Private equity in Southeast Asia

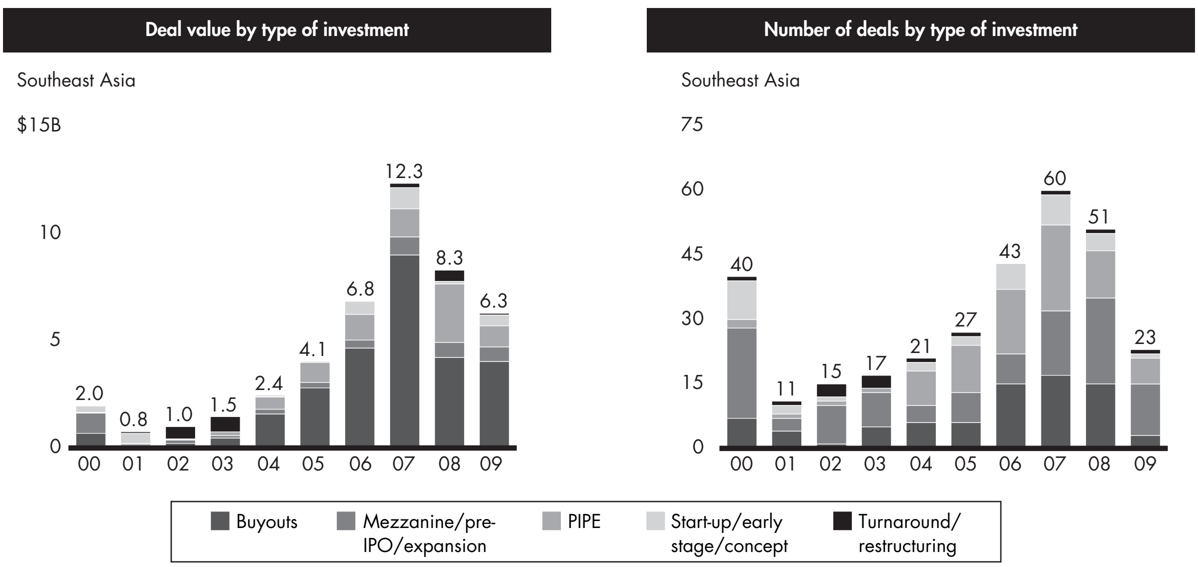
Global private equity investors are stepping up their presence and increasing their capital commitments to the region

Private equity's expanding global scope and influence—particularly in the big emerging markets of China and India—has been one of the leading financial stories of the past decade. Less visible, although no less significant, has been private equity's increasing role in speeding the growth of companies across the dynamic economies of Southeast Asia—from Singapore, Malaysia and the Philippines to Indonesia, Thailand and Vietnam.

The PE industry has sunk deep roots in the region. From peak to peak across the business cycle, the number of deals financed by PE investors rose from 40 in 2000 to 60 in 2007, a 50 percent increase. Even though the deal count in the region dropped to just 23 during the recent downturn, 2009 was still the fourth-best year for transactions in the past decade (see Figure 1). The value of those deals, meanwhile, soared six-fold, to $12.3 billion in 2007. Deal value dropped by nearly half, in 2009, to $6.3 billion; but even at that depressed level, the total value of PE transactions last year was nearly eight times higher than in 2001, when the region began to pull out of the last recession. From 2006 through the end of last year, buyouts comprised less than one-third of all deals, but they accounted for between one-half and three-fourths of total deal value.

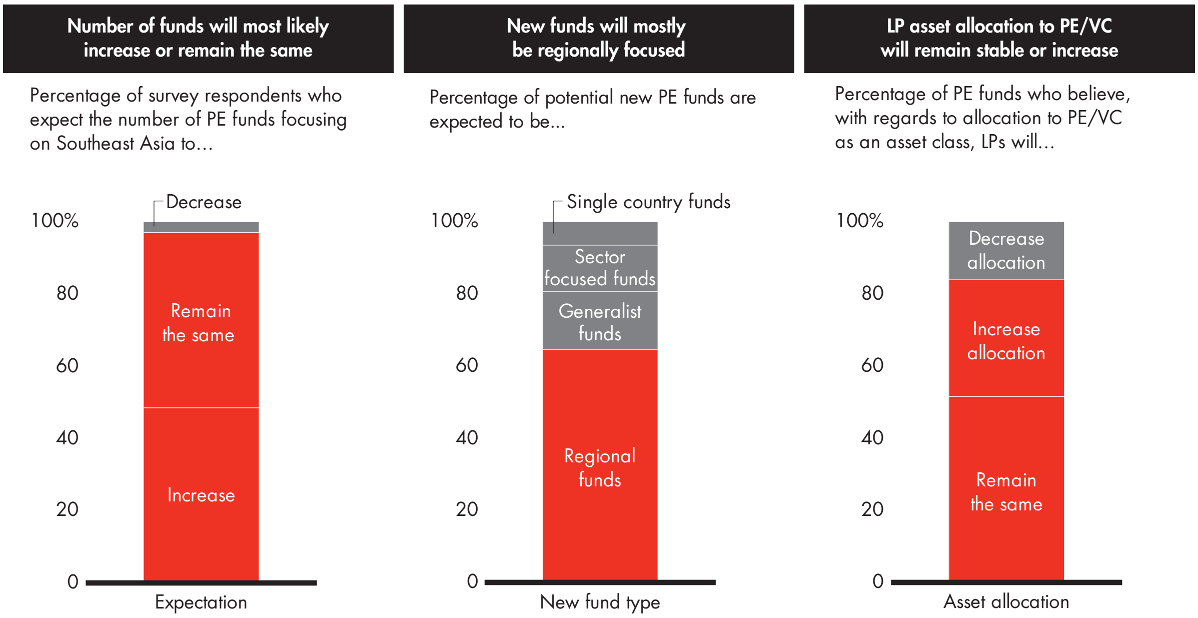
With the return of strong GDP growth across the region since the second half of 2009, PE in Southeast Asia looks poised to resume its ascent (see Figure 2). Deal flow has continued to increase into 2010, along with average deal size. A wide array of large-cap, mid-cap, sovereign wealth funds and Asia-focused funds wielding sizable amounts of "dry powder"—capital targeted for investment but not yet allocated—are

Figure 1: Following years of strong growth, PE dealmaking in Southeast Asia slumped in 2009 but is now rebounding



Notes: Investments with announced deal value only; excludes deals of value <$10M; does not include bridge loans, franchise funding and seed/R&D deals; excludes infrastructure project finance deals, real estate, real estate investment trust and hotels & lodging property deals; Southeast Asia includes Indonesia, Malaysia, Philippines, Thailand, Vietnam and Singapore
Sources: *AVCJ*; Bain analysis

Figure 2: Many factors point to growth of PE as an asset class in Southeast Asia



Sources: Bain Southeast Asia PE Survey; Bain analysis

scouting the region for opportunities. Credit markets have stabilized, laying a foundation for a cautious return of both buyouts and growth capital.

This constellation of favorable conditions makes now a good time to take stock of how the industry will evolve over the balance of 2010 and beyond. To find out, Bain & Company, with the cooperation of the Singapore Venture Capital & Private Equity Association (SVCA), surveyed general partners at many of the leading PE and venture capital funds in the region. The picture that emerges is of a dynamic young industry ready to move into a phase that will require PE firms active in the region to acquire new skills. Let's look at the specifics:

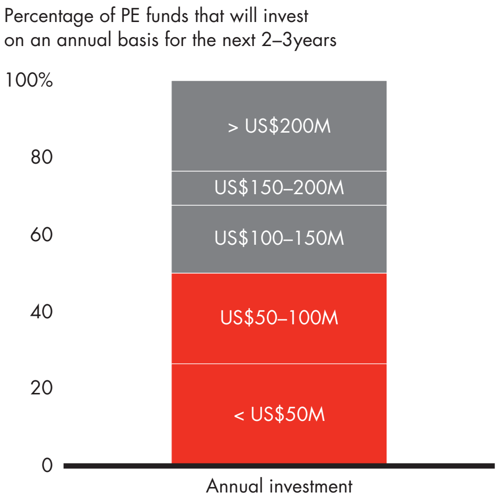
PE is now a major asset class in Southeast Asia

Many factors point to a deepening of PE investor commitment to the region. Half of all respondents look for the number of funds active in Southeast Asia to increase over the next two to three years. The funds will also be bringing a new focus and deeper expertise to the region. Nearly two-thirds of the respondents expect that new funds will be regional specialists, and another 13 percent will specialize by industry sector. Overwhelmingly, PE general partners expect limited partners' interest in investing in the region to remain high, with nearly nine out of 10 looking for them to maintain or increase their asset allocations to PE and venture capital.

PE firms are increasing their physical and financial commitment

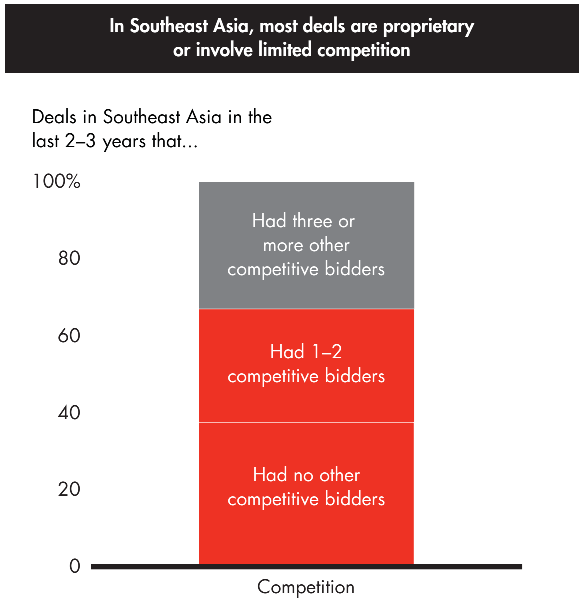
Among funds already active in Southeast Asia, just 20 percent are local specialists, and nearly half of those concentrate on Singapore. The remainder are about evenly split between funds that invest broadly across Asia and global funds that have established a local presence. Continuing to target mainly small and mid-cap companies, the survey respondents anticipate that 50 percent of funds' annual investments in the region over the coming two to three years will be more than $100 million (see Figure 3). They expect that only about one-quarter will invest more than $200 million a year.

Figure 3: Half of PE funds will deploy less than US$100 million annually to deals in Southeast Asia



Sources: Bain Southeast Asia PE Survey; Bain analysis

Figure 4: In spite of increasing competition, about 40% of all deals were solely sourced



Sources: Bain Southeast Asia PE Survey; Bain analysis

Competition will heat up

The influx of new funds wielding large amounts of dry powder to invest will bring a new intensity to the competition for deals across Southeast Asia. But survey respondents report that incumbent funds that have an established presence in the region's fragmented markets have distinct deal-sourcing advantages. About half of all deals completed over the past two to three years were sourced, in about equal proportion, through networks of industry relationships and advisers or by direct approaches to the target companies themselves. Brokers and other intermediaries were the sources for the balance of deal introductions. Those early leads have kept a lid on competition. Nearly 40 percent of deals completed across the region since 2007 and 2008 were proprietary (see Figure 4). In another 30 percent, winning bidders faced just one or two bidding rivals.

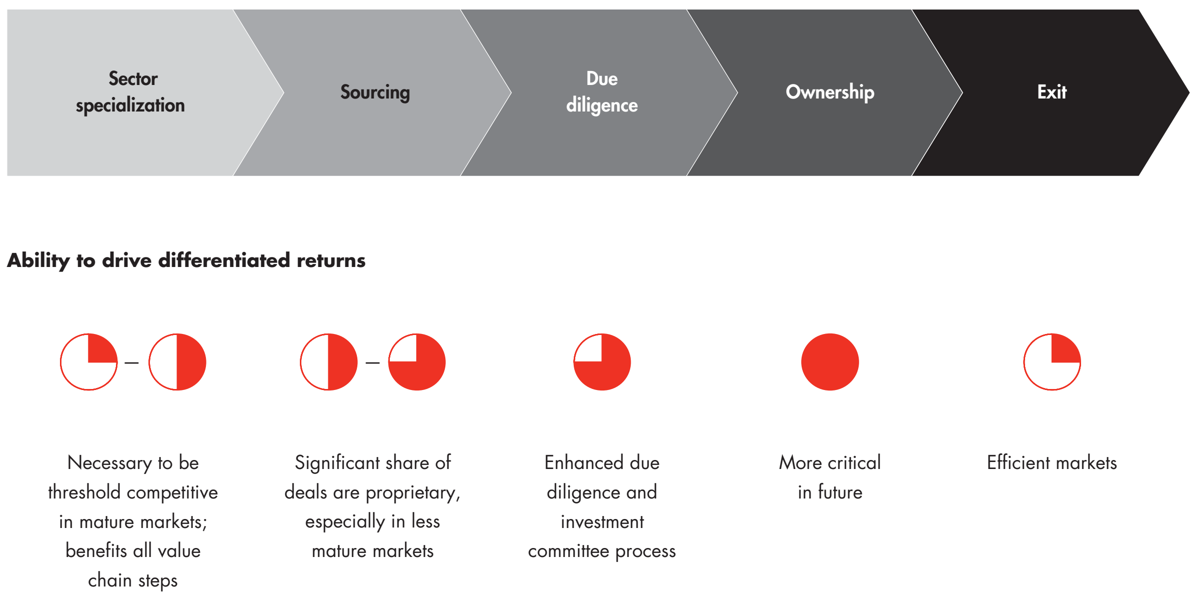
New skills required

As competition to identify attractive deals and to win the best ones ramps up, PE firms will need to sharpen their capabilities along each phase of the investment life cycle, from deal sourcing to exit (see Figure 5).

- In deal sourcing, for example, the leading firms are strengthening their skills as geographic and industry sector specialists, enabling them to differentiate themselves from their peers as the preferred partner to owners of the companies they target. Greater specialization will be an increasing source of competitive advantage for sustaining a strong deal flow.

- Leading firms are honing their due-diligence disciplines, skills that are especially important in Southeast Asia, where a high proportion of potential target companies are small, private and lacking in transparency.

Figure 5: Differentiated investment capabilities will be critical



- PE firms increasingly recognize that they need to work actively with owners to identify high-priority initiatives that create value. They monitor performance by tracking a few key metrics that provide an early warning system to alert management to take fast corrective action if the program begins to drift off course.

- Finally, PE leaders begin weighing how they will exit from each investment well before the time comes to sell by continuously evaluating market conditions for initial public offerings (IPOs) and identifying potential strategic acquirers.

Strong regional growth, dynamic entrepreneurs and increasingly knowledgeable and seasoned investors add up to a promising period ahead for private equity investment in Southeast Asia.

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