**Money**

# PE investment rules to be eased soon, regulator says

By Li Xiang (China Daily)
Updated: 2011-06-21 10:40

BEIJING - China will soon loosen restrictions on domestic securities brokerages engaging in private equity (PE) investment despite investors' concerns that they may manipulate the market by pushing up initial public offering prices to reap exorbitant profits as prefloat investors.

The regulator is planning to turn the pilot program of PE investments by securities firms into one of their regular businesses, according to Huang Wenyuan, director of the department of institutional investors at the China Securities Regulatory Commission (CSRC).

"New rules for PE investment by domestic securities firms will be announced very soon," said Huang on Saturday.

To allow domestic brokerages to launch PE funds will help change the situation of foreign capital dominating China's PE industry."

LIU ZHIYU
VICE-PRESIDENT, DEPARTMENT OF CORPORATE DEVELOPMENT AND FINANCING, CITIC SECURITIES

More securities firms may also be allowed to set up PE funds after the regulator approved the launch by China International Capital Corporation, the country's largest joint-venture brokerage, of a PE fund of 5 billion yuan ($772 million). It is the country's first PE fund to be managed by a securities broker.

At present, domestic brokerages can use no more than 15 percent of their own capital for PE investments and they are not allowed to raise funds from investors in the market to invest in unlisted companies.

The securities regulator launched the pilot program for PE investment by securities companies in 2007. So far, 34 securities firms have gained the license for PE investment and the total investment value has reached 10.2 billion yuan, according to the Securities Association of China.

"To allow domestic brokerages to launch PE funds will help change the situation of foreign capital dominating China's PE industry," said Liu Zhiyu, vice-president of the department of corporate development and financing at CITIC securities.

The expansion of the PE business of securities firms will also broaden their revenue streams because they are still heavily reliant on the traditional trading commissions as their major source of income.

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Global investment banks such as Goldman Sachs and Morgan Stanley on average derive 20 to 30 percent of revenues from the business of asset management, which includes PE investment. The number is less than 5 percent for Chinese securities firms.

"We have seen a sharp decline in our revenues from our commission income due to the sluggish market and intense competition," said He Bin, chairman of the PE investment fund of Guotai Junan Securities.

"It is essential to diversify our business," he said. "Boosting the PE business will help improve our business model and broaden the investment channels of our clients as well."

But what has made the regulator reluctant to make a major breakthrough in expanding the PE business of securities companies over the past few years is the potential conflict of interest between their IPO underwriting business and PE investments.

There have been widespread market concerns about securities brokers using their advantage as IPO underwriters to manipulate IPO prices. It is feared that the brokerages would lower IPO standards or whitewash the financial reports of their clients to push IPO prices higher so that they can pocket huge profits from PE investments.

Securities firms have been required to set up a "firewall" to prevent communication between the investment banking team and PE investment team. The regulator is also considering imposing a rule that forbids a securities firm from investing in an unlisted company after it becomes the underwriter of the company.

The regulator is also hoping to rely more on the market-based mechanism to constrain potential market manipulation by securities companies while the domestic market gradually matures.

"The latest wave of new shares falling below IPO prices showed that making profits from the excessive price difference between the primary and secondary markets will no longer be a sustainable business model for the securities firms," said Huang, the CSRC official.