

## FINANCIAL INSIGHT: VENTURE CAPITAL



**DEAL #1: LALAMOVE RAISED US\$100 MILLION IN A SERIES C ROUND LED BY SHUNWEI CAPITAL A VENTURE FIRM FOUNDED BY XIAOMI CEO LEI JUN**



**DEAL #2: GOGO VAN MERGED WITH 58 SUYUN, THE FREIGHT DIVISION OF 58 HOME, TO FORM A US\$1 BILLION LOGISTICS FIRM**

# Hong Kong's venture capital investment hit record highs at US1.14b in 2017

Analysts reckon that Hong Kong is poised to have its own funding boom due to robust dealmaking in tech and logistics sectors and the government's HK\$2b Innovation & Technology Venture Fund programme.

When venture capital investment in Hong Kong more than doubled year-over-year in 2017, analysts took note that the island is starting to follow in the footsteps of Singapore and is poised to have its own funding boom, helped along by strong government support for local startups and robust dealmaking in the technology and logistics sectors.

Venture capital investment in Hong Kong reached a record US\$1.14b in 2017, continuing a rapid growth trend over the past three years, data from the Hong Kong Venture Capital and Private Equity Association, or HKVCA showed. This amount was more than double from US\$547.4m in 2016 and up sevenfold from US\$159.1m in 2014. Average deal size in 2017 climbed to US\$42.4m, also more than doubling from US\$19.6m and up more than tenfold from US\$3.9m in 2014.

The recent growth in venture capital investment has been underpinned by Hong Kong's favourable startup environment, said **Dennis Plomp**, principal at Nest Ventures, citing the rise in new coworking spaces and venture builders setting up shop in the island to help incubate startups. CBRE had estimated the total footprint of the coworking sector in Hong Kong would rise to 1.18 million sq. ft. by end-2017 from 700,000 sq. ft. in

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2016. Amsterdam-based coworking office provider Spaces led with a headline-grabbing agreement to rent a whole Grade B office block, the 77,000 sq. ft. Sun House at 90 Connaught Road, in Hong Kong's Central for an undisclosed price.

Plomp reckoned another key driver to the venture capital investment momentum is the steady improvement in funding availability over the past two years. "The funding does not only come from local investors, but also from Chinese and Southeast Asian capital providers. Active local investors include Alibaba Entrepreneurs Fund and the Hong Kong X Technology Fund," he said. "Furthermore, the pool of angel investor capital has grown considerably."

### Notable deals

Hong Kong's venture capital scene is "flourishing" with a focus on new technologies such as AI, blockchain, fintech, and healthtech, said **Lap Man**, co-founder and managing partner at Beyond Ventures, a Hong Kong-focused venture capital fund. In April 2018, one of the most notable deals was SenseTime raising US\$600 million in its Series C round of funding, with Chinese technology behemoth Alibaba Group taking the lead role

and Temasek and Suning, among others participating. Man, whose company Beyond Ventures is one of the shareholders before this round, reckoned this was regarded as the biggest round of funding in an AI company and the largest technology startup funding so far.

Plomp said SenseTime's Series C round placed the firm's valuation at US\$4.5b, and was a notable deal since the company started out in Hong Kong, before quickly taking off in China. Currently, SenseTime is one of the leading companies in AI globally, he said, and plans to use the fresh capital to further expand overseas and to develop industrial applications for its AI technology.

Looking a bit further back in 2017, notable deals were also focused in logistics firms GoGoVan and LaLaMove, according to **Denis Tse**, managing principal of Asia-IO Advisors Limited. Logistics on-demand platform startup GoGoVan, which operates in more than a dozen cities across Asia, merged with 58 Suyun, the freight division of 58 Home, to form a US\$1b logistics firm. Market observers had noted at the deal's announcement that the headline-grabbing, 10-digit valuation should serve to galvanize Hong Kong's startup scene.

Meanwhile, LaLaMove raised US\$100 million in a Series C round led by ShunWei Capital, a venture firm founded by Xiaomi CEO Lei Jun, with participation from previous investors including Xiang He Capital and MindWorks Ventures. The company said the funding will help fund talent and process improvements as it tries to expand rapidly across China and Southeast Asia, having already amassed more than 15 million users across 100 cities and a network that exceeds 2 million drivers.

"Logistics and the sharing economy have been key sectors in Hong Kong in the last few years," said Plomp, adding that "AI and blockchain will remain some of the hottest technologies in 2018."

## Bright outlook

Analysts held a bright outlook for venture capital investment in 2018, citing the continued improvement in the environment supporting local startups, and, in turn, the quality and quantity that are ripe for dealmaking.

"More and more venture capital firms have been formed to help drive the innovation ecosystem in Hong Kong and we are confident that the venture capital outlook for 2018 continues to be optimistic," said Man. "We also see more and more high quality startups in Hong Kong and as we expect by 2022, there will be at least 5 unicorns from Hong Kong."

Plomp said Hong Kong "will not be an exception" to the global trend of investors putting their money into fewer, "hopefully higher quality" deals. He also expects a pickup in M&A deals in the region, which would help create a healthy market for venture capital exits. "Many acquisitions will be driven by China's technology giants, as they look to expand internationally in various highly competitive geographies and industries."

But whilst Hong Kong appears to be building a more accommodating environment for planting venture capital seeds, it remains to be seen whether it can nurture those seeds into high-value fruits. "The Hong Kong venture



Dennis Plomp



Lap Man



Denis Tse

capital scene still has to demonstrate consistent long-term returns and success stories to justify the attention of big money," said Plomp. "Many local private equity and venture capital players are so far mainly interested in China or Silicon Valley."

## Taking to the next level

But in order to take Hong Kong's venture capital scene to the next level, the government has to support the island's young startup scene, analysts said. "Whilst Hong Kong's startup ecosystem has made progress in recent years, more needs to be done to nurture local startups and help them grow beyond our borders and contribute to Hong Kong's economy and international reputation," said Man.

Man noted that the Hong Kong government recently launched the HK\$2b Innovation and Technology Venture Fund, or ITVF, aims to stimulate private investment in local innovation and technology startups. The ITVF Corporation, which was set up as a special-purpose vehicle, will passively co-invest with partner venture capital funds in local startups at an overall matching investment ratio of approximately one to two. Partner venture capital funds must have a minimum remaining committed capital of HK\$120m when applying, amongst a few other qualifications, to be eligible for the co-investment arrangement.

"More and more Hong Kong startups have garnered support from investors, incubators and the government in various ways," said Man. "We can see a number of significant venture capital investments for Hong Kong startups in the past months. The momentum is expected to continue in the rest of the year."

"A few Hong Kong-backed companies are reaching growth inflection point and more are expected to follow suit. This growth cycle is similar to what we were seeing in Singapore around two years ago," said Asia-IO Advisors Limited's Tse.

Tse noted that one of the key factors driving the growth cycle is increasing government support, which was further bolstered by the recently announced Innovation & Technology Venture Fund, or ITVF. He said the ITVF effectively supports a HK\$6b investment programme -- HK\$2b from ITVF and HK\$4b from the private sectors -- and translates into a HK\$1.2b annual investment

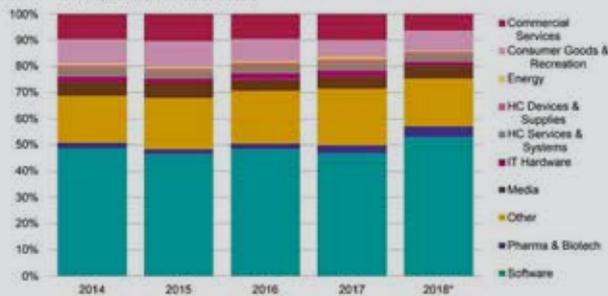
## Top 10 global financing in Q1'18



Sources: Venture Pulse, Q1'18, Global Analysis of Venture Funding, KPMG Enterprise

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Asia venture financings by sector



Sources: KPMG

outlay, assuming a five-year investment period. “This is roughly the total venture amount investment in Hong Kong as recently as 2014, before the market was tilted by a few large fundraising rounds in 2016-2017,” he said.

The ITVF also supports at least 66 rounds of venture investments since it can only contribute no more than HK\$30m in each company funding round. “This means that ITVF will have to proceed with some 13-14 investments a year, which would require a streamlined, rule-based approval process,” noted Tse.

“At a current rate of less than 30 cases of institutional venture rounds in Hong Kong, the ITVF’s target investment frequency could theoretically cover up to 45-50% of the current market size, enough to move the market.”

## Much needed push

Furthermore, Tse reckoned selected co-investing venture managers are expected to make at least three to four investments in Hong Kong a year, preferably without overlapping, which he sees as a “high level of commitment” given that less than 30 Hong Kong institutional venture rounds had been consummated yearly.

Partnering managers are also given a “generous” carry of 35% and “very low-cost” call option of 5.5% per annum or less to purchase ITVF’s unrealised portfolio, in spite of limitations that the ITVF is not intended to be a limited partner of an existing or a specially formed fund nor pays a management fee.

“Overall, in our view, ITVF is a potentially effective program that is well-designed to attract venture capital partners to prudently pursue investment in innovative Hong Kong companies based on commercial, risk-sharing principles,” said Tse.

Looking forward, Tse said that the ITVF must be part of a more comprehensive government strategy to stimulate innovation and commercialisation. This means the government must look to push for stock exchange reforms, income tax reduction for small enterprises and financial technology sandboxing, which would help “stimulate an impactful trickle-down effect on high-quality new enterprise formation for the real economy, which Hong Kong lacks.” It should also pursue a more progressive foreign talent attraction scheme, more entrepreneurship education, assurance for access for small and medium enterprises to basic banking services, and a friendlier regulatory environment for business model experimentation.

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## SINGAPORE VIEW

### ICO boom threatens VC scene in SG

When Uber bowed out of its Southeast Asian operations this year, it sent a clear signal to venture capitalists: transport and logistics startups have had their day. Whilst deals in technology, transport, and logistics, have dominated the scene and should continue to do so as seen in Grab’s \$2.5b Series G funding, funds will now start to pour into promising areas such as blockchain, medical technology, and artificial intelligence. Venture capital activity in Singapore is widely expected by analysts to maintain solid momentum not only for the rest of 2018 but also for the next few years due to an influx in growth-stage funds, a stronger corporate expansion drive into Southeast Asia, and an expected boom in attractive exit deals. But funds will likely have to fight tooth-and-nail for talent and deals amidst strong competition and a growing interest in initial coin offerings as an alternative fundraising path.

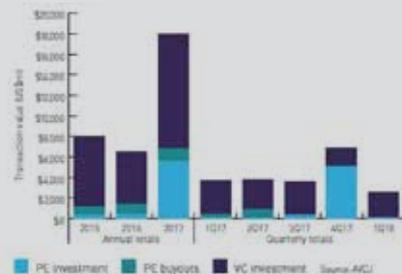
#### Notable deals

There have been a record 23 deals that raised US\$2.68b of venture capital funding in the first quarter of 2018, surpassing previous records, said Kenn Lim, senior associate at CNP Law. “Whilst we are still in the early half of 2018, we have witnessed a vibrant venture capital scene in Singapore thus far.”

Aside from the Grab-Uber deal, which saw the largest amount raised globally from venture capital funding in the first quarter of 2018, analysts said another notable deal in the early part of the year was logistics startup Ninja Van raising US\$85m in its Series C funding round, which was one of the largest ever raised in the region at that stage. These deals, together with venture capital firm B Capital Group closing out its first fund and raising US\$360m, suggests that “venture capital investors continue to invest large pools of money into late-stage companies, in part because of the number of unicorns that have remained private,” said Ken Cheung, partner at Bird & Bird ATMD. He added that so far in 2018 have been predominantly in the transport, logistics, and technology sectors.

One technology deal that was “notoriously underreported” was GO-JEK’s acquisition of Mapan, according to Justin Hall, principal at Golden Gate Ventures. He said the founders and assets of that sale will underpin GO-PAY, which he considers the region’s first “genuinely viable” mobile wallet that has “extraordinary” distribution, integration with many services, and the potential to spin off from GO-JEK.

### PE and VC tech activity in Southeast Asia by investment type



Source: KPMG