# 40th Asian Shadow Financial Regulatory Committee Statement

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## The Demand for Capital, Public-Private Partnerships and the role of Private Equity Firms in Asia-Pacific

It has been estimated that Asia will need to invest $US1.7 trillion per year in infrastructure until 2030 to maintain its growth momentum, tackle poverty, and respond to climate change. Moreover, apart from infrastructure, there is a substantial need for investments in innovative technologies that require a prohibitively large amounts of capital. These investment goals cannot be solely met by government nor by the private sector alone. Hence, there needs to be a partnership between the public and private sectors, in particular private equity. This includes public-private partnerships, not only in infrastructure investment, but also in co-financing innovative technologies. Moreover, buy-out funds can play a role in enhancing the operational efficiency of existing firms and the allocative efficiency of capital.

In the broad sense there are several different classifications of private equity firms including infrastructure, venture capital, leveraged buy-out and growth equity firms. Mordor Intelligence estimated the total value of private equity firms in Asia-Pacific to be $US2.7 trillion in 2024 growing to $US5.4 trillion by 2030 of which China accounted for 23% of the 2024 total. By private equity fund type, leveraged buyout, growth equity and venture capital accounted for 43% of the 2024 total. In the current geopolitical climate investor appetite for private equity firm investment is growing the Coller Capital reporting that 67% of investors in the Asia-Pacific region plan to expand allocations to the asset class.

Countries have different approaches to public private partnerships. China and the US have achieved the most success in financing and developing new technologies but through very different approaches, as discussed below. Moreover, we highlight the experiences of Japan and Korea.

*China*

Venture capital in China differs significantly from that in U.S. and other Western countries in that government-led venture capital (GVCs) plays a very important role in venture capital business. According to data from 1999 to 2018, GVCs accounted for 40% of deals and 50% of

funds raised in venture capital investments in China. Generally, GVCs perform worse than private sector venture capital (PVCs), but they are also less cyclical. The performance gap between GVCs and PVCs shrinks by 60% during economic downturn. In other words, GVCs offset the decline in private-sector risk appetite, enabling innovative, riskier investment projects to continue.

*United States*

The US venture capital market is the largest in the world, with billions of dollars invested annually in high-growth potential businesses. It is projected to reach $2.64 trillion by 2032, expected to grow at an annual average growth rate of 8.17% from 2026 to 2032.

The US has several world-renowned innovation hubs, such as the Bay Area, New York City, and Boston, which attract significant venture capital funding.

Overall, the US venture capital market is a dynamic and vital component of the national economy, fostering innovation and supporting the growth of promising companies.

*Japan*

Japan's venture capital (VC) landscape is experiencing growth, with increased investment activity and a developing ecosystem for early-stage funding. The Japanese government actively supports startups and VC funds mostly using subsidies.

However, it faces several challenges, including a relatively underdeveloped exit environment, regulatory hurdles, and a conservative business culture that can stifle innovation. Additionally, the size of VC deals in Japan tends to be smaller compared to other major markets, and cultural barriers can hinder foreign investment.

*Korea*

The Korea Venture Investment Corp. (KVIC) is a government-backed fund-of-funds that channels public and private capital into startups and growth-stage companies. Through the Korea Fund of Funds, KVIC invests in venture capital funds to boost high-risk sectors like early-stage startups, deep-tech, and regional businesses. It has been key to Korea’s venture growth, expanding the market and attracting private investment.

In successfully delivering major infrastructure projects, Korea has also gained significant experience in public-private partnerships that have contributed to national development. Notable successes include the Busan-Geoje Fixed Link, which dramatically reduced travel time and boosted regional economic growth, and the Incheon International Airport Expressway, which improved connectivity and logistics efficiency.

*Recommendations*

1 Following the experience of China and the US in using equity-based culture to finance investments in innovative technologies, many Asian countries could increase awareness on promoting such a culture. This may be essential for implementing the substantial investment agenda in most countries.

2 With infrastructure there may also be a need for co-financing between the public and private sector. In contrast to the required equity-based financing for innovative technologies, here we see a great potential for involving national investment banks which would provide part of the required loans for an investment project of a company while private parties (such as commercial banks and bond holders) would provide the remainder.

3 Public-private partnerships for co-financing investments, as highlighted in the two points above, have distinct advantages. Promoting an equity-based culture has important advantages for enabling risky and innovative investment projects, even in times of capital shortages, which otherwise would not take place.

4 Promoting a larger role for national investment banks, which enables better risk sharing, may help to bring in private financiers. The example of Europe where the European Investment Bank has been active for almost fifty years, may serve as an inspiration for Asian countries to set up an Asian Investment Bank lending to firms directly. Such an Asian Investment Bank would be distinctly different from the current practices of the Asian Development Bank and the Asian Infrastructure Investment Bank which primarily lend to governments and not to companies.

5 When promoting government venture capital (GVC) or public-private partnerships (PPP), there are challenges to be addressed. As for GVC, this includes over-reliance on public funds and limited flexibility given to venture capital funds in their investment decisions. As for PPP, this includes managing demand risk, financial structure, and the need for transparent contract management.

From 1999-2018, GVC accounts for 40% of VC deals and 50% VC capital raised.

- Depending on information sources, 14% or 1/3 of government fund is directed by the central government and 86% or 2/3 is directed by local (provincial or city) governments.
- Most of the time, the government supplies the capital (as LP) and outsources fund management to private VCs (as GPs).
- GVCs tend to underperform relative to private VCs (PVC). The five-year probability of a GVC-backed portfolio exiting via IPO or acquisition is 5.8%, whereas a PVC-backed portfolio's chance of IPO or acquisition is 11.5%. The underperformance comes from local GVCs only, not GVCs of the central government.
- Across venture market cycles, GVC behavior is less cyclical than PVC: GVCs tend to raise more money and invest more during VC downturns.
- GVC performance is also less cyclical: the performance gap between GVC and PVC is reduced by 60% during downturns. In fact, companies backed by GVC during VC market downturns are more likely to go public ex-post.
- A likely channel for this improved performance is governments' "deep pockets" because the results are driven by fiscally healthy cities. This improvement is not from GVC's ability of finding high-quality VCs during downturns, nor is it explained by other unobservable government assistance during downturns.
- Many local governments have veto right to steer the investment in the expected direction and require the sponsored VC funds to invest substantially in deals in the same city (47%), in some designated industries (98%), and in the early stage (53%).
- Overall, government's policy orientations and its ability to deploy capital locally during challenging times are crucial to understanding GVC's role in capital markets and the broader economy.