Asia Pacific Private Equity Barometer 2023

PE investment trends and opportunities

Thought leadership

In association with AVCJ

Content

01

Private equity in Asia Pacific: Down but definitely not out

Section 01

Private equity in Asia Pacific: Down but definitely not out

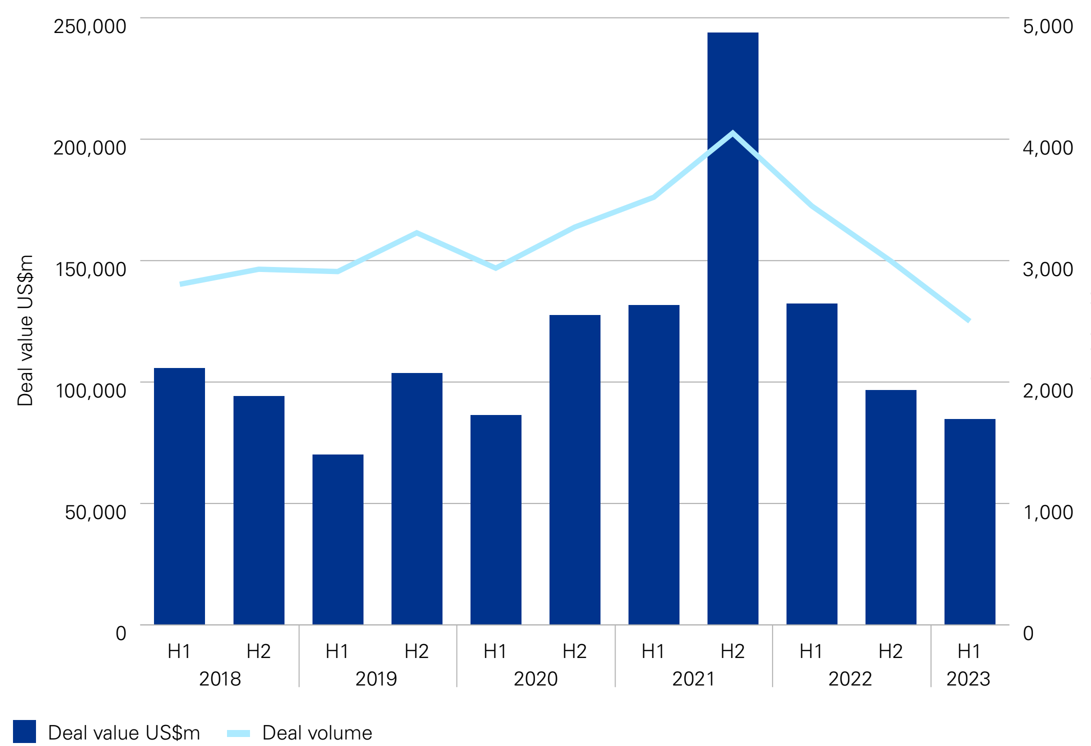
The years 2020-21 were without a doubt groundbreaking for the private equity (PE) industry in the Asia-Pacific (ASPAC) region. Buoyed by vast liquidity pools and enticingly low interest rates – not to mention digital acceleration and pandemic-induced opportunities – the region experienced a surge in PE investments.

However, as data over the last 12-18 months shows, this activity has lost much of its momentum. Total investment value across the region plunged by 36% to US$84.7bn in the first half of 2023. That's compared to US$132.3bn in 1H2022, which itself was a major dropoff from the five-year high of US$243.9bn recorded in 2H2021.

Clear and present challenges

Several factors have contributed to this downtrend. For starters, the frenzied activity in 2020-21 led to an overheated market. The widening delta between buyer and seller valuation expectations has seen many private equity investors become more cautious about overpaying for assets, while vendors are reluctant to sell at discounts to the prices that were on offer just 24 months ago.

Figure 1:
Asia-Pacific private equity investment trends



Source: AVCJ

Equally, rising interest rates and inflation in Western and Asian economies have dried up liquidity and increased borrowing costs. This is making it harder for private equity sponsors to secure financing for new deals.

At the global level, uncertainties ranging from supply chain challenges to geopolitical rifts between key markets have added to current complexities. And regionally, a slowing Chinese economy alongside regulatory changes and stricter government controls in China have made investment activity and outcomes less predictable.

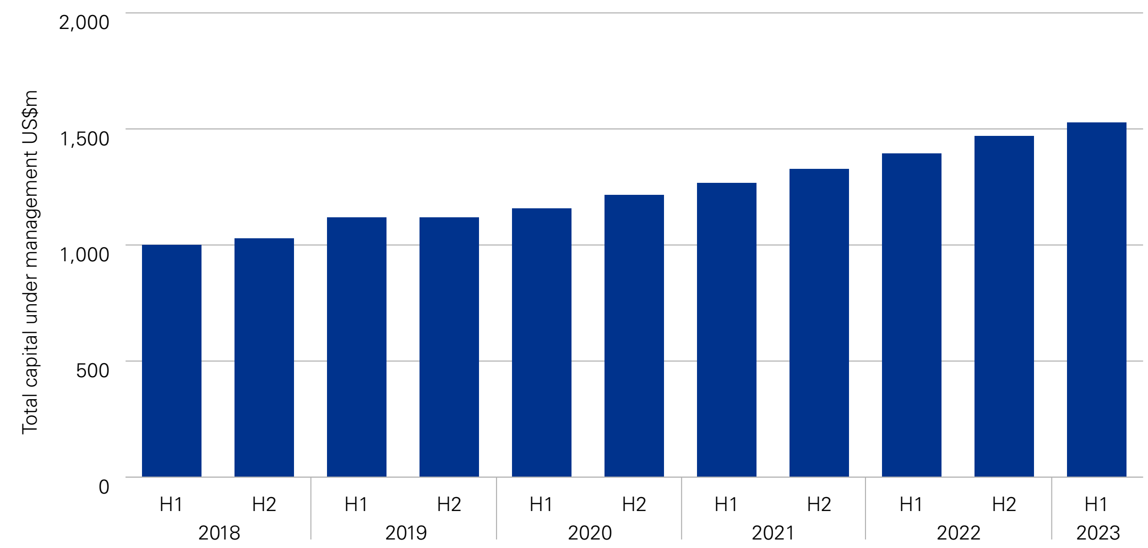
Slowing deal activity has meant private equity funds have been unable to generate exits and make distributions to investors that can then be recycled into new fund vintages. In addition, investors have also had to pare back new fund commitments because of the denominator effect, which has seen institutions over-allocated to private equity as valuations of other asset classes in their portfolios have oscillated.

Confidence in ASPAC remains strong

Yet, it's vital to understand that even while facing such a daunting list of challenges, overall PE investment remains confidently buoyant, echoing some of its pre-pandemic vibrancy. Likewise, the current tempering in the pace of activity, while noteworthy, isn't indicative of a lack of opportunities or interest but rather a market recalibration.

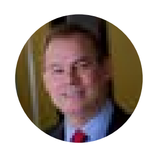
The maturing markets of ASPAC, their vast growth horizons and expanding middle classes are indeed promising. The ebb in activity is far from a retreat – and rising capital under management figures substantiate confidence in the private equity investment class for its ability to navigate market complexities and deliver outsized returns.

Figure 2:
Asia-Pacific total capital under management (US$m)



Source: AVCJ

"News of the death of private equity has been greatly exaggerated. While we have seen private equity investment dip to some of its lowest levels since the onset of the pandemic, the market remains robust and we're already seeing a strong deal pipeline start to take shape across ASPAC. While uncertainties remain, there are early indicators of a resurgence in 2024.



Andrew Thompson
Head of Private Equity,
KPMG Asia Pacific

Fundraising totals over the past year contribute to this optimism. While the number of funds declined, fund values remain on par with pre-pandemic raises. Managers targeting the region also still have long capital runways, with some estimates showing that ASPAC funds still have approximately US$680bn of uninvested dry powder available to deploy.

Outlook 2024

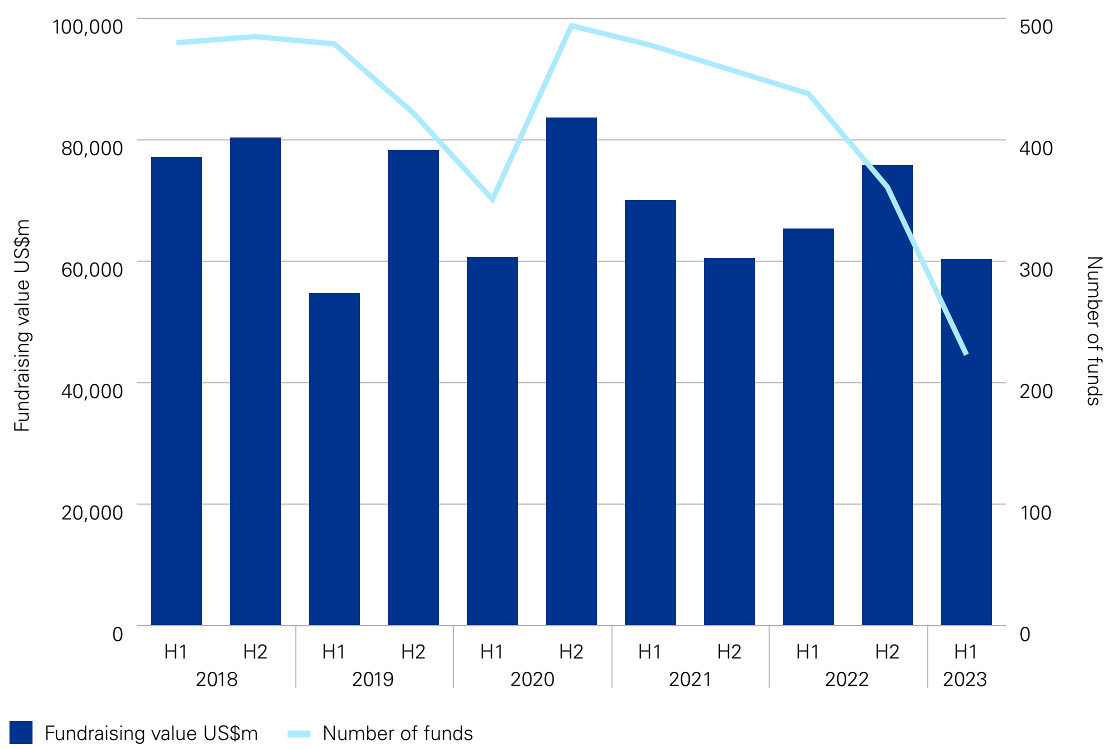
So what awaits investors as 2024 approaches?

The upcoming year promises to be a blend of prudence and ambition – and while the sheer volume of deals might harken back to quieter times, the number of opportunities across ASPAC only seems to be expanding.

For instance, a preference for ventures that not only promise profitability but also prove sustainable will be a theme as environmental, social and governance (ESG) considerations become primary investment criteria, emphasizing responsible growth. While China will remain pivotal, investors are eyeing alternative markets for fresher opportunities. The tech revolution, spearheaded by artificial intelligence (AI), is reshaping various sectors with ASPAC's unique blend of established and emerging tech hubs offering prime investment opportunities. Concurrently, the healthcare landscape is generating myriad opportunities, from eldercare in developed nations to digital health solutions in emerging markets.

The exit market, however, stands to be a challenge in the year ahead. In particular, record-low exit activity and the subsequent delays in returning capital to LPs could impact fundraising. This alongside a reluctance from investors, particularly those from North America, to commit to any fund with a China strategy will dampen capital raises.

Figure 3:
Asia-Pacific private equity fundraising



Source: AVCJ

Overall, market conditions are likely to remain challenging for the foreseeable future, but well-capitalized fund managers will be ideally positioned to see out this period of dislocation, invest in good assets at attractive valuations and emerge from the current downturn stronger than ever.

02

Navigating ESG: Moving beyond basics

Section 02

Navigating ESG: Moving beyond basics

ESG, once a niche concern, has surged to the forefront of investment strategies in recent years – and private equity firms in ASPAC are discovering that sidelining ESG is no longer an option. Rather, ESG should be central to investment strategies and infused within portfolio company operations. ESG is increasingly a "watermark" across all investment strategies.

Next steps

This represents a major shift in mindset. Historically, most PE firms in the region have viewed ESG as a separate compliance initiative, rather than an integral part of value creation. But with large LPs now assessing GPs on ESG performance and as funds integrate ESG data into early stage investment decisions, fund managers across ASPAC are rethinking how ESG can enhance returns.

At the heart of this change, leading ASPAC funds have started screening potential investments for ESG risks and opportunities. As such, due diligence has shifted from a mere exercise in numbers and profitability forecasts to one that extends to a company's carbon footprint, labor practices and governance models. They are also linking ESG performance to carried interest and portfolio company executive compensation. As ESG valuation premiums become more common capital is being deployed to take advantage of this trend.

Bridging the gap

While adopting ESG is becoming the norm, implementing it is a multifaceted challenge – and sometimes the gap between ESG intent and actionable strategy can often resemble a chasm. Smaller funds may lack the resources and expertise to collect ESG data and devise concrete improvement plans. Portfolio company management may be resistant to operational changes. And in emerging markets, like Vietnam and the Philippines, ESG consciousness among local businesses is still in its infancy.

To overcome these hurdles, PE firms in ASPAC are resorting to a blend of traditional wisdom and modern innovation. Some are strengthening in-house ESG capabilities with ESG director-level hires. These specialists don't merely act as gatekeepers during the investment phase but continue to shape the ESG trajectory post-acquisition.

Others are leveraging third-party consultants and auditors to collect ESG data and identify areas for value creation.

Regulatory pressure

However, as ESG benchmarks develop, they're shadowed by another key development: that of the regulatory landscape. Indeed, ASPAC's regulatory ecosystem is rich and diverse. China has begun to set the tone by embedding ESG considerations into corporate norms. Japan's influence is nudging markets towards a more ESG-aligned mindset. Meanwhile, Southeast Asian nations, like Singapore, are refining their sustainability reporting mechanisms, raising the bar for corporate transparency.

Global policies are also extending their reach. For instance, there is growing momentum behind mandating ESG disclosures, with major markets like the UK and EU finalizing corporate sustainability reporting standards. The US Securities and Exchange Commission is also expected to roll out climate disclosure rules for PE firms.

Regulatory scrutiny of ESG commitments will only increase going forward – and PE firms should prepare now to avoid being caught off guard as mandatory ESG reporting goes global.

Every deal is an ESG deal and between rising LP expectations and tightening global and regional regulations, ESG is quickly becoming mission-critical for PE firms' license to operate. Even if potential companies or target investments have strong financials and operations, if the ESK risks are too high, the deal probably won't go through.

Angus Choi
Partner, ESG Advisory,
KPMG China

03

Regional opportunities: Searching for the next China?

Section 03

Regional opportunities: Searching for the next China?

China has long been the cornerstone of ASPAC's private equity narrative, due in no small part to its economic dynamism and massive population. However, recent geopolitical tensions, coupled with sputtering economic growth and intensifying regulatory scrutiny, are leading investors to reconsider their ASPAC strategies.

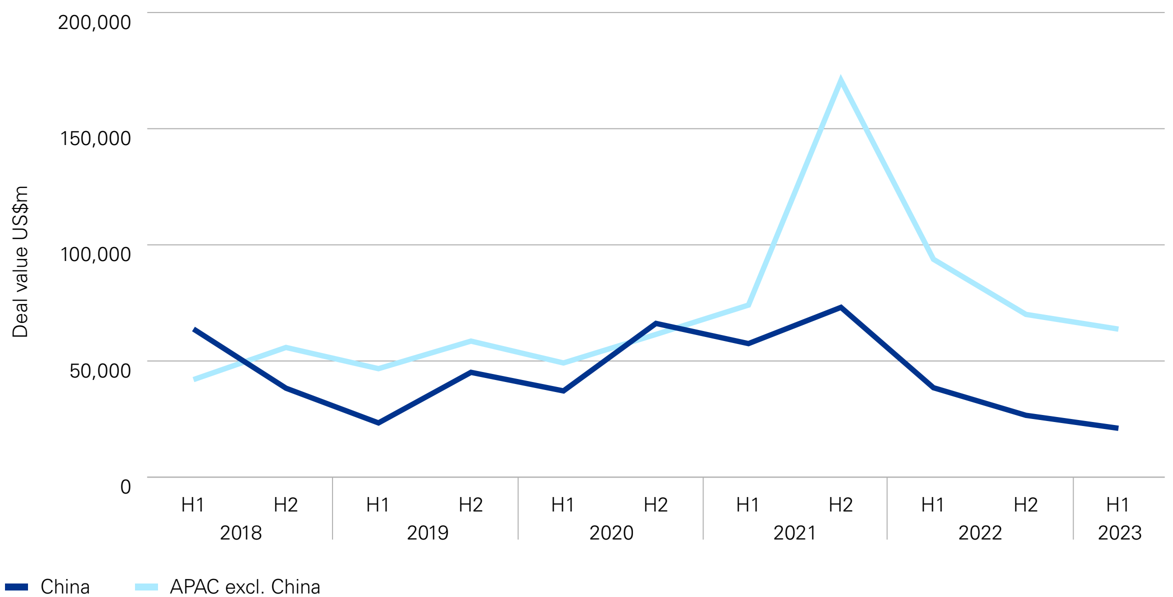
Indeed, since 2018, the gap in investment between China and the rest of ASPAC has widened. At the same time, GPs are looking to separate their China operations from regional and global activities – and this trend extends to LPs who are likewise reducing exposure to purely China focused funds. The pandemic has likely only exacerbated this rebalancing, with investors locked out of the China market due to travel and regulatory challenges – although notably, even in the first half of 2023 as China reopens, this trend has yet to reverse.

New frontiers: India and Southeast Asia

Though no single market can replicate China's scale, those in South and Southeast Asia are already emerging as new epicenters of investment interest.

Specifically, the vast subcontinent of India is undergoing an economic metamorphosis. With a young, tech-savvy

Figure 4:
Asia Pacific PE investment: Target geographies (US$m)



Source: AVCJ

Figure 5:
Asia Pacific heat chart: Companies for sale

	Greater China	Southeast Asia (excl. Singapore)	Singapore	Japan	South Korea	Australia & New Zealand	India	Grand Total
Industrials & Chemicals	788	44	27	55	83	55	79	**1131**
TMT	399	75	83	45	82	109	105	**898**
Financial Services	255	89	16	40	26	57	95	**578**
Energy, Mining & Utilities	280	69	28	16	15	104	45	**557**
Consumer	217	56	11	15	44	112	94	**549**
Pharma, Medical & Biotech	255	49	28	21	20	66	76	**515**
Business Services	305	28	16	13	18	71	59	**510**
Real Estate	209	24	6	4	2	14	7	**266**
Construction	170	15	1	5	11	17	21	**240**
Leisure	78	33	7	6	25	44	7	**200**
Transportation	76	34	6	3	12	28	21	**180**
Agriculture	43	16	2	2	2	19	6	**90**
Defense	5						1	**6**
Grand Total	**3080**	**532**	**231**	**225**	**340**	**696**	**616**	**5720**

Scale

- 300+
- 100-299
- 80-99
- 60-79
- 40-59
- 20-39
- 10-19
- 0-9

Source: Mergermarket

Note: The Intelligence Heat Charts are based on 'companies for sale' tracked by Mergermarket in the respective regions between 01/09/2022 and 18/08/2023. Opportunities are captured according to the dominant geography and sector of the potential target company.

population that has already outstripped China in numbers, it promises a burgeoning consumer base for decades to come. And it's not just about the country's demographic dividend – India is witnessing a tech renaissance as well. Cities like Bangalore are buzzing with startups, birthing tech unicorns at a pace, drawing global eyeballs.

Global investment banks, meanwhile, are moving to expand their footprints in India, both as a tactical pivot in response to the slowing market in China as well as to take advantage of the rapidly growing private equity and M&A ecosystem there. While challenges remain around infrastructure gaps, corporate governance and bureaucracy, many PE firms are already betting these will be outweighed by the country's huge growth potential.

Southeast Asia's appeal lies in its diverse economies – not to mention a population of 650 million individuals, a majority of whom are young, tech-savvy and poised to reshape consumer behaviors in tech, retail, finance and more. Each nation, from emerging economies like Vietnam, the Philippines and Indonesia to the mature economic landscapes of Singapore and Malaysia, provides a multifaceted platform for PE investors. Even traditional Chinese mainland investors are frequently adapting their investment strategies to consider Southeast Asian businesses that are part of the China linked global supply chain or consumer markets.

While both India and Southeast Asia have seen investment flows decline since 2H2021, in line with regional trends, their recent peaks show firm commitments to these markets when conditions are better. PE investment in India, for instance, hit a five-year high of US$43.4bn in late 2021, almost doubling from the same period in 2019 (US$22.9bn). Likewise, investment in Southeast Asia rose from US$8bn in 2H2019 to US$16.4bn in 2H2021.

Mature markets: Japan and Australia

Alongside ASPAC's emerging market opportunities, Japan and Australia offer more developed investment environments to explore. Australia, for instance, has long been a stable and well-regulated market and the

Japan's lower GDP growth relative to other ASPAC markets is linked to its stability as a highly transparent and well-regulated market. It might not get the limelight as much as other high growth, frontier markets, but it offers a predictable and relatively safe business environment where private equity investors can yield great returns.

Paul Ford
Head of Transaction Services,
KPMG in Japan

country benefits from ongoing political stability, a skilled workforce and proximity to the rest of Asia Pacific's growth markets.

Japan, likewise, remains an intriguing market. Despite an aging population and perceptions of limited growth, sectors like healthcare, tech and financial services continue demonstrating strong potential. Equally, private equity transactions in Japan tend to be majority control – rather than oriented toward minority investments like in India or China – which better enables private equity to fully implement operational improvements and a value creation program post-deal.

Another positive is that given the economic environment (a devalued currency and near zero interest rates), Japanese assets appear to be on sale compared to other markets. This trend is likely to continue – as will interest from global GPs toward Japan.

One of the key challenges in Japan is a general reluctance toward foreign ownership among traditional Japanese business owners. However, government policies aim to make the economy more open and welcoming to foreign capital.

China: Balancing risks and rewards

Despite shifting sentiments, it would be presumptuous to declare the China story over. While there is an undeniable ebb in the flow of investments, China remains the world's second-largest economy, only behind the US. The nation is a titan of manufacturing, a hub for tech innovation and home to a burgeoning consumer market, all factors that make it difficult to ignore.

Equally, despite the dislocation faced by China's private equity market during the last 12-18 months, the country accounted for roughly 40% of Asian private equity fundraising in 2022 (US$57.4bn), a number that rose to 73% (US$44.2bn) in 1H2023. China has also consistently accounted for close to half of AUM totals across ASPAC since 2018. Likewise, heat charts show that China still offers abundant and diverse opportunities, ranking far above other Asian geographies.

While the risk of tensions becoming entrenched remains, high level political efforts have been made to thaw Sino-US relations. However, Beijing's recent regulatory actions touching sectors from tech to education have proven more of a curveball for investors. While trade issues might ebb and flow with political tides, regulatory uncertainties in China hint at longer-term shifts.

In short, while the rewards of investing in China can be great, so too are the risks. Navigating the Chinese market today requires strong local partners and market experts more than ever before. But with the right strategy, investors can still reap substantial returns in China.

"The question on everyone's mind is this: is it finally India's time to shine? India – and Southeast Asia for that matter – have long been considered the "next big" market opportunities in Asia, but various factors have held them back from realizing this potential. Regardless, momentum is building and investors are increasingly eyeing these markets as critical pivots in their growth strategies.

Andrew Thompson
Head of Private Equity,
KPMG Asia Pacific

"While sentiment among foreign investors may be cooling towards China, the reality is that there are very few markets in ASPAC that offer both a similar abundance of deal opportunities and sizable, investable targets. For some of the larger PE firms, nothing has changed and they're still closing sizable funds and focusing on larger value deals in China.

Louis Ng
Co-head Private Equity sector,
KPMG China

04

Sector spotlight: Tech and healthcare

Section 04

Sector spotlight: Tech and healthcare

Nowhere has PE investment been more rigorous than in ASPAC's tech space. Since 2018, tech deals have accounted for more than half (55%) of all private equity investments in ASPAC and 36% of total invested values (US$464.4bn).

Over the past decade, the region has become popular for its technological growth and innovation. Breakneck internet and smartphone adoption, for instance, has opened up many new digital opportunities, from e-commerce and fintech to digital healthcare and enterprise software. Disruption from the pandemic has helped accelerate this trend, propelling businesses and consumers into the digital realm and forcing many companies to complete digital transformations within months rather than years.

The age of AI

Yet the crown jewel of the tech industry – and certainly an area of much hype lately – has quickly become AI. As an innovative force, AI is not only transforming industries but also offers the promise of unprecedented value creation.

The applications for AI are indeed vast, ranging from cyber-security and fraud prevention through to manufacturing automation. Centers of innovation in

Figure 6:
Asia Pacific PE investment sector breakdown - value (2018 – 1H23)

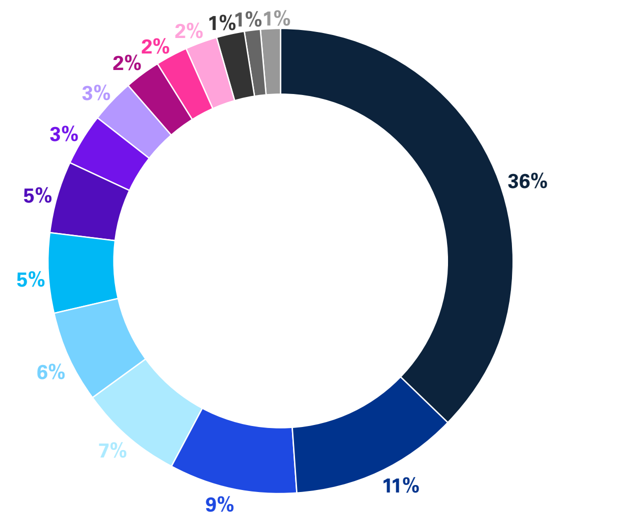
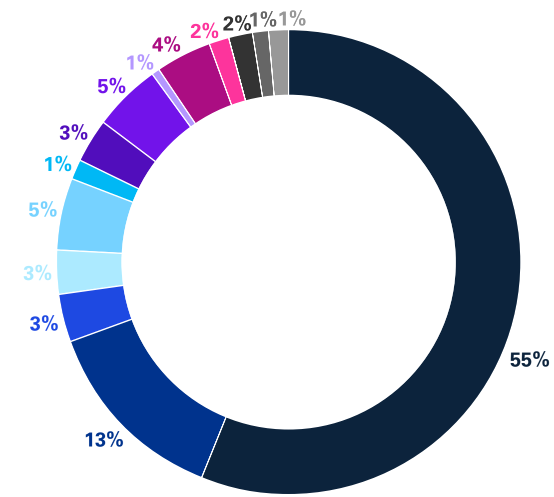


Figure 7:
Asia Pacific PE investment sector breakdown - volume (2018 – 1H23)



Tech, Medical, Transportation/Distribution, Financial services, Electronics, Utilities, Manufacturing - Heavy, Services - Non-Financial, Telecommunications, Consumer products/services, Retail/Wholesale, Infrastructure, Leisure/Entertainment, Travel/Hospitality, Manufacturing - Light

Source: AVCJ

Singapore, Shenzhen and Bangalore are drawing global talent and investment, laying the foundations for robust R&D. Governments, likewise, are placing big bets on AI, with visionary initiatives like Singapore's "Smart Nation" blueprint or China's aspirations to be a global leader in AI underscoring a regional commitment to embedding AI into the societal and economic fabric.

Value creation ally

AI is not only presenting PE investors with compelling investment theses, it also offers new ways for firms themselves to enhance internal operations. The trifecta of AI, big data and machine learning are being used by firms to improve investor reporting, automate contract drafting and streamline other back-office functions. Some firms are already deploying AI and big data to help front office dealmakers to originate and execute deals.

PE firms are also realizing that infusing AI capabilities can significantly elevate the value proposition of their portfolio companies. As AI becomes a sought-after asset in the ASPAC region, companies with robust AI integrations often command higher valuation multiples.

Healthcare

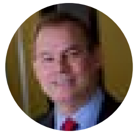
Healthcare similarly offers a compelling investment thesis. The sector accounted for 13% of all PE investments and 11% of investment values since 2018, the second largest sector in ASPAC. Significant unmet demand for healthcare provision, rising middle class wealth, an aging population and rapid growth in the pharmaceuticals and medical devices industries has provided a firm foundation for growth.

Yet, while demand is surging, healthcare penetration remains low across most of the region. Areas like telemedicine, medical infrastructure and genomic testing have tremendous room for growth. Likewise, building platforms that deliver healthcare services to the region's underserved markets could prove to be valuable plays.

Firms have seen value in backing spin-offs and carve-outs from larger healthcare groups to form businesses with specialized focus on particular therapeutic areas. In Australia, for example, Adamentem Capital carved out the cardio business of KKR-backed Genesis Care, and have also moved behind fast-growing healthcare and healthtech companies.

Regulatory changes across the region are also creating an encouraging environment for private investment in healthcare. Relaxed foreign ownership laws in markets like India and Southeast Asia are enticing investors. Governments are promoting public-private partnership models to develop healthcare infrastructure and services. This shifting regulatory landscape signals to private equity firms that investments will face lower barriers going forward.

> **Asia's enormous middle class continues to rise in wealth and prosperity. Technology-enabled businesses, distribution infrastructure, healthcare and financial services are all obvious beneficiaries of this mega trend. Private capital continues to invest in Asia ahead of these long-term tailwinds.**



Andrew Thompson
Head of Private Equity,
KPMG Asia Pacific

05

Exits: Nowhere to go but up – but when?

Section 05

Exits: Nowhere to go but up – but when?

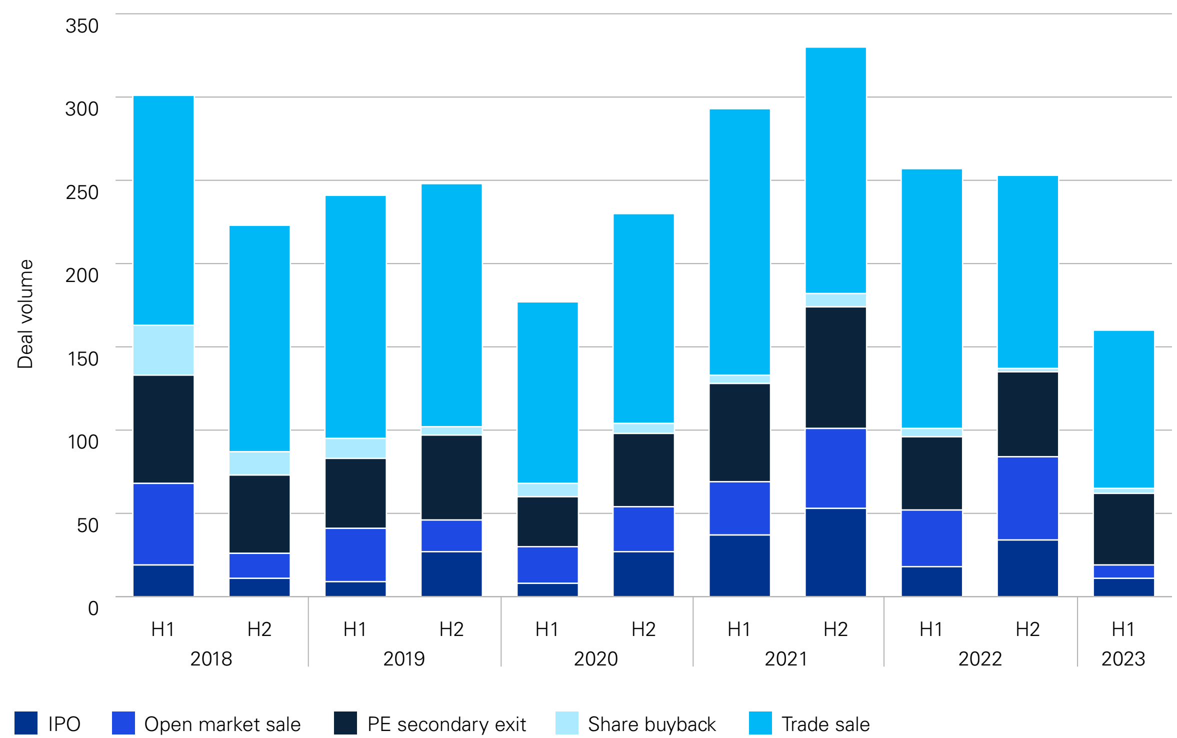
Private equity firms across ASPAC are facing the most challenging exit environment since the first round of COVID-19 lockdowns in 2020. This multi-front downturn has been marked by lower IPO markets, fewer trade sales, and cautious financial sponsors limiting options for private equity firms wanting to sell.

For both the number of exits and the value of those exits, totals for 1H2023 slid sharply compared to the same period in 2022 and were far below the lofty heights of 2H2021. Across all mainstream exits channels, volumes have declined, with IPO exits all but drying up completely.

As a result, private equity firms have had to rely more on trade sales or secondary buyouts to exit investments. However, finding buyers has become difficult amidst economic uncertainty and geopolitical tensions. Strategic corporate buyers have become more selective with acquisitions and financial sponsors are also cautious about taking on assets at potentially peak valuations.

Other firms are focusing on value creation like never before. Where assets have been held for longer than anticipated, GPs are implementing operational improvements that involve streamlining processes, optimizing supply chains and enhancing productivity.

Figure 8:
Asia-Pacific exit trends (volume)



Source: AVCJ

Digital transformation has become a cornerstone of these moves as portfolio companies are equipped with advanced analytics, AI and other digital tools to innovate their business models.

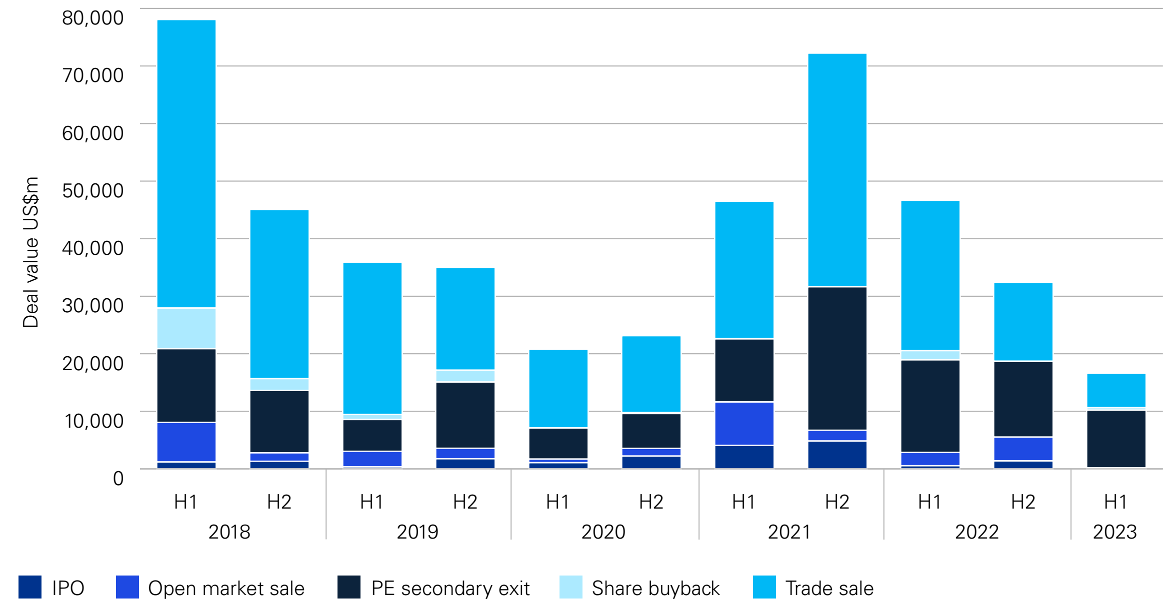
The soft exit market has had a direct impact on distributions to LPs, which has in turn contributed to tougher fundraising markets, as LPs lack the same volumes of cash available to recycle back into the next vintage of funds.

Heading into 2024, the exit environment looks to remain challenging and managers will be looking at alternative routes to provide some form of liquidity. GP-led secondaries are one option, although overall secondaries volumes dropped 25% over the first half of 2023, with GP-led activity adversely impacted. Selling down minority stakes in assets is another option, while some managers may simply opt to extend hold periods until conditions improve.

There are signs, however, of calmer conditions ahead. Interest rates across the globe remain high, but as inflation cools there are hopes that rates may be close to peaking. A clearer picture on interest rates, as well as visibility on how potential target companies have traded through the market dislocation of 2023, could help to give buyers comfort of valuations and close the gap with the pricing expectations of vendors.

Much focus is on the IPO "window" and its potential to re-open. Unfortunately, a couple recent bellwether transactions did not appear to gather the hoped for support suggesting that global ECM may remain subdued well into 2024. It is anticipated that IPO markets around the world will start reopening later in 2024, while the record levels of dry powder ASPAC managers are sitting on will have to be deployed at some point, potentially boosting secondary buyout exit routes.

Figure 9:
Asia-Pacific exit trends (value)



Source: AVCJ

"IPO markets have been particularly quiet over the past 18 months but we're starting to see green shoots of activity. Already, the pipeline is starting to grow in the mid-cap and large end of the market and PE-backed IPOs will likely make up a meaningful proportion of new listings, similar to what we saw a decade ago when IPO markets reopened after a period of low new issuance.

Cecily Conroy
Head of Equity Capital Markets Advisory,
KPMG Australia

About KPMG

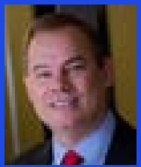
KPMG is a global organization of independent professional services firms providing Audit, Tax and Advisory services. KPMG is the brand under which the member firms of KPMG International Limited ("KPMG International") operate and provide professional services. "KPMG" is used to refer to individual member firms within the KPMG organization or to one or more member firms collectively.

KPMG firms operate in 143 countries and territories with more than 236,000 partners and employees working in member firms around the world. Each KPMG firm is a legally distinct and separate entity and describes itself as such. Each KPMG member firm is responsible for its own obligations and liabilities.

KPMG International Limited is a private English company limited by guarantee. KPMG International Limited and its related entities do not provide services to clients.

For more detail about our structure, please kpmg.com/governance.

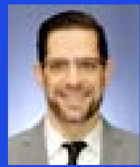
KPMG Asia Pacific



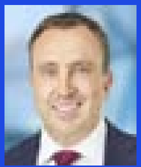
Andrew Thompson
Global Lead Partner,
Asia Pacific Head of
Private Equity,
KPMG in Singapore
T +65 6213 2929
andrewthompson8@
kpmg.com.sg

James Hindle
Partner,
Transaction Services
and Co-Head of
Private Equity,
KPMG Australia
T +61 4 3148 5058
jhindle@kpmg.com.au

Priscilla Huang
Partner,
Co-Head of Private Equity,
Deal Advisory,
KPMG China
T +852 2140 2330
priscilla.huang@kpmg.com



Paul Ford
Partner,
Head of Transaction
Services and Asia Pacific
Head for Elevate,
KPMG in Japan
T +81 335 485 774
paul.ford@jp.kpmg.com



Nicholas Combes
Partner,
Deal Advisory,
Co-Head of Private Equity,
Mergers & Acquisitions
KPMG Australia
T +61 3 9288 6223
ncombes@kpmg.com.au

Louis Ng
Partner,
Co-Head of Private Equity,
KPMG China
T +86 10 8508 7096
louis.ng@kpmg.com

Darren Bowdern
Partner,
Head of Alternative
Investments Hong Kong
SAR, China and
Asia Pacific Head of Asset
Management Tax,
KPMG China
T +852 2826 7166
darren.bowdern@kpmg.com

Jin-Won Kim
Partner,
Deal Advisory,
KPMG in Korea
T +82 2 2112 0795
jinwonkim@kr.kpmg.com

kpmg.com

home.kpmg/socialmedia