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Private equity investment can be welcomed with open arms in China, provided that you pick the right sector

Edan Lee, managing director of Olympus Capital Holdings Asia, manages funds worth more than US\$1 billion. About 20% of its latest fund is focused on mainland China. The company distinguishes itself by engaging in "active management" situations; 80% of the capital is invested in control or shared control deals. The sectors it favors include environmental-protection services, business process outsourcing and agribusiness.

Q: How much of an issue is local "protectionism" for PE funds in China?

A: Instead of seeing local "protectionism" as an issue, we actually see it as something we can use to our advantage. A lot of our transactions are approved at local level, and local governments are very proactive in promoting the interests of their industries. One thing to keep in mind is that China has for the past couple of decades relied on foreign direct investments to help develop industries. Every year, US\$60 billion still enters the country as foreign direct investment. On the other hand, the Chinese government is trying to take a balanced approach to the types of capital that can come in and play the active role. China is walking a fine line, welcoming the value-added capital that will bring expertise and open up new industries.

Q: What are the key metrics when evaluating the highly cyclical businesses in China?

A: We invest in companies with a competitive cost structure that can withstand cycles. Clearly, the cost of labor and land in China is quite competitive, although this is changing. But if you look at overall inputs, tax rates in many instances are quite favorable. You have to look at the infrastructure support, the entire cost package. Minzhong, a company in our portfolio that is involved in vegetable processing, probably has one of the most competitive cost bases on a global scale. They not only compete against other firms in China, but also against suppliers all around the world. For example, when you are supplying to the Western European market, you are competing against Eastern European and North African producers.

Q: What sectors do you see as holding the greatest profit potential?

A: The environmental sector, as our strategy is to invest in themes that the government supports. China's 11th Five-Year Plan aims to reduce energy intensity by 20%, increase the share of energy consumption coming from renewable sources and cut emissions by a substantial amount. Meanwhile, China has the one of the lowest levels of available per

capita water resources in the world. We have proactively invested in industries that are looking for ways to resolve these issues. And we are starting to see homegrown solutions. One of the companies we got involved in has done such a great job developing a low-cost solution which meets the technical standards and the requirement of the market that it is now beginning to export products and services to other countries. You can see the potential of companies that take Chinese businesses and turn them into multinational enterprises.

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