



Patience pays off?

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Money troubles

"YOU COULD COUNT ON YOUR FINGERS

how many people know how the waterfall works, the LPs understand it better," one GP observed to AVCJ, when asked how well mid-level staff understood their compensation structure.

"A waterfall is a description communicated between the fund and the LPs. There could be a completely different mechanism in terms of how members of the GP get their carry."

Most GPs avoid documenting these details. "If you document then you can't always deliver in a tax-efficient manner," the GP added.

These comments were made last year during an interview for a story on how LPs conduct due diligence on GPs. Compensation is obviously an area of focus. Most LPs want a European-style waterfall, with carried interest only accrued once all drawn down capital has been returned to LPs and an IRR hurdle has been met. At the same time, a fund manager might worry about retaining junior staff if carried interest payments are pushed several years down the line.

But the more pressing question for LPs, and one they might hope to answer during due diligence, is whether those junior and mid-level members of staff believe they are paid fairly. The GP's point was that cross-examining a partner on compensation is fine, but doing the same with a junior staffer is not. A confused answer might leave the LP to conclude "team unhappy, may move," when that is not necessarily an accurate reflection of the workplace environment.

Nevertheless, this lack of transparency regarding compensation is a problem for the industry. Roy Kuan, managing partner at CVC Capital Partners, told the AVCJ Forum last week

that it was the number one reason for people looking for new employment, based on job interviews conducted by his firm. He also noted that "it is so easy to change the carry rules or the share ownership rules or the bonus rules."

Pool-based carried interest systems where people are paid according to their job title as opposed to the work they put into successful deals can lead to certain team members feeling underappreciated. However, just as damaging is when the bulk of the fund economics go to one or two founders rather than being shared out more equally.

A Preqin study on private equity compensation and employment – based on responses from 200 PE firms globally – shows a gradual increase in headcount among GPs operating in the sub-\$1 billion in assets under management space (the average number of employees for managers below \$250 million is 14, rising to 25 for \$250-499 million and 28 for \$500-999 million). This reflects the relative leanness of firms in their early stages, but it should not be accompanied by meanness on compensation.

Founders that want to build a sustainable franchise and scale up without losing the talented people who can make that additional capital count would do well to invest in the future and share the wealth.

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PE firms' headcount by assets under management



Source: Preqin

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ISSN 1817-1648 Copyright © 2015

AVCJ FORUM

Co-investments strengthen GP-LP bond

LPs that pursue co-investment opportunities alongside their portfolio GPs can build a stronger relationship with the managers. Sandra Bosela, global head of private equity at Optrust Private Markets Group, said that while co-investment has become a common component of private equity deals, not all LPs are capable of executing on those intentions. GPs will quickly learn which investors can follow through on their demands and which cannot. "You ask every GP, there are a handful of LPs who say they want it and will never execute. And the GPs will very quickly put them to the side," Bosela said. "The LPs who show that, yes, they can actually do it, are the ones that are going to get the calls over and over."

VCs say more is to come from the tech boom

The technology boom has seen a large amount of capital enter start-ups in the online-to-offline and mobile consumer spaces, and VC investors think there are still plenty of innovative start-ups worth backing. Raymond Yang, managing partner of China and US-focused WestSummit Capital, expects to see more companies in the robotics, drones and internet-of-things spaces challenge traditional businesses. Jenny Lee, managing partner at GGV Capital, agreed that connected devices is an area of particular interest, as investors look to create ecosystems that link to different types of hardware products.

GLOBAL

OTPP funds director named ILPA chair

Tanya Carmichael, director of global funds and private capital for the Ontario Teachers' Pension Plan (OTPP), has been appointed to chair the board of directors for the Institutional Limited Partners Association (ILPA). Carmichael has been a member of ILPA's board since 2007.

ASIA PACIFIC

Adams Street's PV Wang to step back

Piau-Voon Wang, a partner at Adams Street Partners who opened the firm's Singapore office

Investors see opportunity amidst volatility

Asian private equity is experiencing some volatility – driven in part by macroeconomic concerns and public markets turbulence – but investors told the AVCJ Forum that they are still finding ample opportunities.

"PE is a bottom-up business. It is about finding sectors, segments, business models and opportunities where we can take a longer-term



view and create value for investors," said David Shen, managing director at Olympus Capital Asia. "In the current cycle there is a lot of volatility and that impacts our view of risk when underwriting investments, but we are seeing some very interesting opportunities in our target markets."

Rob Petty, co-founder of special situations investor Clearwater Capital Partners, views the "multi-faceted, cyclical environment opportunity" presented by Asia as one of the region's most attractive qualities. It allows investors to ride a rebound in one economy while taking advantage of a downturn in another. "We can exit what we bought in India several years ago when everyone hated the market and enter China today when it is right at the forefront of the head winds," said Petty.

Clearwater has been looking at industrial companies in China and Asia that are struggling with heavy debt burdens, high leverage ratios and falling earnings. The industrial sector is also of interest to Shaw Kwei & Partners, albeit from the perspective of a China and Southeast Asia-focused middle market PE firm.

"We are less focused on interest rates and foreign exchange rates and the recently announced PMI [purchasing managers' index] and more focused on opportunities where we can move a company up the value chain, introduce disruptive technologies, and support management teams to move to their next stage of development," said Kyle Shaw, founder and managing director at the firm.

in 2006, is stepping back and transitioning to an advisory role. He will leave Adams Street in due course but will stay within the private equity

industry in a different capacity, AVCJ understands. Yar-Ping Soo, also a partner, has already assumed some of Wang's management responsibilities.

Shaw Kwei strengthens Hong Kong team

Middle market Asian PE firm Shaw Kwei & Partners has hired Brian Lau as an executive director based in its Hong Kong office. Lau was formerly a partner at boutique investment banks and advisory firm Prometheus, where he specialized in cross-border advisory and investment collaboration. Lau is expected to offer operational expertise in the technology and manufacturing sectors.

AUSTRALASIA

Archer Capital backs NZ education business

Archer Capital has created an education business in New Zealand following the acquisition of five privately-owned institutions. The new business – Aspire2 Group – aims to become the country's largest private provider of vocational education services to international students as well as a significant player in the domestic space and in safety and workplace communication training.

GREATER CHINA

China's securities regulator to resume IPOs

The Chinese Securities Regulatory Commission (CSRC) has said it will resume the domestic IPOs, lifting a three-month suspension on new listings that was imposed in response to market turmoil in July. The first batch of companies to list will comprise 28 candidates that had been approved before the suspension began.

Hony commits \$381m to oil player Santos

China's Honi Capital will buy A\$500 million (\$381 million) worth of shares in Australia-based oil and gas supplier Santos, as part of the firm's bid to cut debt by raising A\$3.5 billion. It will also issue A\$2.5 billion in new shares to existing investors.

Biosensors agrees to CITIC PE buyout

The board of Singapore-listed medical devices manufacturer Biosensors International has

accepted a buyout offer from CITIC Private Equity that values the company at approximately \$51.4 billion (\$996 million). The private equity firm already holds a 19.57% stake in Biosensors. It will pay \$50.84 per share for all shares it doesn't already own. An initial bid of \$50.815 per share was not endorsed by the board.

Alibaba agrees Youku Tudou acquisition

Alibaba Group has agreed to acquire US-listed Chinese online video platform Youku Tudou in an all-cash deal that values the company at approximately \$4.8 billion. This came after the offer was increased to \$27.60 per share from the initial bid of \$26.60 per share. Alibaba and Yunfeng Capital acquired a combined 18.5% stake in Youku Tudou for \$1.22 billion in 2014.

Innovation Works to list on New Third Board

Innovation Works, a Chinese early-stage VC firm founded by Kai-fu Lee, ex-head of Google China, has applied to list on the National Equities Exchange and Quotation, also known as the New Third Board. Lee said the listing would generate more capital to support potential unicorns – companies that are valued at \$1 billion and above.

China Q&A platform Zhihu raises \$55m

Tencent Holdings has led a \$55 million Series C round of funding for Zhihu, a Chinese question-and-answer platform similar to US-based Quora. New investors also include Chinese search engine Sougou, a subsidiary of web portal Sohu. Existing investors SAIF Partners, Qiming Venture Partners and Innovation Works all participated.

Intel backs two Greater China start-ups

Intel Capital has invested in Taiwan-based internet of things (IoT) solutions provider Microprogram Information and Chinese imaging and video technology specialist Perfant Technology. The captive GP expects to invest more than \$500 million in start-ups globally in 2015, up from \$359 million last year.

NORTH ASIA

Fortress raises \$1.1b for third Japan fund

Fortress Investment Group has closed its third

Asian GPs should share the wealth internally

The Asian private equity talent pool is deepening but GPs must ensure their compensation schemes are well balanced in order to retain mid-level staff, industry participants told the AVCJ Forum. Roy Kuan, managing partner at CVC Capital Partners, said that dissatisfaction over payment – because the bulk of carried interest goes to one or two founders rather than being shared out more equally – was the number one reason for people switching firms, based on job interviews he has conducted.

“You see many young GPs or PE firms not sharing the economics or not being transparent about the economics. It is so easy to change



the carry rules or the share ownership rules or the bonus rules,” Kuan said. Pool-based carried interest systems where people are paid according to job title as opposed to the work they put into successful deals can also be a source of frustration.

This has contributed to relatively high turnover within the industry, even though there are more talented investment professionals in Asia than ever before. H. Chin Chou, CEO of Morgan Stanley Private Equity Asia, views the situation in the context of a maturing market. He noted that on joining Morgan Stanley in the US nearly 30 years ago, there were plenty of role models who had spent 20 years or more at the firm. This was not the case when he arrived in Asia.

“When I first came to Asia the senior people were jumping around a lot. It took time and cycles for senior people to recognize that there is something about staying in your seat for a while and let the compounding do the work,” Chou said. He expects to see greater stickiness in time, in part because there will be more established figures in the industry to serve as role models.

Japan-focused special situations fund at the hard cap of \$1.1 billion. Ten deals have already been completed with more than JPY17 billion (\$140 million) deployed. Fortress Japan Opportunities

Fund III makes opportunistic investments in distressed real estate-related debt and other assets. It looks to take advantage of supply and demand gaps, limited credit availability, price distortions, volatility, and sales of non-core or distressed assets.

Korea's NPS loses chairman, CIO

South Korea's National Pension Service (NPS) is recruiting a new chairman and CIO after the two incumbents stepped down due to tensions over strategy. CIO Wan-Sun Hong's two-year term ended last week and he will be replaced. This follows the resignation of Chairman Kwang Choi in response to conflicts with the Ministry of Health & Welfare over whether or not to renew Hong's term.

Wind Point buys Korean lens manufacturer

Chicago-based private equity firm Wind Point Partners has acquired Daemyung Optical, South Korea's second-largest manufacturer of optical lenses. The PE firm sees the purchase as a means of broadening the product range and market penetration of another of its portfolio companies, US-based Vision Ease. Daemyung will also have the opportunity to enter the North and South American markets that Vision Ease serves.

SOUTH ASIA

Creador in part-exit from Cholamandalam

Creador has made a partial exit from Cholamandalam Investment & Finance (CIF), an India-based non-banking finance company (NBFC), securing a 2.8x multiple and a 33% IRR in US dollar terms. The divested stake – for which the proceeds were \$21.5 million – represents 36% of Creador's total holding in CIF. The company was Creador's first investment. It paid \$21.3 million for a 5% interest in March 2012.

Fairfax seeks controlling stake in ADI Finechem

The India unit of Canada-based Fairfax Financial Holdings has agreed to buy a 44.66% stake in chemicals manufacturer ADI Finechem for approximately INR1.3 billion (\$20 million). Fairfax India will acquire 6.16 million shares in ADI at INR212 apiece, according to a regulatory filing. It has also made an open offer for a further 3.58 million shares, or a 26% stake, at the same price.

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Deal Status: Agreement in Principle
Acquisition Technique: Leveraged Buyout
Acquisition Attitude: Neutral

Involved Companies

Company Name	Deal Role	Amount(USD\$m)	Deal Status	Industry	Nationality
Carplus Asia - China	Investor	n/d	n/d	Private Equity	United States
CDI China Management Co., Ltd.	Investor	n/d	n/d	Private Equity	Hong Kong
China Everlight Ltd.	Investor	n/d	n/d	Finance	Hong Kong
CTIC Capital Partners Ltd.	Investor	n/d	n/d	Private Equity	China (PRC)
Everlight Asia Fund Ltd.	Investor	n/d	n/d	Private Equity	China (PRC)
Non-Other Yang	Investor	n/d	n/d	Unclassified	China (PRC)
China Pacific (China) Holdings, Co., Ltd. (China Pacific)	Investee	n/d	n/d	Advertising	China (PRC)
Private International Ltd.	Seller	n/d	-17.20%	Steel	China (PRC)
Undisclosed Shareholder(s)	Seller	n/d	-65.24%	Unclassified	United States
Chengdu Global Markets Asia Ltd.	Financial Adviser, Investor (CDI China Management Co., Ltd.)	n/d	n/d	Securities/Investment Banking	United States
Chengdu Global Markets Asia Ltd.	Financial Adviser, Investor (CDI China Management Co., Ltd.)	n/d	n/d	Securities/Investment Banking	United States
Chengdu Global Markets Asia Ltd.	Financial Adviser, Investor (CDI China Management Co., Ltd.)	n/d	n/d	Securities/Investment Banking	United States
Chengdu Global Markets Asia Ltd.	Financial Adviser, Investor (CDI China Management Co., Ltd.)	n/d	n/d	Securities/Investment Banking	United States
Chengdu Global Markets Asia Ltd.	Financial Adviser, Investor (CDI China Management Co., Ltd.)	n/d	n/d	Securities/Investment Banking	United States
Chengdu Global Markets Asia Ltd.	Financial Adviser, Investor (CDI China Management Co., Ltd.)	n/d	n/d	Securities/Investment Banking	United States

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The long hold

The notion of patient or permanent capital draws interest from both GPs and LPs, but evergreen funds are rare in the US and even rarer in Asia. This state of affairs is unlikely to change any time soon

AT 18 YEARS, ELECTRA PARTNERS ASIA'S

investment in India-based Zensar Technologies can claim to be one of the longest-held in the region to see a successful exit. This happened in October when Apax Partners bought Electra's 23.2% stake for \$129 million, a 16x return once dividend payments are included.

The original commitment was made in difficult circumstances. Zensar was a software services subsidiary of a struggling listed computer hardware manufacturer. The parent, RPG Enterprises, used the \$9 million it received from the PE firm to pay off the listed entity's debt so the business could be wound up. The software services unit then performed a merger with the remaining shell, which was renamed Zensar.

Governance mechanisms and a management team were put in place so Zensar could operate independently. Over the ensuing years there were also several bolt-on acquisitions as the company rode the wave of growth in India's business process outsourcing industry, expanding headcount from 900 to 8,000. Revenue for 2015 reached INR26.3 billion (\$406.4 million).

The length of the investment is a function of the nature of the ultimate shareholder as well as the strength of the business. Electra made the investment through a London-listed investment trust, an open-ended vehicle that promised shareholders annual capital growth of 10-15%. With Zensar consistently expanding at a rate of 12-18%, there was no pressure to exit. Indeed, the sale was largely driven by a shift in Electra's strategy that has resulted in a reduction in exposure to Asia.

"People say they would like to add value and get out after five years, but if you are in a decent business why would you sell?" asks John Levack, managing director at Electra. "Patient capital looks at all of the fees and extraneous heat generated by doing a deal and says, 'When you find a good business, do what Warren Buffett does, which is back a management team to ride it through some of the cycles.'"

Room to grow

Evergreen fund structures, a private markets near-equivalent of Electra's listed investment trust, perform a similar function. However, they are rare globally and even rarer in Asia. This not

only a sign of the industry's relative immaturity in this part of the world, but also a reflection of the fact that extended life or even perpetual structures are not for everyone in private equity – GPs or LPs.

Sutter Hill Ventures is generally acknowledged as the first firm to adopt an evergreen structure in the 1970s and it remains in business to this day. Jordan Silber, a partner at Cooley, estimates there are currently no more than 30 in existence in the US – a tiny fraction of the number of traditional 10-year funds – with his firm having served as formation counsel for half of them.

"We at Cooley believe they provide some very positive commercial attributes to investors once deals get done, but these funds are very hard to raise and you risk losing a lot of LPs along the way"

– Jordan Silber

The Sutter Hill portfolio unsurprisingly exhibits several of the characteristics that make evergreen funds attractive. Its holdings include Pure Storage – for which Sutter Hill provided a Series A round in 2009 and which it then continued to support through an IPO last month – as well as Menlo Security, a two-year-old start-up that received a Series B round from the VC firm in June.

Silber notes that anyone investing in an existing evergreen fund tomorrow would get immediate exposure to a mixture of early, mid, and late-stage companies built up over a very broad period of time. "It is one of the things we have heard from LPs that they view as a positive – they get opportunities to reduce risk by buying into a highly diverse portfolio of assets," he adds.

The Sutter Hill portfolio also features an LP

interest in Shanghai-based Chengwei Ventures' first fund, raised in 2000. For its follow-on vehicle, Chengwei opted for an evergreen structure; the most recent regulatory filing in 2012 lists a target of \$535 million. Yuantai Investment Partners, a spin-out from Chengwei, is another to have raised an evergreen fund.

Other members of the elite club of Asia evergreens include two Indian GPs that have so far wholly or largely focused on long-hold PIPE deals – Nalanda Capital and WestBridge Capital – and NSSK Fund I, which was raised last year by a group led by Jun Tsusaka, former Japan head of TPG Capital. Capital Today Group, a growth-oriented Chinese firm, is expected to join this number: It is said to be nearing a final close of \$600 million, plus a 25% additional draw, on its third fund, an evergreen vehicle.

Big ambitions

According to one source familiar with Capital Today, the founder, Kathy Xu, is "a big believer in the laws of compounding." This translates into a desire for longer holding periods and no longer being at the whim of LPs, trying to manage the timing of exits to suit their liquidity needs.

Capital Today remains a shareholder in JD.com, having participated in the online retailer's Series A round in 2007, seen the business go public, and taken more than \$100 million off the table through an IPO and subsequent share placement last year. The firm is sitting on a partially realized return of more than 100x, but is said to have come under pressure from certain LPs as early as 2011 to sell some or all of its stake as the valuations of private rounds grew in size.

More is expected from JD.com and from other portfolio companies such as Yi Feng, a brick-and-mortar pharmacy chain now listed on the A-share market, so Capital Today wants to stay involved.

Chengwei is said to have made a similar pitch when raising its evergreen fund, saying it wanted to build the Exxon Mobil and Procter & Gamble of China, one LP who looked at the fund notes. Among its current investments is Youku Tudou. Chengwei was Youku's first backer in 2005 and remained a shareholder as the online video platform went public in the US and then

merged with domestic rival Tudou. Alibaba Group recently agreed a buyout at a valuation of \$4.2 billion.

The primary challenge of an evergreen fund is creating a structure with which investors are comfortable. Phil Culhane, of counsel at Simpson Thacher, has designed several structures for GPs in Asia but it has proved impossible to date to sell LPs on novel approaches in a region they already view as high risk.

On one occasion, the structure and terms allowed investors – after an initial lock up – to annually elect to exit or rollover their positions.

substantially greater than for a traditional PE fund. In order to facilitate exits, at the end of each four-year period all of the assets in the portfolio must be marked to market, with even unrealized gains and losses allocated out to the capital accounts of participants. This means that, should new investors enter, they are buying a pro rata portion of the existing portfolio at fair market value.

“All of these funds have the relief valve of a mechanism whereby the LP can get out, but they aren’t really designed for people to exit,” says Cooley’s Silber. “You might go so far as to say they are set up to incentivize LPs to stay in for

proprietary capital; they are able to be patient or even permanent.

By contrast, a fund-of-funds, which is bound by its own fixed-term lifecycle and must return capital to investors, is generally not a good fit for an evergreen structure. Public pension funds may also shy away from such an approach, if not because of unpredictability in their future exposure to alternatives as part of a broader basket of investment, but rather due to a residual discomfort with structures that depart from the norm. (It is, however, worth noting that open-ended funds are commonplace in infrastructure.)

According to Lorna Chen, a partner at Shearman & Sterling, some LPs also struggle to decide how evergreen funds should be addressed internally. “The risk profile doesn’t fit the hedge fund team’s requirements because there is such a big illiquid pocket, but if you go to the PE team then the redemption part doesn’t fit its profile.”

Asked about evergreen funds, Nicole Musicco, managing director and head of Asia Pacific at Ontario Teachers’ Pension Plan (OTPP), observes that they are an innovative and interesting structure for long-term investors, but she hasn’t seen many of them. “Maybe that kind of desire is being met through managed accounts that some of the larger LPs are taking on. If you can do it in a captive way with one or two like-minded LPs, then it could work but it’s still hard to figure out a structure,” she says.

Andy Hayes, private equity investment officer at Oregon State Treasury, tends to avoid evergreen funds. He wants managers to display the full PE skill set – buy a company, make it better, and then sell it. Hayes adds that a GP is only likely to get traction on a differentiated structure of this kind if it has very strong relationships with LPs and an impressive track record. Indeed, the Cooley clients that have successfully raised evergreen funds were all between vintages three and five.

Capital Today has, in short, earned the right to be creative. At least four of the investments from the GP’s 2005 debut fund have individually returned the entire fund, including JD.com, Yi Feng, Rongqing Group and Youku Tudou, while Fund II is said to be tracking well. If Capital Today wanted to raise a traditional vehicle, the consensus view is that it would happen swiftly and smoothly.

Given the track records of many PE firms in Asia are still works in progress – in large part due to challenges faced by minority investors that want to take portfolio companies public – an evergreen structure represents a leap of faith. An LP must be confident that, even on achieving an IPO, a manager can then secure a timely exit. The danger is that a manager falls in love with his

Select Asia PE funds with evergreen structures

Fund	Manager	Vintage	Strategy	Market
Chengwei Ventures Evergreen Fund	Chengwei Ventures	2004	Venture	China
Nalanda India Fund*	Nalanda Capital	2007	PIPE	India
Yuantai Investment Partners Fund I*	Yuantai Investment Partners	2010	Venture	China
Nalanda India Equity Fund	Nalanda Capital	2011	PIPE	India
WestBridge Crossover Fund	WestBridge Capital	2011	PIPE/growth	India
NSSK Fund I	NSSK	2014	Growth/buyout	Japan
Capital Today Evergreen Fund	Capital Today Group	2014	Growth	China

* Converted from traditional to evergreen structure
Source: AVCJ Research

Exits would be facilitated through a mechanism that mimicked the traditional PE approach: a return within a proposed range of five or seven years, with a calculation that factored in hurdle rates and carried interest, as well as when the capital was to be returned to the LP. Although the structure addressed concerns over liquidity and fair valuations, and drew intellectual interest as permanent capital vehicle that could offer liquidity, the fund did not get traction.

“Even if you have great alignment and the right set of professionals, many LPs aren’t always ready for such a big change,” Culhane explains. “They say, ‘Okay, I have a certain amount to spend in Asia every year, do I want to be breaking my head over a fund structure I don’t understand or do I want to look at industry standard models and make industry standard comments? It’s high risk to be a first mover LP on a new structure in Asia.”

The structure that has worked for Cooley is a 28-year fund divided into seven four-year activity periods. If an LP commits \$10 million at inception, at the end of year four it can choose either to re-up, which means putting in another \$10 million, liquidate its position or in some cases place it in a run-off account to be wound down over time. An LP that re-ups every time would therefore end up investing \$70 million.

The amount of back office work that must go into keeping track of different positions is

the long term because only by doing that do you get all the compounding benefits. The historical incidence of LPs exiting these funds has been near zero percent.”

Nalanda, which converted its 2007 vintage traditional fund to an evergreen (although the GP is no longer investing out of it) and then raised a separate evergreen fund in 2011, has a somewhat different approach: an LP makes the full commitment up front and has the option to exit every five years. However, the stability in the investor pool is just the same, with a source familiar with Nalanda saying that 95% of the firm’s LP base remained unchanged since 2007.

Foundation’s friend

The reason for this consistency is both a negative and a positive of the evergreen approach: the range of LPs that like it is very limited, but those select few tend to like it a lot. The vast majority of Nalanda’s investor base is in the US and dominated by endowments and foundations. Chengwei is also popular among the US endowments.

A number of endowments are known for approaching managers they like and suggesting an evergreen structure for the next fund. The motivation is in part access – an LP has the right to re-up at every juncture, no matter how much the GP might want to replace it – but more about longevity. These groups represent long-term,

“Even if you have great alignment and the right set of professionals, many LPs aren’t always ready for such a big change”

– Phil Culhane

investments and never wants to let go.

“If you look at people who are successful in private equity, in general those who sell too early and take money off the table faster probably do better over the long term. Firms that hold on to stock over long periods of time – whether public or private – and think they are going to create more value certainly could run into trouble,” says Doug Coulter, a partner at LGT Capital Partners.

Another significant obstacle for evergreen funds in Asia is team depth and volatility. While these vehicles may run nearly three times as long as traditional funds, they tend to come with similar key person clauses. This means the leaders must commit to staying around for the full 28-year cycle. In reality, the likes of Sutter Hill have managed succession planning in the standard

way – every eight years a couple of people might step back and others are promoted from within – and LPs haven’t felt the need to trigger to the key person clause.

The problem in markets like China and India is that most firms have been around for no more than a decade and one or two founders remain dominant figures in the hierarchy. Were they to depart, there is no guarantee the franchise would survive. If an LP is uncertain how many out of a core group of partners in their 40s will still be with the firm 10 years down the line, then it will be wary of making a commitment that could last more than twice as long.

While the exit mechanism is a comfort, expecting to use it undermines the rationale for backing the fund in the first place: that a particular team has the skills to consistently outperform its peers by holding companies for longer.

An infrequent occurrence

Should Capital Today make an evergreen structure work effectively, others will certainly want to follow suit – not least because they crave being freed up from fundraising every few years. However, even though industry participants say they are seeing movements away from traditional structures, this is more towards deal-

by-deal strategies rather than longer duration blind pools.

“As a manager raising a fund, you have to decide which battle you are going to fight – explaining the structure to investors or laying out your credibility or strategy to investors,” one GP observes. “People would rather fight the second battle than get into an evergreen structure.”

Cooley’s Silber adds that it will be more difficult to raise these funds in Asia than the US. First, most of the investors familiar with this structure are based in the US and so their approach to Asia is likely to be more conservative. Second, Asian LPs don’t know the structure, which means a concerted educational effort is required to get them comfortable with it. Regardless of geography, the law firm asks its clients to think carefully about whether they really want to proceed with an evergreen structure.

“We at Cooley believe they provide some very positive commercial attributes to investors once deals get done, but these funds are very hard to raise and you risk losing a lot of LPs along the way,” he says. “Some won’t be able to proceed with you because of their nature, such as fund-of-funds, and others may be fine with the idea of patient capital but at the end of the day it is too complicated for them.”

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Face to face

Dealing with a family office can be uniquely challenging for GPs. Managers who want success have to be able to handle the unique dynamics of this situation

SPYRIOS POULIOS KNEW THE NEXT DAY

would be key. The co-founder and managing partner at multi-family office Seminal Capital Partners was scheduled to meet with a potential principal investor and his wife who were returning from a holiday in the Maldives. To convince them to sign up, he had prepared a lengthy, detailed business plan.

However, at a dinner that night, Poullos met a friend of the principal, whose advice caused him to revise the entire presentation. The friend told him that the principal's wife had been pushing him to work less and spend more time with the family.

"He said, 'You're going to scare him, but more importantly you're going to scare his wife, about getting into something that's way over the scope that she's looking for,'" Poullos told the AVCJ Forum. "So instead we did this sort of Saudi-style, two-pager, big font, masthead. And the first line, about why he should have it, is: 'To work less.'"

Poullos' experience taught him a valuable lesson about dealing with families that many GPs have yet to learn. While it is always important to understand the concerns of one's audience, the unique dynamics of families put a spin on the process that can be difficult to appreciate. However, fundraisers who take the time to fit themselves into that dynamic will be rewarded for their efforts.

Willing investors?

Though family offices in Asia-Pacific represent a relatively small portion of the global family office market, they exercise more influence in the private equity scene than their global peers. According to the Global Family Office Report 2015, an annual survey published by Campden Wealth Research and UBS, more than 27% of the average Hong Kong family office portfolio was in private equity, as opposed to the global standard of 22%.

In addition, Asia-Pacific family offices had the second-best investment performance globally in 2014, which the report attributed to their comparatively larger involvement with private equity. Asian family offices saw a return of 6.3% in dollar terms, after Europe, at 6.4%.

These groups are an attractive target for GPs, but several family office heads in the region complain that the managers who pitch them are

often so unaware of the needs of a family office that they just end up wasting everyone's time.

"GPs won't like this, but you have about 10 minutes to grab our attention. And after that, you either are winning, or you've lost your audience," says Kaj-Erik Relander, who runs a family office in Switzerland that focuses on global blue chip liquid investments and private equity. "During those 10 minutes you win the right to try to close the investment, if you did your homework well."

Most managers are aware of the importance of research to a successful presentation. However, their mistakes lie in the kind of research that they do. GPs often make their presentations too broad,

which one was given the job as a sinecure? Getting this question wrong could mean, at best, a wasted meeting with someone who has no decision-making power; at worst, it could mean the complete failure of a pitch.

Show you care

Another issue is the necessity to maintain a connection with the family outside of their fundraising periods. Managers who only seek out the office when they need money are likely to be written off as having no understanding of the family's needs and no ability to help meet them.

"From a family office perspective, there

"From a family office perspective, there are a lot of things that we worry about. And your fund is not one of them"

— Dan Farrell

as if for committees; but family offices are often much more reliant on the preferences of their founders.

Alexander Pestalozzi, who runs the Asia branch of the family office of German consumer goods magnate Theo Mueller, says that when GPs treat the family as just another investor it is natural to reciprocate that lack of interest. More importantly, such a pitch is likely to be dismissed because the intended recipient cannot understand what is being proposed.

"We've all been there, we have a PowerPoint presentation, we have to do 20 presentations in two weeks, and so we start at page one and we finish at page 30, and we read half of the words off the presentation," says Pestalozzi. "But he doesn't want that, that's not how he built his business. He wants you to put away your presentation and explain to him, in your own words, how the thing works."

In addition to the concerns of the founders, family offices are often the arenas for internal family conflicts to play out as well. This is another difficulty that GPs often underestimate, and which can lead to fatal misunderstandings.

For instance, a company founder with many children might appoint several of them to posts in the family office – which one earned the position through business competence, and

are a lot of things that we worry about. And your fund is not one of them," says Dan Farrell, chairman and CEO of global multi-family office LP Privos Capital. "If we don't see you regularly, then we don't care about you, we don't have a relationship with you."

Despite these complicating factors, family offices, and those from Asia in particular can still be a useful source of capital for fund managers. Seminal's Poullos points out that he sees relatively little interest from GPs in Asian family offices, partly because they are a relatively recent phenomenon in the LP community. However, as the Global Family Office Report shows, the offices themselves do have considerable interest in private equity.

Mueller's Pestalozzi emphasizes that making things work with a family office investor means identifying the key players in the organization and building a positive relationship with them. That first step will set up all the future opportunities.

"If you can actually help the family office guy, that's key," says Pestalozzi. "If you guys are good, and you're going to perform, it's going to reflect positively back to me, so I want to make sure it goes through well. So you need to find the guy that likes you when you make the original pitch, and then he can help you as well." ▀

DEAL OF THE WEEK

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KKR eyes Asia content

WITH THE TRADITIONAL MEDIA IN

most South and Southeast Asian markets dominated by conglomerates and large family-run businesses, most private equity deals are relatively small, perhaps \$50 million or below. KKR wanted to tap into the lucrative media content segment, but these market dynamics presented a problem.

The PE firm's recently announced media and entertainment investment platform – known as Emerald Media – is a solution. It has committed \$300 million to the venture, with The Chernin Group (TCG) participating as a minority co-investor. TCG's existing Asia-focused team, currently operating under the CA Media banner, will join Emerald and KKR will take a significant minority stake in CA Media.

"If you look at the trends in India and other geographies in the region, we see huge changes in consumption patterns. Mobile devices are disrupting how we live our lives, and content is king," says Rupen Jhaveri, a director at KKR. "Emerald gives us the operating mindset and the ability to play in the space [in terms of ticket size]

where a lot of the action is taking place."

TCG is a privately held media holding company founded by Peter Chernin, a former COO of News Corp. It invests globally in media, entertainment and technology-related assets. CA Media was created in 2010 by Paul Aiello, who previously worked for Chernin as head of New Corp-owned Star TV Asia. He was joined by Rajesh Kamat, formerly COO of Viacom18 Group and CEO of Colors.

They built up the CA Media portfolio, which currently has four companies in India and one in Indonesia. The company acquired a 49% stake in global independent television producer Endemol's India business, best known for non-scripted shows like "Bigg Boss," the local equivalent of "Big Brother." It has since expanded into scripted and film production.

CA Media also has minority stakes in a live events business and a graphic animation company, as well as incubating a digital celebrity

network comprising multiple platforms including video-blogging and merchandise sales. In Indonesia, it backs a free-to-air broadcaster.

Teaming up with KKR as Emerald will see the CA Media team make investments of \$15-75 million, as opposed to the \$5-25 million they committed previously. "The ticket size throws open many more opportunities," says Kamat. "We would probably have focused on a certain kind of sub-sectors within media, but there is consolidation happening on the distribution front in India with a number of pan-Asian players coming in. We now have access to more of these assets."

The other change is geographic. Emerald will still deploy roughly half of its capital in India, but the rest is expected to be deployed more widely across Southeast Asia and eventually North Asia. "We have a lot of experience in these markets, but we had to prioritize. With the support of KKR these opportunities become very real," Aiello says. ▀



Content: Emerald is interested

Taiwan AI draws global investors

VENTURE CAPITAL HAS GAINED

momentum in Taiwan over the past two years. Local start-ups received \$219 million in funding across 13 disclosed deals in 2014, the highest level in six years, although GIC Private's investment in music streaming platform KKBOX accounted for nearly half of that.

So far this year, there have been seven disclosed investments worth a collective \$94 million, compared to \$88 million for 15 deals in 2013 as a whole, according to AVCJ Research.

The 2015 total includes a \$23 million Series B round for Taipei-based advertising technology company Appier, which was announced last week. Its investors include UOB Venture Management (UOBVM), a VC unit of Singapore bank UOB, Japan's Jafco, Silicon Valley-based TransLink Capital, and Taiwan corporate VC arm MediaTek Ventures. Existing backer Sequoia Capital also participated.

The three-year-old company uses artificial intelligence (AI) and machine-learning technology to optimize advertising campaigns for brands and analyze what users will do on

different smart device screens – ranging from smart phones to tablets to smart watches – at different times of the day.

"We're living in a post-mobile era, the era of cross screen," says Chih-Han Yu, CEO and co-founder of Appier. "Cross screen is no longer optional, but advertisers trying to reach customers online face mounting complexity as the number and types of screens multiply. And yet Asia lacks AI scientists to help make sense of this huge amount of information."

Yu has long been fascinated by AI, robotics and machine learning technology. While a student at Harvard and Stanford, he developed a self-adapting robotics system to help polio patients walk correctly, and helped create Stanley, an autonomous car that became the basis for Google's self-driving car project. AI-based cross screen analytics was the next step.

"According to our research, eight markets experienced growth in both two- and three-

device usage in the first half of 2015, so this trend is only set to continue," Yu says. "AI can help resolve this complexity and make cross screen easy for businesses here in the region."

The start-up has worked with more than 500 advertising clients since inception. It reported a 300% increase in revenue between 2013 and 2014, and a 600% increase since Sequoia led a \$6 million Series A round in June 2014. The latest funding has been earmarked for R&D, as well as for further expansion within Asia. Appier's international investors are expected to assist in this effort.

"UOBVM is very strong in Southeast Asia, a key market for us. Jafco specializes in helping companies strengthen their position in Japan as well as expand across Asia, with a particular emphasis on those of us in the technology sector. Both TransLink and our original partner Sequoia exemplify Silicon Valley's entrepreneurial heritage, while MediaTek is strong in Taiwan," Yu adds. ▀



Appia: Chih-Han Yu plus team

Meili Jinrong targets P2P consumer finance

OF THE NEARLY 3,600 PEER-TO-PEER (P2P)

online lending platforms operating in China, more than one third had run into trouble or gone bankrupt as of October, according to Online Lending House, a portal that tracks the industry.

As these platforms proliferated over the past couple of years, it was hoped they would fill a hole in China's inefficient banking system – helping small businesses obtain funding and by giving individual lenders higher investment returns. Venture capital activity grew in tandem with overall market interest. However, the rate of closures has risen sharply since the start of the year, as borrowers default on loans and industry controls become more restrictive.

"Online finance actually doesn't present a huge market opportunity along the lines of what we have in e-commerce and the online auto markets," says Yannan Liu, founder and CEO of online P2P site Meili Jinrong. "Investors and founders were previously too optimistic about this sector. In fact, entry barriers for setting up P2P lending platforms were very low, which led to higher default risks."

Liu, formerly of Merrill Lynch and TPG Capital, co-founded P2P lending site Yooli.com in February 2013. The platform, which received backing from Morningside Venture Capital and SoftBank China Capital, claimed it stood out from the competitive field because credit ratings are accessed by third-party institutions that aren't involved in the transactions.

In September, Liu left Yooli, reportedly due to strategic differences with his co-founders. He spun out Yooli's second-hand car financing business and set up Meili Jinrong. In addition to lending to car buyers, the company now also covers purchases of 3C products (computers, communication and consumer electronics) and home rental.

Liu has no longer holds any shares in Yooli and his new company last week received a \$65 million Series A round led by Bertelsmann Asia Investment (BAI). Morningside came back to Liu again, alongside GX capital and Chinese PE-

backed online personal finance site Wacai.com.

"When I started Yooli in 2013, investors had already shown their interests in consumer finance," Liu says. "That's why when I set up Meili Jinrong and several investors want to support us."

The company has a separate subsidiary through which it sources customers looking for car financing and matches them with investors on the main platform. A parallel consumer-focused subsidiary – Youyong Fenqi – has also been set up, targeting blue-collar workers who repay 3C loans in installments. Liu notes that this consumer group has a lower risk of default compared to the



Meili Jinrong: Auto financing

college students targeted by many P2P lending sites. JD Finance and Alibaba Group's Sesame Credit to assess borrowers' credit ratings.

BAI is also an investor in Fenqile.com, an electronics retailer that allows college students to pay in instalments. The firm has received backing from the likes of JD.com and DST Global. ■

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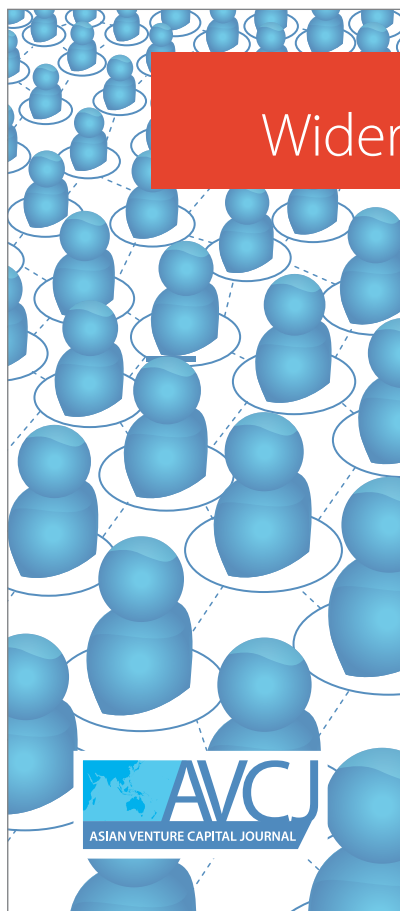
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First mover

The launch of Philippines-focused Navegar represented another breakthrough for Asian private equity. For Honorio Poblador IV, the firm's managing partner, it was more than a decade in the making

IT BECAME CLEAR TO HONORIO

Poblador IV and Javier Infante, over the course of the 2000s, that hardly anyone was willing or able to sink private capital into small- to mid-size Philippines companies.

Having previously attended the same high school and college, the two were neighbors in Singapore when Infante approached Poblador with a business proposition: He was looking for \$2 million to support Ambergris Solutions, a business process outsourcing (BPO) company set up in 2001. Poblador, then working at Morgan Stanley, had to turn down the opportunity; his firm's minimum check size was \$15 million.

Global BPO player Telus acquired a controlling interest in Ambergris in 2005, by which point Infante's attentions had by this point switched to another venture. Working with this Ambergris co-founders and several other business leaders, he launched Enderun Colleges, an undergraduate educational institution.

Needing to raise \$10 million to build a campus, Infante called on Poblador, who was by this point in the Philippines investing his own money and also investing on behalf of friends and family. Again, Poblador demurred, citing his limited resources. "We said, 'It's so hard to raise money in the Philippines; if you need a significant amount of capital there is no go-to guy. We should be doing this,'" he recalls.

However, it would be another five years before this ambition was realized with the launch of Navegar Fund, a dedicated Philippines private equity fund supported by Swedish alternative asset manager Brummer & Partners.

Transactional to principal

Poblador started out in investment banking in Hong Kong in 1996. After completing a management economics degree at the Ateneo de Manila University, he completed an MBA at Columbia University in New York and was then dispatched back to Asia. His employer was Barclays de Zoete Wedd (BZW), the predecessor to Barclays Capital.

When the equities and corporate finance divisions were sold to Credit Suisse in 1997 Poblador followed. He covered technology, media and telecom (TMT) at both firms. During this period, he worked on a number of notable "nearly deals," such as the initial attempt to

privatize Thailand's telecom sector following government-mandated liberalization.

"We had two mandates, one to advise the Ministry of Telecommunications on the sale of Communications Authority of Thailand [one of two state-owned enterprises, SOEs, in the sector], and the other to review concession fees amongst telecom operators," Poblador says. "We had been trying to unwind some of the mess brought by the bidding for concessions, where



"Private equity was becoming a hot sector in 1995-1997, particularly in Asia. I had read about it and was fascinated by it, but never thought it was the industry I would end up in; it was a very opportunistic move"

the winners ended up paying too much. Neither the privatization nor the attempt to rationalize concession fees happened."

By the time it did happen, in 2003, he was already established in PE. In 1999, Morgan Stanley Private Equity Asia wanted to build out a Southeast Asia team to complement its existing presence in Hong Kong. Poblador joined the Singapore office but within a year was back in Hong Kong as the two offices were merged.

"I had no specific plan to get into private equity early on in my investment banking career," he says. "Private equity was becoming a hot sector in 1995-1997, particularly in Asia. I had read about it and was fascinated by it, but never thought it was the industry I would end up in; it was a very opportunistic move."

Morgan Stanley was combining traditional private equity investing with forays into the technology space, operating primarily in South Korea, China and Japan. The firm's first dedicated Asia fund didn't come until 2005; before that it was the Morgan Stanley Global Emerging Markets Private Investment Fund, a 1997 vintage vehicle with a corpus of \$330 million.

The deal with which Poblador was most closely involved was eAccess, Japan's first DSL provider. It was essentially a start-up deal: Morgan Stanley, Goldman and Orix Corp. provided around \$40 million to support Sachio Semmoto, founder of mobile carrier DDI, on a new venture. After a few more rounds of funding, eAccess raise went public in 2003 and is now a unit of SoftBank Corporation.

Poblador credits Morgan Stanley with helping

him transition from a transactional to a principal capital mindset. "The way we valued transactions was very different – it is almost mechanical when you are on the investment banking side, but you have to be more careful about projections and more diligent in figuring out what matters when you are on the principal side."

There and back again

It was in the early to mid-2000s, having returned to the Philippines, that he passed on the Enderun Colleges investment. Poblador describes this period in his life as somewhat experimental. Companies in the Philippines were too small to attract meaningful interest from foreign investors, and so he completed a number of small-ticket deals on an independent basis – filling a small portion of the country's private funding hole.

This ended in 2005 with a call from Andrew Rickards, Asia CEO at Rothschild, who was trying to set up an in-house PE arm. "He said, 'I need you to help me, but you have to be on the inside. The only way you are going to do that is by returning to investment banking,'" Poblador recalls.

As the executive responsible for Rothschild's

Philippines business, and financial sponsor coverage in Southeast Asia for a while, he advised on the privatization of the National Transmission Corporation and the acquisition of eTelecare by Providence Equity Partners and Ayala Corporation, among others. Getting the PE arm off the ground was a side project and progress was far slower than expected. Rickards departed in 2007 to set up Providence's Hong Kong office.

Throughout his time at Rothschild, Poblador continued his dialogue with Infante about starting a Philippines-focused private equity firm. "The only thing missing was someone to help us raise the money. We thought we could raise \$20 million on our own, but that's not a private equity business – 2% of \$20 million wouldn't have been enough to cover our operating costs," he says.

In 2010, the missing piece fell into place. Poblador and Infante were put in touch with Brummer. The Swedish group had raised \$88 million for the first-ever Bangladesh-focused PE fund (a successor vehicle launched last year) and was looking for a new project in Asia.

Speaking at the AVCJ Philippines Forum in September, Anders Stendebakken, managing director at Brummer, offered a list of reasons why the country was so attractive: strong and reasonably predictable GDP growth; an economy not driven by the same forces as others in Asia;

a stable currency; favorable demographics; and the potential to be a relatively early mover in the private equity space.

"What was remarkable to us when we were looking at it a few years ago was that even though the stock market here has about 50% foreign participation we had an opportunity to be one of the first movers in growth capital – investments of \$10-20 million, mainly minority, sometimes control," he said. "That space was wide open."

Breakout phase

After traveling to Stockholm to make a presentation to senior members of the Brummer team, Poblador, Infante and their new partner started fundraising in 2012. Third-party commitments came from a string of development finance institutions, including the International Finance Corporation, Germany's FMO and DEG of the Netherlands, as well as from several European family offices. Navegar Fund has PHP5 billion (\$106 million) in committed capital.

"When we raised the fund we knew there was an opportunity but we didn't know how to define that opportunity. We didn't know how many opportunities we would get to look at, and we didn't know what the bite sizes would be,"

says Poblador, who transitioned to an advisory role at Rothschild shortly after fundraising started. "We have since deployed 50% of the money and bite sizes have been \$15-18 million – this is a sweet spot, because nobody in the Philippines provides that amount of money to private businesses."

Stendebakken said that in the past two-and-a-half years Navegar had considered 186 potential investments, signing 12 letters and completing three transactions. Those three deals also cover industry sweet spots, namely services, consumption and healthcare. Navegar has backed BPO provide TaskUS, local healthcare maintenance organization (HMO) Intellicare, and The Bistro Group, a premium casual dining operator with over 50 restaurants nationwide.

None of these transactions moves the needle in terms of overall private equity deal flow in the Philippines, and even at Navegar's end of the market companies have more capital-raising options than before, including IPOs and investments from strategic players. But on balance, Poblador is pleased by what he is seeing.

"There have been some large transactions over the last two years, and a lot of private equity guys come through the Philippines. Most of them come to see us to get our insights," he says. "So for sure there is a lot of interest." ■



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