Speech by SFST at 17th HKVCA China Private Equity Summit (English only)

Following is the speech by the Secretary for Financial Services and the Treasury, Mr James Lau, at the 17th Hong Kong Venture Capital and Private Equity Association (HKVCA) China Private Equity Summit today (June 5):

Eric (Chairman of the HKVCA, Mr Eric Mason), Conrad (Conference Chairman, 17th HKVCA China Private Equity Summit, Mr Conrad Tsang), distinguished guests, ladies and gentlemen,

Good morning. I am delighted to join you all today to share my thoughts on the opportunities for private equity in China's new era of economic development.

The remarkable story of China's economic transformation is well documented. According to the IMF, China's GDP in 1980 was US$305 billion, amounting to 2.7 per cent of the world's GDP. Last year, China's GDP was over US$12 trillion, amounting to 15 per cent of the world's GDP, but it contributes some 30 per cent of global economic growth.

In terms of trade, China's total trade amounted to US$21 billion in 1978, accounting for 0.8 per cent of the world total. Last year, the amount was over US$4 trillion, accounting for 11.5 per cent of the world total, making China the largest trading entity out of 204 economies.

In 2018, 40 years after the start of China's economic reform, China's GDP has grown by over 40 times over the period. China's latest development strategies continue to provide plentiful investment opportunities for private equity.

First, China is moving from an investment-based economy to one where consumption now is a key component of growth. There will continue to be strong appetite for retail products, increased expenditure on leisure pursuits and robust demand for education and healthcare.

In particular, I would like to highlight the active role of private equity in the healthcare industry. According to Asian Venture Capital Journal, private equity investments in China's healthcare industry totalled US$2 billion in 2017, up from US$686 million in 2016. Indeed, Beijing's policy reforms aimed at building a competitive healthcare industry have drawn in private investment in what McKinsey estimates could be a US$1 trillion industry by 2020.

Relevant to the consumer theme is an interesting investment thesis by Morgan Stanley economists, arguing that it is the smaller cities that will drive China's consumption boom. In a recent report, the investment bank estimated that China's private consumer market will grow from its current

US$4.4 trillion to US$9.7 trillion and account for 47 per cent of China's GDP by 2030, and that lower-tier cities will fuel two thirds of the national consumption increase from 2017 to 2030.

This is not surprising because there is some consumption catching up to do for the increasingly prosperous smaller cities. The relative affordability of properties in lower-tier cities together with more flexible official residency policy could bring better social security coverage and reduce the need for precautionary passive savings. This would mean lower living costs and higher consumption power in lower-tier cities.

Secondly, China is seeking to transform itself from the "factory of the world" to an entrepreneurial and innovation base driven by more high value-added industries.

Today, China is home to a dynamic start-up scene and has emerged as a global leader in Internet finance. Underpinned by a huge domestic market, a high mobile penetration rate, and an open and supportive regulatory environment, China has embraced a development strategy with innovation at its heart.

Last year, more than half of the 406 blockchain-related patent applications in the World Intellectual Property Organization's database were from China. Various studies have highlighted China's numerous investments in artificial intelligence, in applications ranging from drones to autonomous vehicles.

According to a report released by the Hurun Research Institute in April this year, China had more than 150 unicorns at the end of March, with a combined value of over RMB4 trillion, around US$630 billion. These include over 30 new unicorns that were added to the list in the first quarter of this year. In comparison, data from CB Insights suggests that the US is home to around 235 unicorns worth US$812 billion.

What is interesting is that the start-ups in China appear to be scaling up faster than those in the United States. A report by the Boston Consulting Group suggests that Chinese tech start-ups are reaching the US$1 billion mark for unicorns three years faster than their U.S. counterparts, taking an average of four years, compared to seven for American companies.

One observation in this space is in relation to the role played by corporate investors such as Alibaba and Tencent, which have invested in many unicorns in China. On the one hand, China's technology giants may be competitors to private equity firms in chasing investment opportunities in promising start-ups. On the other hand, strategic sales to these companies can bring exit opportunities for venture capital investments by private equity firms.

Thirdly, China is keen to develop environmentally friendly cities and industries and has emerged as a leader in the global green economy. According to the Institute for Energy Economics and Financial Analysis, China was the biggest investor globally in renewable energy last year, with a total investment of US$44 billion in clean energy projects, a 40 per cent increase over US$32 billion in 2016.

Indeed, China currently accounts for around 60 per cent of global solar cell production, while the country's global presence in wind power is also rising. In addition, China is a bright spot for electric vehicle sales and plays a crucial role in the industry. Electric vehicles are expected to account for 34 per cent of global sales by 2035.

In fact, green funds are thriving in China. Aside from the Clean Development Mechanism Fund of the Ministry of Finance, many provinces and cities have established regional green development funds. Private green investment funds, such as the US-China Green Fund, have also been set up, and there are over 260 green funds registered with the Asset Management Association of China.

Fourthly, China is also the proponent of the Belt and Road Initiative, which aims to strengthen trade and promote investment along the Silk Road Economic Belt and the Maritime Silk Road. There is huge potential for private equity investments in infrastructure along the Belt and Road economies.

According to the Asian Development Bank, as much as US$1.7 trillion a year will need to be invested in infrastructure in Asia until 2030. The Asian Infrastructure Investment Bank puts the estimate at an even higher figure of US$2.7 trillion per year.

The Hong Kong Monetary Authority has set up an Infrastructure Financing Facilitation Office, which provides a platform for collaboration in infrastructure projects. To date, around 80 key stakeholders have joined as partners, including multilateral development banks, financiers, pension funds, insurance companies, commercial banks, professional services firms, and of course private equity funds.

Having looked at the four clusters of opportunities for private equity in China, let me now speak briefly on the types of investments we are likely to see for both private enterprises and state-owned enterprises.

One trend among private enterprises is the increase in buyouts by private equity firms. According to Bain & Company, the value of private equity buyout deals in Asia almost doubled to US$72 billion last year. In China, the growing number of buyout opportunities is attributed to the void in business succession that Mainland entrepreneurs face when their next generation does not want to take over their family businesses. Growing competition has also prompted first-generation entrepreneurs to seek operational transformation and resource injection for their companies.

Another trend we are seeing is increased opportunities to invest in state-owned enterprises in collaboration with state-owned restructuring funds, under ongoing mixed ownership reform. Private equity investors may be in a position to help state-owned enterprises improve their governance structure and implement more market-driven decision-making processes.

Finally, let me conclude by saying a few words on Hong Kong's role as a private equity hub. Hong Kong is the second largest private equity hub in Asia, just behind Mainland China. According to the Asian Venture Capital Journal, as at end-2016, the capital under management of private equity funds in Hong Kong amounted to US$120 billion. We have excellent financial infrastructure, a huge talent pool of investment and fundraising professionals, and strength in professional services such as law and accounting, all of which are essential to private equity businesses.

In addition, profits tax exemption for offshore funds was extended to private equity funds starting July 2015, and we are also currently studying the proposal to introduce a limited partnership regime in Hong Kong to make Hong Kong a more attractive location of domiciliation for private equity funds. Issues being considered include the legal framework for limited partnership as a fund vehicle as well as the associated tax treatment.

Last but not least, our vibrant equity market provides an exit option for private equity investments. Our Stock Exchange has just put in place a new listing regime for companies from emerging and innovative sectors, and we are already seeing sizeable applications under the new rules.

One major change to our listing requirements is tailor-made for biotech companies, taking into account their long and costly journey of turning research into effective products and applications. Biotech companies with no prior record of revenue or profit are now allowed to list on the Main Board of Hong Kong's Stock Exchange, subject to certain requirements. There is specific guidance for biotech sectors such as pharmaceuticals, biologics and medical devices.

The second listing change is to permit high growth and innovative companies with weighted voting rights (WVR) structures to list on the Main Board of our Stock Exchange, subject to requirements in market capitalisation, business model, role of research and development and track record in business operations.

Since companies with WVR structures potentially carry additional risks to investors, we have also put in place certain safeguards, such as requirements for WVR beneficiaries, limits on WVR powers and enhanced corporate governance and disclosure. Our safeguards introduce a higher standard of corporate governance and investor protection, and we believe this will attract more investor interest in such WVR companies.

In short, with appropriate safeguards in place, our listing reforms will deepen and broaden our fundraising platform and increase our overall competitiveness, thereby providing an attractive exit option for private equity investments.

Ladies and gentlemen, I attempted a tour of the horizon on the investment opportunities in private equity in China. China is a massive consumer market, home to a dynamic start-up scene, a leader in the global green economy, and the proponent of the Belt and Road Initiative. Hong Kong's experience, expertise and international connections allow us to be a vibrant private equity hub, and our recent listing reforms in particular present an attractive exit option for private equity investments. I am sure you are all well placed to capitalise on these opportunities and I wish you a successful conference. Thank you.

Red flags hoisted at several beaches

Attention TV/radio announcers:

Please broadcast the following as soon as possible:

Here is an item of interest to swimmers.

The Leisure and Cultural Services Department announced today (June 5) that due to big waves, red flags have been hoisted at Stanley Main Beach, Turtle Cove Beach, Shek O Beach and Big Wave Bay Beach in Southern District, Hong Kong Island; Silverstrand Beach, Clear Water Bay First Beach and Clear Water Bay Second Beach in Sai Kung District. Beach-goers are advised not to swim at these beaches.

Thousands join London Hong Kong Dragon Boat Festival 2018 (with photos)

Thousands of people enjoyed the London Hong Kong Dragon Boat Festival 2018, sponsored by the Hong Kong Economic and Trade Office, London (London ETO) on June 3 (London time). The festival took place in London's Docklands and helped raise money for Chinese charities in London.

The London Hong Kong Dragon Boat Festival is organised by the London Chinatown Lions Club, the London Chinese Community Centre and the Hong Kong Executives Club. Thirty-three dragon boat teams took part in a full day of racing. The teams were drawn from all walks of life, from the local community and from businesses, public organisations and charities, and also included British Dragon Boat Association teams.

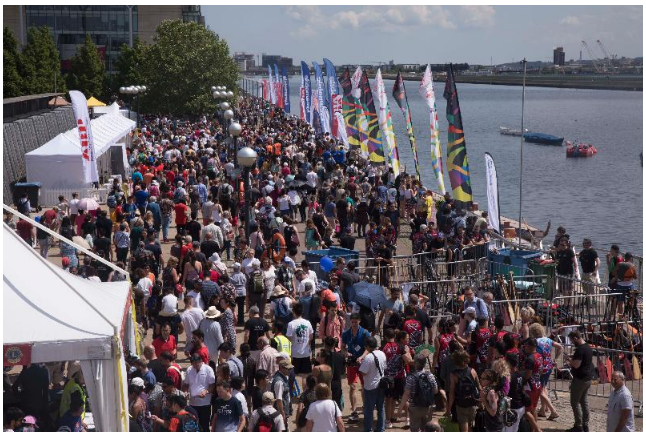
Addressing the opening ceremony, the Director-General of the London ETO, Ms Priscilla To, said that dragon boat racing dates back more than 2 000 years, and since Hong Kong held the first international dragon boat festival three decades ago, it has developed into a truly global event.

"Celebrating the Dragon Boat festival has been a significant part of Hong Kong's lifestyle. Nowadays, in many places around the world where there is a major Hong Kong community, we can find people celebrating this traditional festival. So, no wonder here in London, the London Hong Kong Dragon Boat Festival has also become a key event in the city's calendar.

"Dragon boat racing is emblematic of the strength, energy and competitiveness that Hong Kong is renowned for," Ms To added.

Apart from racing, the festival also featured cultural performances organised by Beat Nations, City Showcase, Chinese Youth Radio and Spectrum Radio. These included lion and dragon dances, live music from local and UK pop music acts and martial arts and tai chi demonstrations. There was also a food festival allowing people to try traditional food from Asia and all over the world.

More information about the London Hong Kong Dragon Boat Festival 2018 is available at www.dragonboatfestival.co.uk.



Hong Kong Customs seizes suspected methamphetamine (with photo)

Hong Kong Customs yesterday (June 3) seized about 3 kilograms of suspected methamphetamine with an estimated market value of about $1.6 million at Hong Kong International Airport.

A male passenger arrived in Hong Kong from Ho Chi Minh City, Vietnam, yesterday. Upon examination of his luggage, Customs officers found the suspected methamphetamine concealed inside the false compartments of three backpacks placed in his luggage. The 33-year-old man was then arrested.

Investigation is ongoing.

Under the Dangerous Drugs Ordinance, trafficking in a dangerous drug is a serious offence. The maximum penalty upon conviction is a fine of $5 million and life imprisonment.

Members of the public may report any suspected drug trafficking activities to the Customs 24-hour hotline 2545 6182 or its dedicated crime-reporting email account (crimereport@customs.gov.hk).

[Updates on CFS’ investigation on French raw milk cheese suspected to be contaminated with E.coli (O26)]

The Centre for Food Safety (CFS) of the Food and Environmental Hygiene Department said today (June 4) that the CFS had been closely following up on the incident of some French raw milk cheese suspected to be contaminated with Escherichia coli (E. coli) (O26) and had earlier suspended the import into and sale within Hong Kong of the affected cheese. CFS' further investigation and the latest information provided by the French authorities revealed that the product recall was extended to cover four other kinds of raw milk cheese which might be contaminated with E. coli (O26) and were manufactured by three processing plants. For the sake of prudence, the CFS has immediately suspended the import and sale in Hong Kong of all raw milk cheese products manufactured by the three plants. The trade should stop using or selling the affected products immediately if they possess them. Members of the public should not consume the products concerned if they have bought any.

The sanitary marks of the three plants are respectively FR 74.289.050CE, FR 74.096.050CE and FR 74.303.050CE. The four kinds of raw milk cheese include Demi-fromage AOP Reblochon laitier au lait cru (240 grams per pack) under the brand names of Chabert, Saveurs de nos Regions, and Nos Regions Ont du Talent as well as Fromage de Savoie au lait cru (450 grams per pack) under the brand name Tartiflard.

The CFS immediately contacted major local importers and retailers for follow-up. Preliminary investigation found that the above products have not been imported into Hong Kong. The CFS has also enhanced surveillance on raw milk cheese products imported from France. All results are satisfactory.

"People will contract E. coli causing gastro-intestinal disease through consumption of contaminated water or undercooked and contaminated foods. Intestinal bleeding and serious complications such as hemolytic uraemic syndrome may also develop in some people. Moreover, due to poor personal hygiene, person-to-person transmission of this pathogen is possible through the oral-faecal route. E. coli cannot survive under high temperature and can be killed by thorough cooking," said a spokesman for the CFS.

The CFS will alert the trade to the incident. It will continue to closely monitor the incident and take appropriate follow-up action. Investigation is on-going.