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Investment Opportunities Generated in Diversified Development of Education & Training Industry

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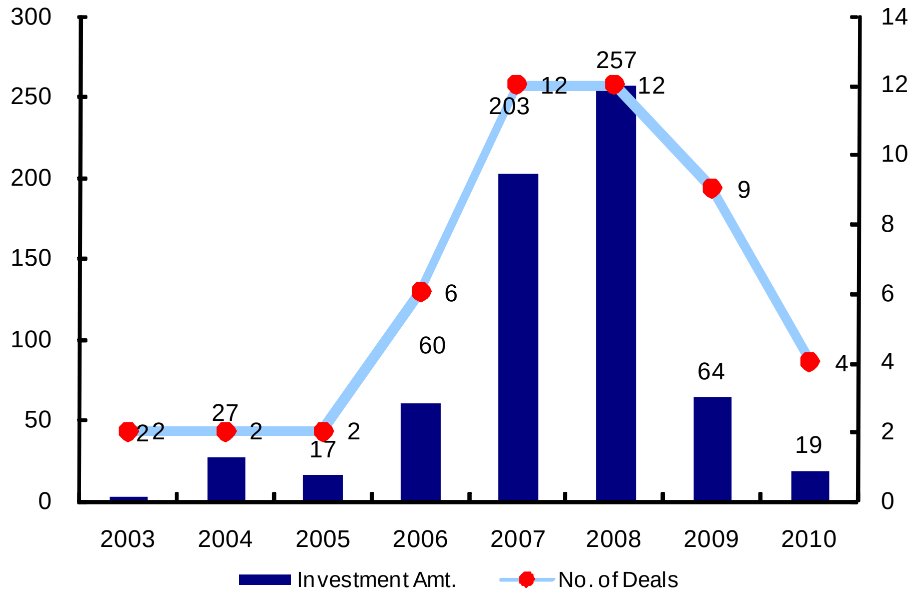
Investment Opportunities Generated in Diversified Development of Education & Training Industry

Written By Sylvia Xiao, Analyst of Zero2IPO Research Center

Since the year 2010, Chinese enterprises have been on an oversea listing spree again, especially in the education industry: on August 5, 2010, Ambow Education went public on NYSE; on October 8, 2010, Global Education & Technology Group Ltd. was listed on NASDAQ; on October 20, TAL Education Group was traded on the New York Stock Exchange; on November 2, Xueda Education was officially traded on NYSE. By the end of 2010, there had been a total of 10 education and training institutions that were successfully listed, all of which chose overseas stock exchanges without exception. The successful listing of so many companies indicates the positive attitude of international capitals towards the prospects of China's education and training industry. Since 2006, the number of successfully listed education and training companies in China has reached ten.

Year-on-year Comparison of VC/PE Investments in China's Education & Training Industry in 2003-2010



Source: Zero2IPO Research Center

However, in contrast to the highly-concentrated IPO deals, the education and training industry in China engaged in more rational investment in 2010.

The statistics of Zero2IPO Research Center from 2003 to 2010 showed that 50 VC/PE investment deals were disclosed in China's education and training industry, 38 of which involved an aggregate investment amount of US648.00M.

From the perspective of historical investment, 2007 and 2008 witnessed a peak of investment activities in the education and training industry, with 12 deals closed respectively each year. Specifically, 11 deals in 2007 disclosed a total investment amount of US203.00M, while the year 2008 disclosed the investment amount of 10 deals, totaling US$257.00M. Following the two-year peak, the enthusiasm for investment in the education and training industry saw a decrease. Only four investment deals were reported in 2010, two of which disclosed a total amount of US19.05M involved.

Regarding the investment opportunities, Zero2IPO Research Center observes that the development of China's education and training industry is facing the following favorable situations:

The trend of diversification in youth's growth

As the education market has been increasingly internationalized, the growth paths for the youth are no longer limited to primary school, secondary school, college entrance examination and university study. After graduating from primary, secondary or high schools, they have more options for further study, such as studying abroad or learning some courses on art or physical culture. However, the traditional public education cannot provide satisfying education services of the kind.

Baby boom in the developed areas may drive the development of baby economy

Although China is moving towards the "aging society" with a decline of youth population, the number of newborn babies in the developed areas remains stable due to population mobility. Especially, newborns in the baby-boom 1980s have reached their child-bearing ages, and the new birth control policy allows couples who are the only child in their families to give birth to two children. Therefore, developed areas have seen baby-booms in recent years, like "Golden Pig Babies" and "Olympic Babies".

The target set in education programs to increase the gross enrollment rate at all levels

According to National Fundamentals for Medium-Long Term Education Reform and Development (2010-2020), as of the year 2020, China's pre-school coverage rate will reach 95% (74% currently), the attendance rate of compulsory education 95% (90.8% currently), and gross enrollment rate of higher education 40% (24.2% currently). But state investment in education accounts for just about 4% of GDP, so it is inevitable to introduce private capital to ensure the achievement of the targeted enrollment rate.

Revitalization plans for key industries enhances the need for the vocational training

China is at its critical period of industrial restructuring. The 12th Five-year (2011-2015) will be a transitional period for China to move forward from its industrialization metaphase to the post-industrialization phase. In the next few years, the development of China's industrial structure will attach more emphasis on manufacturing high-end, low power-consumption industry and modern service industry. The corresponding demand for talents (like culture creative talents, etc.) will be in line with the industrial restructuring, which presents not only new requirements to the traditional academic system, but also driving force for the development of vocational training market that is more sensitive to market reactions. In 2010, China proposed the revitalization plans of seven strategic emerging industries and corresponding demand for talents-training will bring more opportunities to the vocational training industry.

Generally speaking, China's education and training industry now is not limited to the traditional academic education any more. With the diversified development of social demands, the development of business pattern and mode is evolving in a diversified way as well. The investment situation of education and training industry in recent years showed that the invested companies have various business types. From 2003 to 2010, among disclosed investment deals involving China's education and training industry, the professional training took a good lead both in the number of deals and the total investment amount, by accounting for 62% of the total number of deals and 78% of the aggregate investment amount. Out of 31 investment deals in professional training, ten were about IT training, representing the highest proportion, while six deals were about foreign language training and four about supplementary training. Furthermore, companies providing training services on art, animation design, postgraduate school entrance examination and even civil service examination, etc, had obtained VC/PE investments. Among five investment deals in formal schooling education, one was completed in private higher learning institution and one international school, while the other three deals were closed in comprehensive education groups. In the 11 disclosed investment deals in pre-school education, it is hard to distinguish kindergartens and early learning companies, as a majority of invested companies cover the both.

Despite the fact that the educational training industry has created some investment opportunities with full potentials, policy risk remains to be a double-edge sword facing capital that is taking a wait and see attitude towards these opportunities.

Non-state Education Promotion Law promulgated in 2002 gave acknowledgement to the non-profit status of the non-state education industry, suggesting the government principle of "active encouragement, great support, correct guidance and administration in pursuance of the law" on the operation of the non-state education sector under which non-state-operated schools and public schools enjoy the same legal status, and stating explicitly school operators are entitled to reasonable returns. For those institutions willing to engage in profit-making education and training business, a favorable signal is sent that profitability of the education and training industry can be legally acknowledged.

However, profit distribution of education and training institutions cannot be determined by its own totally in real practices and proportion of returns in school operating balance acquired by these institutions remains to be subject to various limitations, for instance, "charge items and standards", "expenditures covering education teaching activities and improving school operating conditions in charged fees", "school operating level and education quality", but there are no official provisions available so far in determining the proportion of returns. Uncertainty in policies makes it hard for non-state education institutions to strike a balance in non-profit nature and reasonable return and creates doubts for capitals to enter into the sector.

Q1'11 Saw US $3.36B Raised, 232 Investments Unprecedentedly Taking Place and 118 Exits Completed in Chinese VC Market

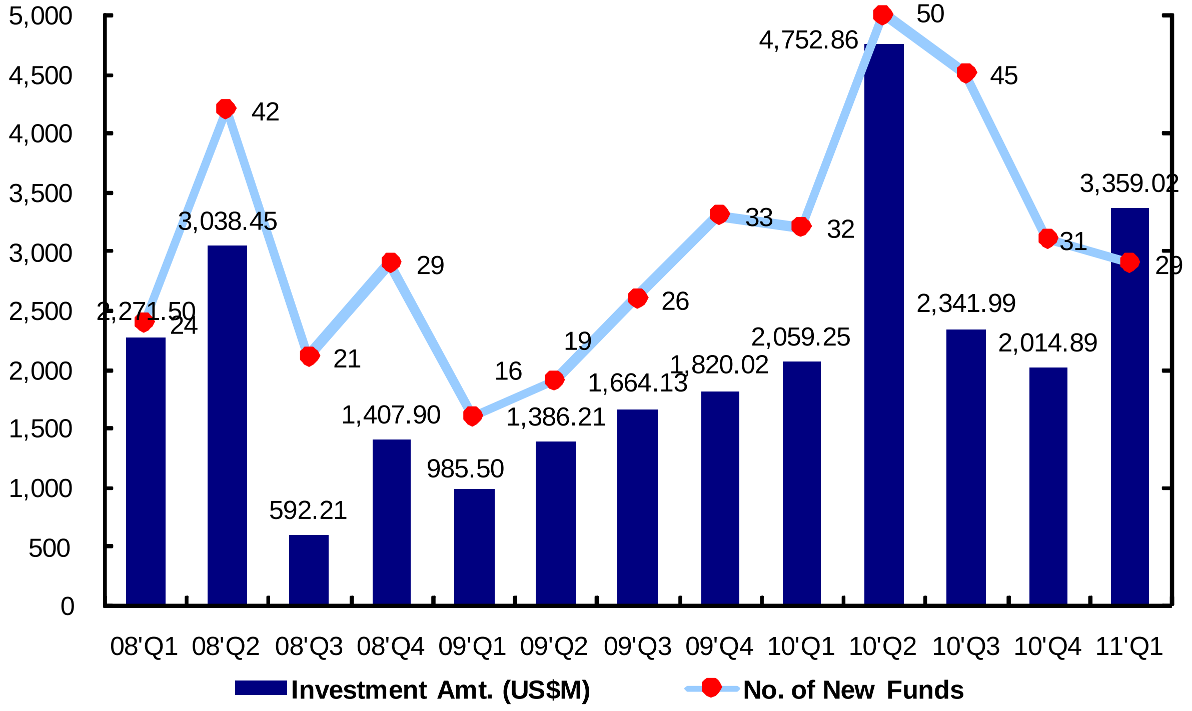
Apr. 6, Beijing, Zero2IPO Research Center

According to the data recently published by Zero2IPO Research Center, a well-known VC and PE research institution in Greater China, the fundraising boom in Chinese VC market persisted in Q1'11, despite a mild slide in the number of new funds, the capital raised accordingly continuously climbed up. Moreover, RMB funds dominated the market as same as the previous year, with the average fund size edging up obviously. VC investments in Q1'11 were on the increase both in terms of the number and amount involved, hitting a new high again. To be specific, Internet industry, without any doubt, embraced more investments, the same as the last year, the ranking of other industries was upside down. As for geographical distribution, Beijing saw more Investments happening, while Shanghai reaped the hugest capital from VC investments in Q1'11. The central and west regions like Xinjiang and Inner Mongolia also pocketed more investments than a year earlier. The number of exits completed in Q1'11 was above 100, mainly in ChiNext and SMEB.

According to the statistics from Zero2IPO Research Center, there were a total of 29 new funds raised by VC institutions at home and abroad to contribute US $3.36B available for the investments in Chinese mainland. As for investment, Q1'11 saw 232 deals involving US $1.93B in total in the relevant 192 disclosed investments. In terms of exit, among the 118 deals in Q1'11, 110 were completed via IPOs.

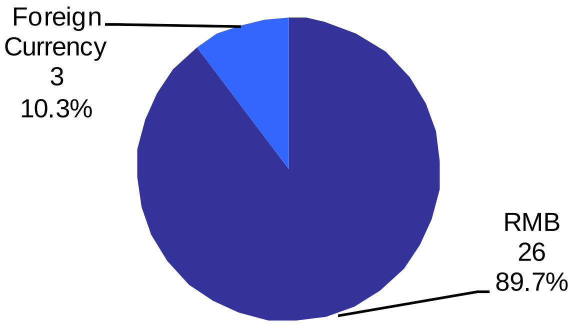
The data mainly came from the China Venture Capital Survey Q1 2011 conducted by Zero2IPO Research Center and China Venture Capital Report Q1 2011. The Center has released the results of quarterly and annual China VC market survey and ranking and staged out quarterly

Figure 1 Quarter-on-quarter Comparison of Fundraising of Investment Institutions in Q1'08 - Q1'11



Source: Zero2IPO Research Center

Figure 2 Distribution of New Funds in Q1'11 by Currency (By No. of Funds)



Source: Zero2IPO Research Center

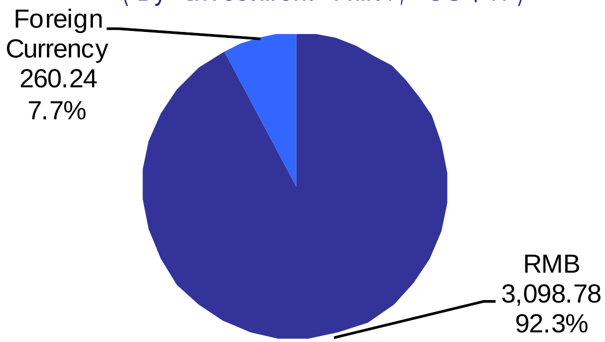
and annual research reports since 2001.

New Funds Boast Bigger Scale; RMB Funds Sustain A Leading Position

In Q1'11, Chinese VC market saw a drop in the number of newly raised funds, namely only 29, down 6.5% quarter-on-quarter. But Q1'11 witnessed a total of US$3.36B raised by those funds, only second to the peak in Q2'10, surged by 66.75% quarter-on-quarter or 63.1% year-on-year. (See Figure 1)

The data show there were only three funds out of the 29 new funds in Q1'11 denominated in US dollar, with US$260.00M raised in total, 10.3% and 7.7% of the total number and fundraising amount of new funds in the quarter. In other words, RMB funds occupied an un-

Figure 3 Distribution of New Funds in Q1'11 by Currency (By Investment Amt., US$M)



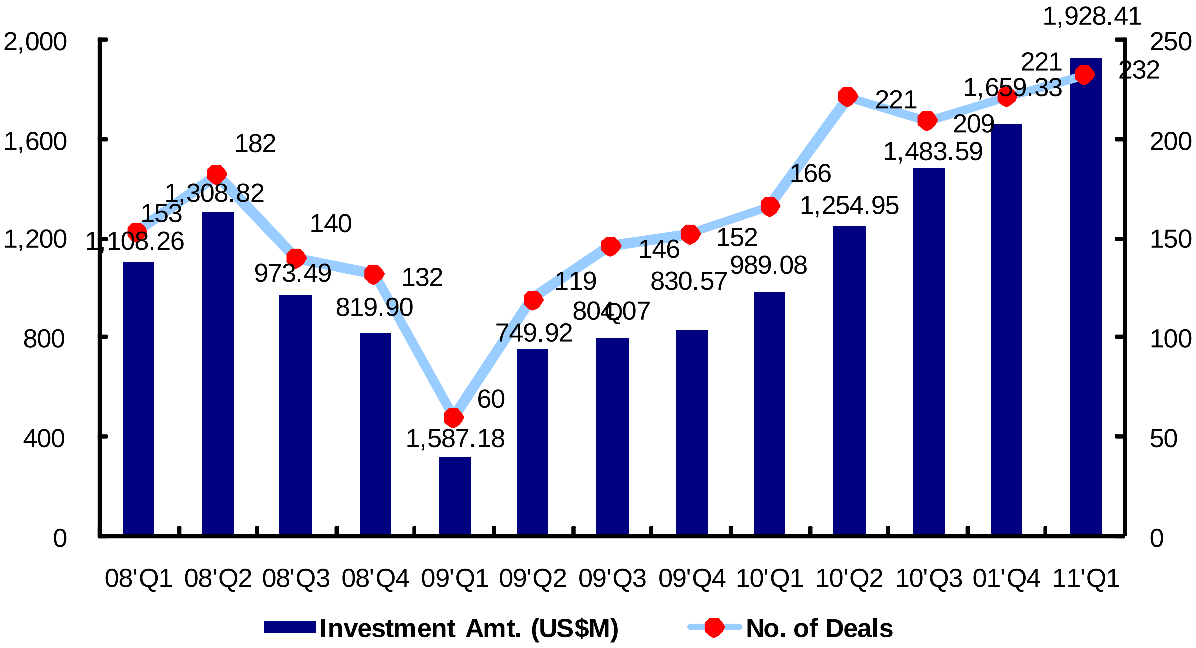
Source: Zero2IPO Research Center

shakable leading position in the market, with 26 RMB funds pooling a total of US$3.10B, 89.7% and 92.3% of the total. (See Figure 2 and Figure 3)

It is noteworthy that some large-sized RMB funds came into being in Q1'11, four of which each possessed more than RMB2.00B and all were raised by local institutions, including RMB5.00B Tencent Collaboration Fund and RMB3.50B Hunan Cultural Industrial Fund. This broke the deadlock featured by the slim sizes of RMB funds raised by local VCs.

The funds raised in Q1'11 were featured by: First, Big RMB funds appeared. All of the top five funds in the quarter were denominated in

Figure 4 Quarter-on-quarter Comparison of Investments in Q1'08 - Q1'11



Source: Zero2IPO Research Center

RMB raised by local institutions, shattering the pattern of prevailing small-sized RMB funds in the past. Second, VC funds' industrialization trend loomed large, with Internet of things funds, cultural funds, new materials funds popping up. Third, limited partnership became the mainstream for VC funds in choosing organizational structure. Among the 26 funds that disclosed their organizational structure, 19 adopted limited partnership, as high as 73.1% of the total.

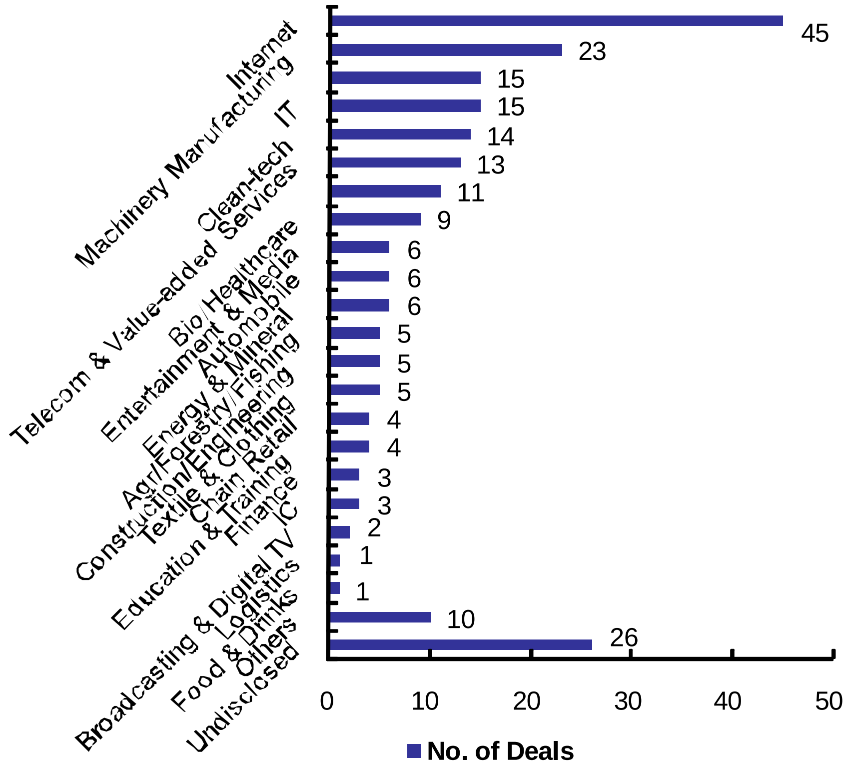
VC Investments Hit All-time High

Chinese VC market was once mired in the depression in Q1'09, but has climbed up quarter by quarter in the past two years and even hit a new high in Q1'11. There were 232 investment deals occurring in Chinese VC market in Q1'11. Among them, 192 deals disclosed a combined investment amount of US$1.93B. As for a quarter-on-quarter comparison, although the number of investments merely increased by 5.0%, the investment amount surged up 16.2%, a sharp liftup compared with the same period of the previous year, i.e. an increase of 39.8% in the number of investments and 95.0% in the amount invested. (See Figure 4)

Internet Remains as Bellwether; Investment Pattern Changes

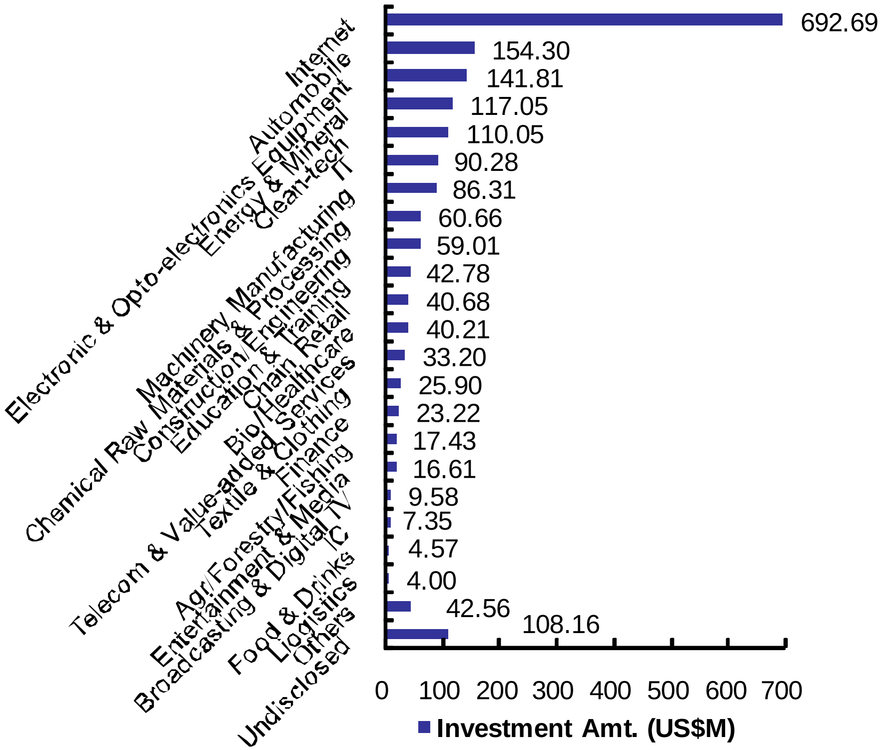
In Q1'11, the 232 investments in Chinese VC

Figure 5 Industry Breakdown of VC Investments in Q1'11 (By No. of Deals)



Source: Zero2IPO Research Center

Figure 6 Industry Breakdown of VC Investments in Q1'11 (By Investment Amt., US$M)



Source: Zero2IPO Research Center

market were scattered in 22 grade-1 industries. Internet undoubtedly took the lead with 45 deals and US$693.00M invested, nearly close to the annual investment amount of the industry in 2010, i.e. US$718.00M. It is noteworthy that foreign VCs remained dominating Internet investments, a total of US$590.00M investments in the industry came from 26 foreign investors in Q1'11.

In addition, the industry breakdown of VC investments in Q1'11 changed a lot from the past "Internet, Clean-tech, Bio/Healthcare VC investment domination". Machinery manufacturing and electronic & opto-electronics equipment industries reported more investments, which was not benefited from active local institutions. As for investment amount, automobiles, energy & mineral and other industries ranked up, because that the industries do trading with a high concentration of capital, reaping some relatively big investment deals in the quarter accordingly. (See Figure 5 and Figure 6)

Shanghai Ranks Top in Investment Amount; Central and West Regions Show Better Performance

In terms of geographical distribution, Beijing ranked first by reporting 53 deals or 22.8% of the total in Q1'11. However, as for funding invested, Shanghai took the lead with US$562.00M for the biggest deal in the quarter occurring in there. In addition, the investment booms in Jiangsu, Shenzhen and Guangdong

Figure 7 Geographical Distribution of VC Investments in Q1'11 (TOP 10)

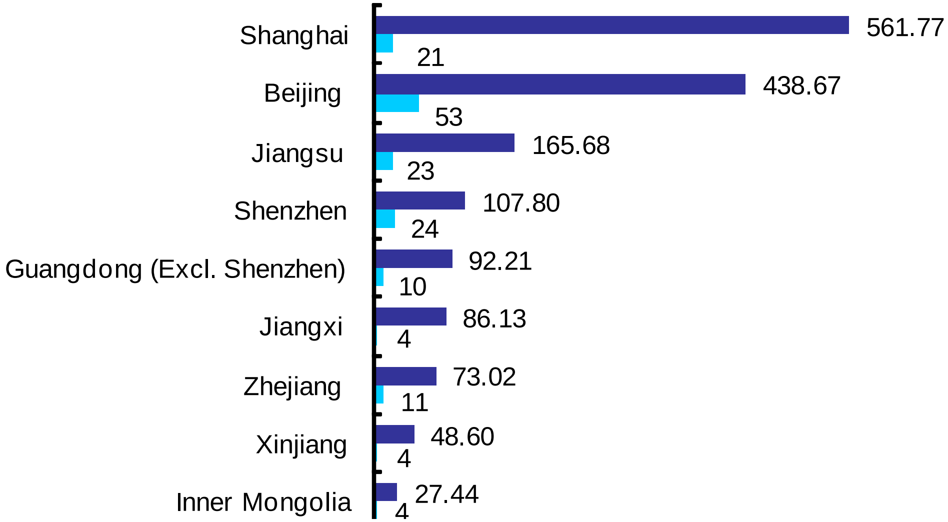


Figure 8 Quarter-on-quarter Comparison of VC Exits in Q1'08-Q1'11 (By No. of Exits)