

US\$5.8B Flows into Chinese VC Market

By Zero2IPO Research Center

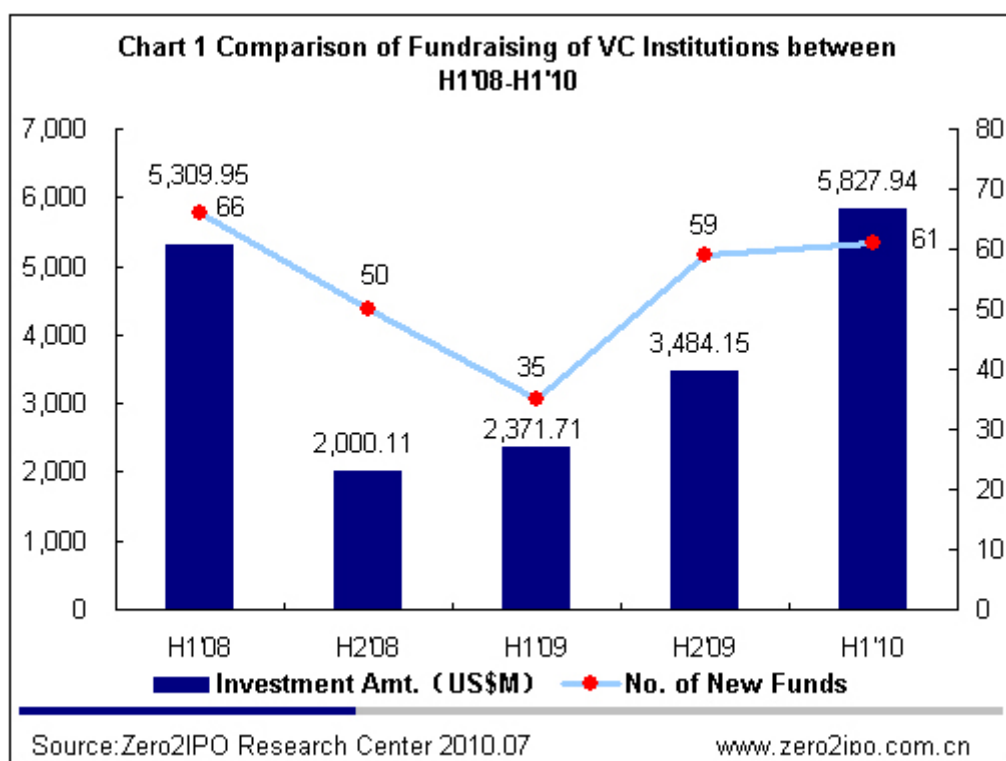
According to the data recently published by Zero2IPO Research Center, a well-known VC and PE research institute in Greater China, the global economy will remain volatile against the backdrop of a widening European sovereign debt crisis and a weak US economic recovery. External factors would have a limited impact on China's economy, despite inflation expectations and asset bubbles. But with the active policy adjustment initiated by the Chinese government, the local economy is expected to remain on a moderate growth path in 2010. Against such a background, China's VC market saw an upbeat momentum in terms of newly-raised funds in H1'10, with the overall amount raised almost comparable to that of the entire 2009. The foreign currency-denominated funds regained their dominant position, but the enthusiasm about RMB-denominated funds remained unabated. While the total investment amount saw a slight decline, the market saw a marked growth from the same period last year. The Internet sector remains an investment hotspot, while bio/healthcare and clean-tech sectors have also been a focus. In terms of currency denomination, RMB-denominated investment dominated, though the average value per deal was still small. The total number of exit transactions saw an increase, with the proportion of exits via IPOs growing further.

According to the statistics from Zero2IPO Research Center, local and foreign VC institutions raised a combined 61 new funds in H1'10, with newly-added capital available for investment in Chinese mainland standing at US\$5.83B. In terms of investment, 295 investment deals were closed in H1'10, including 235 deals with a total disclosed value of US\$1.59B. In terms of exits, a total of 136 VC exit deals were closed in H1'10, including 123 exits via IPOs.

The statistics and conclusion were mainly derived from the Q1'10 China Venture Capital Report and Q2'10 China Venture Capital Report of Zero2IPO Research Center. The Center began to conduct nationwide quarterly and yearly survey and rankings of China's VC market in 2001, and has since published quarterly and annual research reports.

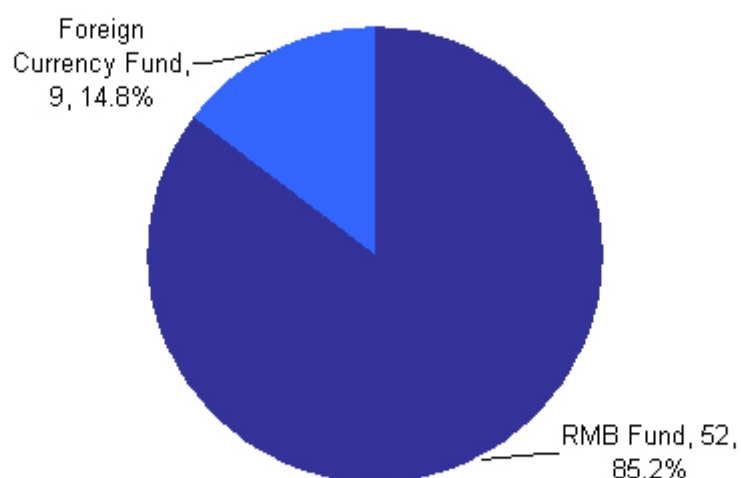
VC fundraising scale comparable to that of the entire 2009, with raised funds posting a new record high in 10 years

Both the number of new funds and the amount raised saw a beautiful upturn curve in China's VC market in H1'10, building a very upbeat momentum. A total of 61 new funds were raised by local and foreign VC institutions, up 3.4% from H2'09, or up 74.3% from H1'09 when 35 new funds were raised, apparently pointing to a quickly recovering market. The amount of new capital available for investment in Chinese mainland stood at US\$5.83B, jumping up 67.3% and 145.7% from Q1'10 and Q2'09, respectively. The reading was also larger than the previous peak of US\$5.31B recorded in H1'08, and almost equaled to the total funds raised in the entire year of 2009 (See Chart 1).



Since the outbreak of the financial crisis, RMB-denominated funds underpinned by strong competitive advantages had been quickly overtaking foreign currency funds in terms of fundraising, with both the number of new funds and the amount raised exceeding those of foreign currency funds even in Q1'10. Overall, foreign currency funds saw a strong rebound in H1'10, as the total amount raised by these funds regained the leading position, though the number of new foreign currency funds was far smaller than that of new RMB funds. (See Chart 2 and Chart 3)

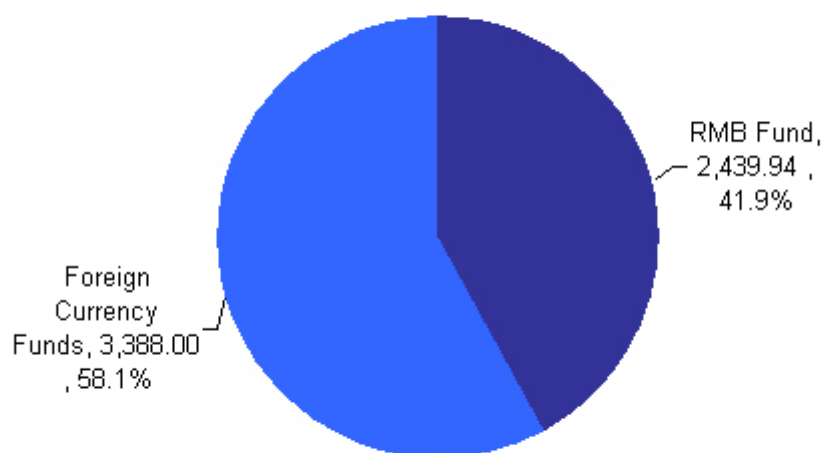
**Chart 2 Comparison of Funds Raised in H1'10 by Currency
(By No. of Deals)**



Source: Zero2IPO Research Center 2010.07

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**Chart 3 Comparison of Funds Raised in H1'10 by Currency
(By Investment Amt., US\$M)**



Source: Zero2IPO Research Center 2010.07

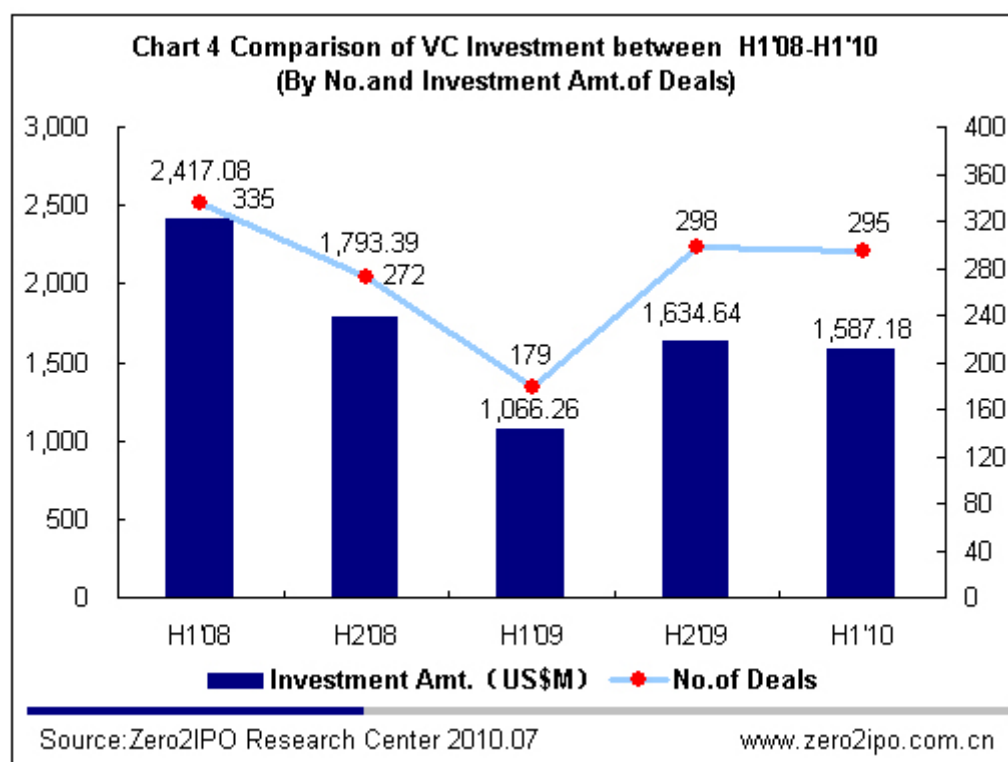
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As the shadow cast by the financial crisis gradually clears up, the overseas LPs have revised their cautious investment strategies to some extent, with some well-known VCs including SAIF Partners, Sequoia Capital, NEA, and others successfully raising large-scale USD-denominated funds, directly pulling up the total amount raised by USD-denominated funds. Locally, Chinese LPs saw a rapid expansion, as the promulgation of the Several Opinions of the State Council on Encouraging and Guiding the Healthy Development of Private Investment, also known as the "36 Articles", which has encouraged

private capital to enter the market. In H1'10, the National Council for Social Security Fund also resumed its investment by injecting over RMB3B into CITIC Mianyang Private Equity Fund and IDG's Harmony Growth Fund. Institutions including private banking units of commercial banks as well as third-party money managers have also successfully opened up the channels between wealthy local individuals and VCs. QFLP pilot program is also likely to be launched soon. Overall, the RMB funds still have very strong potential to compete.

The aggregate value of investment saw a substantial year-on-year increase, despite a small quarter-on-quarter drop

A total of 295 investment deals were closed in H1'10 in China's VC market, including 235 deals with a total disclosed value of US\$1.59B, with the total number of deals and aggregate deal value down 1.0% and 2.9% from H2'09, respectively. But by comparing with Q2'09, it can be seen that China's VC market is bouncing out of the bottom since the outbreak of the financial crisis (See Chart 4)



In addition, given the pre-crisis peak recorded in 2008, the total investment in China's VC market still has a big upside potential. There is a correlation between fundraising and investment. Given the upsurge in the total number of new funds raised in H1'10 and ample capital in the hands of VC institutions, we expect the overall investment in China's VC market will increase in H2'10.

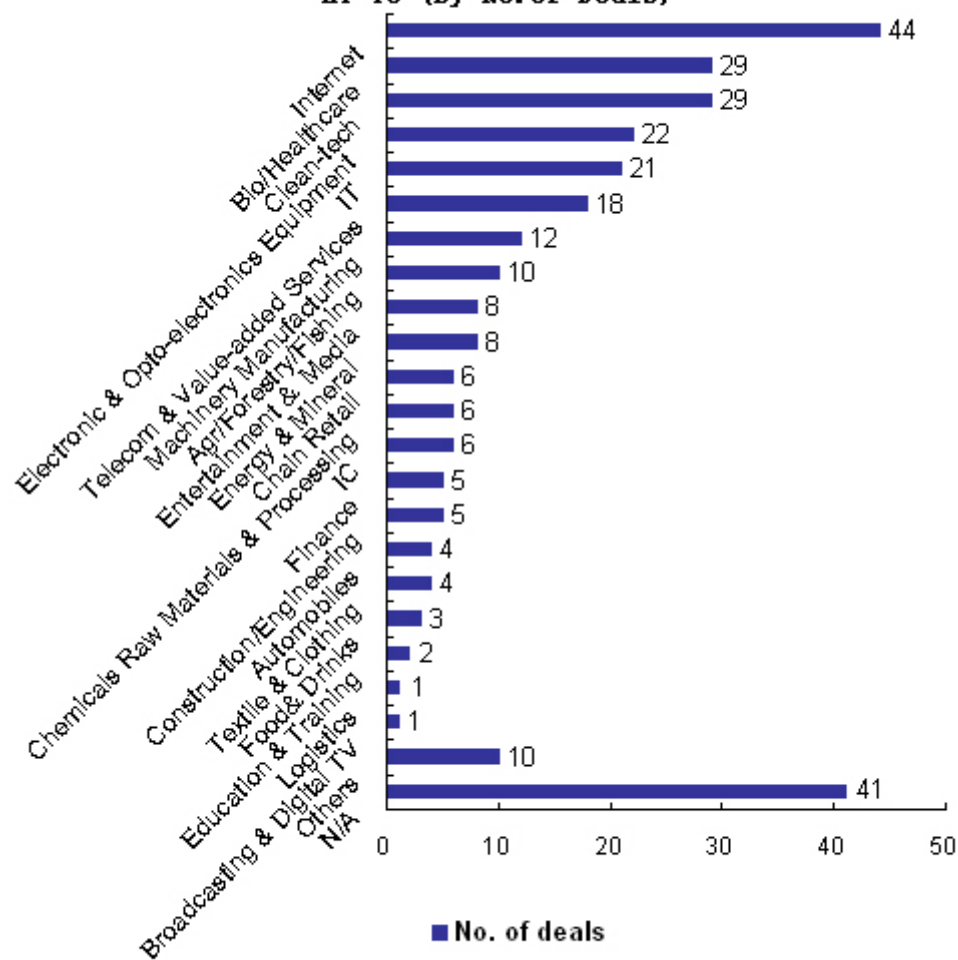
Internet regained favor after a decade; Bio/Healthcare and clean-tech also became a focus

The investment in Internet saw a superior performance in H1'10, with 44 investment deals worth US\$209M closed, running ahead of other sectors with clear margins. According to the statistics from CNNIC, the number of China's Internet users grows rapidly, with the annual increase exceeding 85M new Internet users for 2 consecutive years, and the Internet's penetration rate also rose to 28.9% at the end of 2009 from 16% in 2007. Such a high growth rate in the number of Chinese Internet users foreshadows a

large room for development. In subsectors including e-commerce, online game, online communities, as well as supporting logistics and distribution, electronic payment, and other areas, there are many investment opportunities.

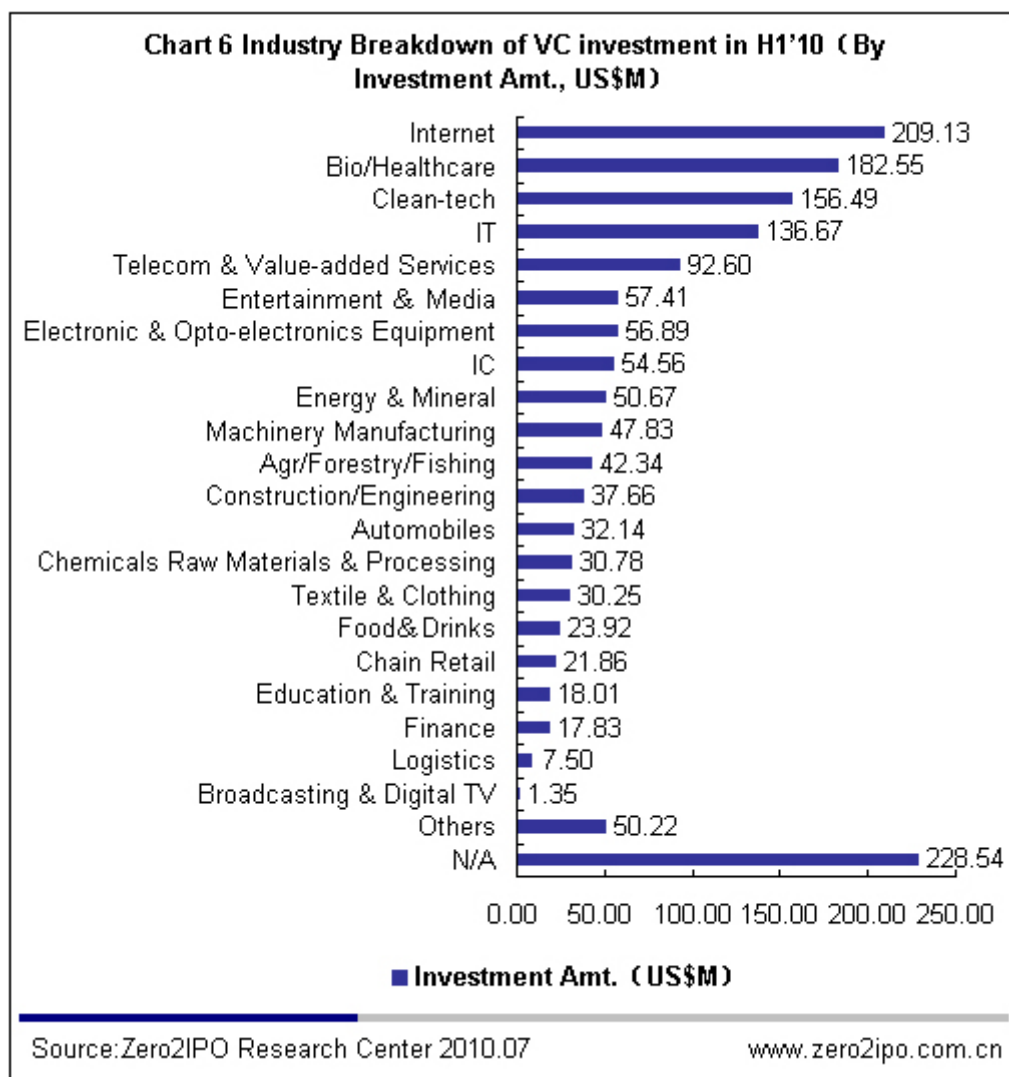
Second only to Internet, bio/healthcare sector saw 29 investment deals closed, involving a total value of US\$183M. China's healthcare sector has a huge market base. With the announcement of the new healthcare reform plan and the improvement in citizens' health awareness nationwide, the bio/healthcare sector will see more development opportunities and will also usher in a lot of investment and M&A opportunities. Clean-tech sector ranks third, with 29 deals involving a total investment value of US\$156M. (See Chart 5 and Chart 6)

Chart 5 Industry Breakdown of VC Investment in H1'10 (By No. of Deals)



Source : Zero2IPO Research Center 2010.07

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RMB-denominated investment dominates, but average value per deal is still small

According to the statistics from Zero2IPO Research Center, while foreign currency-denominated investment had been historically dominating Chinese VC market, H3'08 marked a watershed period as RMB-denominated investment staged an outperformance. In 2010, USD-denominated funds have adopted prudent investment strategies due to the financial crisis, with foreign currency-denominated

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