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INVESTMENT, PRIVATE  
EQUITY, AND MULTI-TIER  
CAPITAL MARKETS IN  
CHINA

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# Financial Sector Development and Private Equity in China

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<sup>1</sup> The views expressed in this presentation are those of the author and should not be attributed to the IMF, its Executive Board, or its management.

# Capital Market Development: Progress toward multi-tier market

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- **Bank reforms:** progress in recent years (recapitalization; restructuring; IPOs; strategic investors).
- **Equity market:** non-tradable share reform; increase in IPOs; increase in market size since 2006.
- **Corporate bond market:** reforms underway to ease regulatory burden (quota; interest cap).

## But banks/capital markets still finance small share of investment

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- Fixed asset investment still financed mainly by retained earnings (55-60 percent).
- Outside financing mainly bank loans (20 percent). Equity and bonds still have very small role.
- And large SOEs dominate bank loans, as well as equity/bond finance. SMEs/private firms crowded out.

# Role of private equity/venture capital

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- Additional source of financing, particularly for unlisted companies, including SMEs and private companies.
- In several countries, PE/VC important in financing start-ups/innovative firms (e.g., Silicon Valley).
- Comes with risks: transparency important.

# Private Equity/Venture Capital in China: Small but growing fast

## Private equity and venture capital investment (\$, bns.)

	2006	2007 (first 11 months)
PE Investment	7.7	12.49
VC Investment	1.8	3.18
Total PE/VC Investment	9.5	15.67

Source: Zero2IPO research center

# Some hurdles

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- **Company Law:** until recently did not allow limited liability partnerships.
- **Exit routes:** IPO, share transfer, mergers. But secondary exchange needs more development (like NASDAQ).
- **Onshore structures:** Most funds set up using offshore structures and foreign currency. International firms asking to set up onshore RMB funds.