Comment

Politics

China's private equity haven status is slipping, but Middle East ties offer light

While political concerns may cloud opportunities for foreign investment in China, the country itself is steaming ahead with fundraising and developing closer ties with the Middle East, writes **Peter Lu**

China's reputation as a haven for private equity has begun to slip away in the eyes of many. With the reported number of United States dollar-backed deals on the decline, many predict the future for PE in China to be overshadowed by a multifaceted set of increasing challenges. Yet, while commercially sensitive political anxieties and regulatory concerns are a key element of any deal, it is worth questioning whether China's situation is that much different from other PE opportunities. Crucially, two things that have been severely overlooked amid a clamour of US-China commentary are the steady growth of state-backed yuan fundraising and the nascent economic connections that China is forming with the Middle East.

From China's Open Door Policy of the late 1970s to US President Joe Biden's 2023 regulations, the status of China's PE landscape — and the challenges resulting from its evolution — have long been viewed through the lens of the nation's proximity to foreign investment.

The marriage between entry into the World Trade Organization in 2001 and a fertile regulatory system produced a legal environment for foreign investment that could facilitate the rapid influx of US PE firms investing in China. On the heels of the dot.com boom came an accelerated investment into China from the likes of Blackstone, Caryle Group and other major US PE firms. This continued to the point that by the mid-2010s, more than two-thirds of total Asian PE investment was being channelled into China, overseeing the financial infrastructure necessary for China's tech boom.

More regulations

Recently, efforts to boost the economy and government-pledged backing for the private sector have come hand in hand with increased regulations. One seismic legislative change arrived on 1 January 2020, when China's Foreign Investment Law (FIL) and Implementing Regulations took effect. Investors have since had to pay close attention to sector-specific restrictions and ensure compliance with relevant FIL provisions. Regulatory action of this kind has been cited as a major hurdle for foreign investors.

There are four first-tier and six second-tier city funds that accounted for 63% of total Chinese PE equity deal volume between 2016 and 2022. As foreign investment has waned, domestic funds have picked up steam, especially as the Chinese economy drifts further away from the global Covid-19 slump. In 2022, Beijing Zhiguangxin Holding acquired Tsinghua Unigroup, one of China's largest semiconductor conglomerates, in a deal worth 54.9bn yuan (about $8.2bn). The local government of Guangzhou has followed suit, having recently invested ¥200bn (about $29bn) in technology-focused funds.

President Biden's declaration of a national emergency in August and consequential announcement of a set of stringent regulations on US investments into China in sectors such as semiconductors, quantum information tech and artificial intelligence has generated a ripple effect of political tension. This regulatory crackdown represents a degree of uncertainty and marks a significantly different attitude when compared to the urgency for the US dollar to make the most of China's meteoric rise through the 2010s.

Riyadh relationship

Sparked in December of last year when diplomatic ties between China and Saudi Arabia were bolstered during Xi Jinping's meeting with Crown Prince Mohammed bin Salman Al Saud, 2023 has witnessed this relationship bounce from strength to strength. The year began with China's esports company, VSPO, being backed by Saudi's Arabia Public Investment Fund in a deal worth $265m. Yet, it was not until June that relations were solidified at this year's Arab-China Business Conference in Riyadh, Saudi Arabia.

Together, the growth of these funds and the movement towards future collaboration gives more credibility to the prediction that China's economy will outperform every developed market in the coming decade. Another element that has drawn investors' attention to the Chinese market is the reality that China's stock market index is at its lowest point since February 2019.

While Chinese officials will continue to uphold strict due diligence processes for foreign investors and the economy will face the heat from the friction of US-China relations, China is well-prepared to disrupt the global PE playing field through its domestic scene and by making the most of new opportunities.

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Despite geo-political concerns, China is well prepared to take advantage of PE opportunities both at home and abroad

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