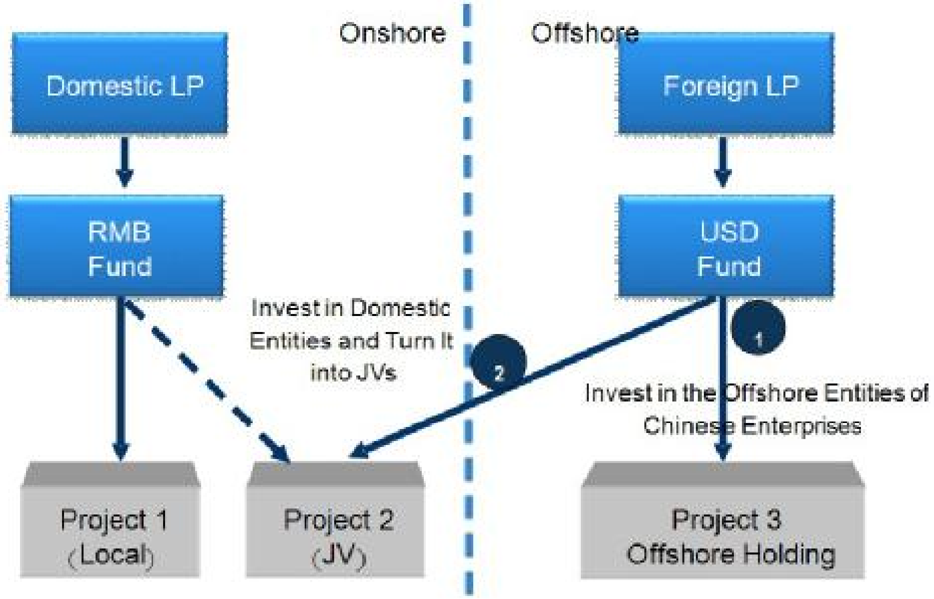
2. Possess experiences and achievements in the operation of USD funds as early as possible.

The current period represents a sound opportunity for excellent local institutions that are oriented towards internationalization to take the first step to "internationalization". With regard to the macro environment, Chinese economy is developing at a full speed and all the capitals from the globe are bullish about China's growth, making the present time relatively easy to raise USD funds. Judging from VC/PE investment institutions, the domestic exit channel for VC/PE has been unobstructed since the equity division reform in China in 2006 and local VC has enjoyed an "exit banquet" since the launch of ChiNext in 2009, so it enters into the harvest stage. In a period of excellent performances, it is also easier to win acknowledgement from overseas LPs and even top LPs in the world. Furthermore, the move to take quicker steps than other local institutions in possessing experiences and achievements in the operation of "USD funds" and establish long-term strategic cooperative relationships with LPs will pave a way for future fundraising of USD funds.

3. Actual investment demand.

Local VC/PE institutions that only have RMB funds often came across superior-quality programs in the previous investment, but due to their offshore frameworks which desire to acquire investments from offshore USD funds, they would miss many good opportunities. Therefore, it is also crucial for local VC/PE institutions to "walk on two legs", so that they can have wider choices and make more flexible investments.

Figure 2 Investment Mode of Domestic USD Funds



Source: Zero2IPO Research Center

4. Enhance risk-resistant abilities.

At present, the domestic capital market maintains sound development and the domestic exits for VCs/PEs are very smooth. However, considering that the domestic capital market may suffer a cold shoulder in the future and the enterprises with "overseas frameworks" invested by USD funds can go public abroad, the establishment of USD funds can reduce potential risks to local VCs/PEs due to the single exit channel.

The behavior that local VC/PE institutions establish USD funds at offshore centers is similar to overseas investments. And as to overseas investment, current laws in China mainly include: The Interim Measures for the Administration of Examination and Approval of Overseas Investment Projects (No. 21 of the National Development and Reform Commission of the PRC) promulgated by the NDRC in 2004, the Measures for the Administration of Outbound Investments (No. 5 [2009] of the Ministry of Commerce) promulgated by the Ministry of Commerce in 2009, the Notice on the Relevant Issues about Foreign Exchange Control over the Financing and Return Investments of Domestic Residents through Overseas Special Purpose Vehicles (No. 75 [2005] of the State Administration of Foreign Exchange) issued by the SAFE in 2005 and the Provisions on the Foreign Exchange Administration of the Overseas Direct Investments of Domestic Institutions (No. 30 [2009] of the State Administration of Foreign Exchange) issued by the SAFE in 2009. (See Table 2)

As the investment strategy adopted by the USD funds set up by local VCs/PEs at present, offshore fund is still invested in the companies that base the main businesses in Chinese mainland. There are two reasons: On the one hand, local VC/PE institutions are more familiar with the investment environment of Chinese mainland; on the other, in such a newly emerging market economy as China, Chinese enterprises are expected to enjoy higher growth than the enterprises in developed countries and the rich SMEs resources make more investment opportunities possible.

Specifically, there are two investment modes: (1) Invest in legal entities that Chinese enterprises establish at offshore centers and later advance to go public in overseas capital markets; (2) Invest in domestic entities in the identity of overseas investors and transform invested enterprises into joint ventures, and go public later onshore. (As shown in the Figure below)

Table 2 Major Laws and Regulation on Overseas Investments

Law Name	Release Department	Promulgation Time	Remarks
Interim Measures on the Administration of Examination and Approval of Overseas Investments Projects (Decree of the National Development and Reform Commission of the PRC No. 21)	National Development & Reform Commission	2004	These Measures shall apply to the examination and approval of overseas investment projects (including new establishment, merger and acquisition, equity participation, capital increase and re-investment) conducted by legal persons within the borders of the People's Republic of China directly or through the overseas enterprises or organizations in which they hold controlling shares.
Measures for the Administration of Outbound Investments (Decree of the Ministry of Commerce No. 5 [2009])	Ministry of Commerce	2009	These Measures shall apply to the establishment of an overseas non-financial enterprise or obtaining of an existing overseas non-financial enterprise's rights and interests, such as ownership, controlling power and operation and management power by the enterprises established in China in accordance with the law through means, such as establishment, mergers or acquisitions.
Provisions on the Foreign Exchange Administration of the Overseas Direct Investments of Domestic Institutions (Decree of the State Administration of Foreign Exchange No. 30 [2009])	State Administration of Foreign Exchange	2009	These Provisions shall apply to a domestic institution's formation of an enterprise or project or overseas acquisition of the ownership of, the controlling stake in or the business management rights to an existing enterprise through formation (in the form of exclusive investment, joint investment or cooperation), merger, acquisition or purchase of shares, upon the approval of the competent administrative departments of overseas direct investment.
Notice on the Relevant Issues about Foreign Exchange Control over the Financing and Return Investment of Domestic Residents through Overseas Special purpose vehicles (Decree of the State Administration of Foreign Exchange No. 75 [2005])	State Administration of Foreign Exchange	2005	The Notice shall apply to overseas enterprises directly established or indirectly controlled by domestic resident legal persons or domestic resident natural persons with their domestic enterprise assets or equities in an attempt to carry out equity financing abroad (including convertible debt financing).

Source: Zero2IPO Research Center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