

## BUSINESS

# Venture capitalists tackle Chinese hurdles

Research campuses in Beijing and Shanghai are brimming with ideas that might invite commercial development. And for the first time, venture capital to take them forward is pouring into the country.

Last year, according to Ernst & Young, venture-capital investments in China totalled US\$1.3 billion — more than those in France, if only a fraction of the \$20 billion raised in the United States. Yet according to a report released last month by the international consultancy, the Chinese venture-capital market remains fragile.

“Chinese venture capital is at a crossroads,” the report concludes. “Unless the conditions necessary to sustain a healthy venture-capital industry are put in place, the pace of investment is likely to slow or even be reversed.” Indeed, the report suggests, an 8% drop in venture-capital investment during the first half of this year may be an ominous sign.

Venture capital in China first got going in 1992, when IDG Technology Venture Investment began investing in information-technology companies there. The field has grown rapidly of late, trebling in value since 2002. Yet only a small fraction of this is going into science-based businesses. Many of the ventures backed are conventional services and manufacturing ones, says Yoshiaki Hasegawa of the Tokyo-based Japan Asia Investment Company. And of the technology firms backed by venture capitalists, most are in semiconductors and information technology.

The report — written by Ernst & Young’s Gil Forer on the basis of a Shanghai workshop co-hosted with the China Venture Capital Association — warns that investor interest is being dampened by venture capitalists’ inability to make money from small Chinese companies by floating them on a stock market. It calls on the Chinese government to set up a stock market similar to the Nasdaq. But earlier this year, the government strengthened restrictions on Chinese companies raising money through share offerings on foreign stock markets. “It is trying to control the flow of capital,” says Forer.

International investment funds such as IDG and the SoftBank Asia Infrastructure Fund, based in Hong Kong, account for about 70% of total venture-capital investment in China, according to Ernst & Young. The majority of the 200 domestic venture-capital funds that

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REASONS

At the crossroads: venture capitalists are getting mixed signals from the Chinese government.

account for the rest are closely tied to city and provincial governments. And foreign funds tend to follow their lead. “They want assurance” concerning the reliability of target firms, says Ming-Wei Wang, president of SiniWest, a biotechnology company based in San Diego with interests in China and the United States.

According to Wang, government investment is often spread too thin, as it tries to please too many people. And government-associated funds often base their investments on personal connections, rather than potential profitability. “We need independent evaluation,” he says.

Researchers themselves can put off venture capitalists by refusing to share information, Wang adds. Such refusals are understandable, given the weak legal mechanisms that are available to protect intellectual property in China, but they make ideas hard to evaluate.

Guo-Ping Zhao, executive director of the Chinese National Human Genome Research Center in Shanghai, says that venture funds in China often lack the know-how to evaluate their investments. “Those who have the money don’t understand technology,” he says. “Those who understand it don’t have any money.”

There are some signs that the government would like to foster venture capital: last month, it actually eased some restrictions on citizens’ activities on foreign stock markets. And seasoned investors are confident that the market will continue to expand. “China is moving in a positive direction,” says Hasegawa, whose firm has already invested in two dozen Chinese companies. ■

David Cyranoski

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## IN BRIEF

**PATENT PEACE** Brazil and Abbott Laboratories have averted a patent showdown by announcing that they have agreed on pricing for a key AIDS drug.

Beginning next March, the Illinois-based drug company will make the protease inhibitor Kaletra (lopinavir and ritonavir) available to the Brazilian government for 63 US cents a pill, rather than the current price of \$1.17.

In June, Brazil’s health ministry threatened to break Abbott’s patent — which doesn’t expire until 2015 — and begin producing a generic version of the drug if the company didn’t lower its price. Kaletra is a staple in Brazil’s renowned, publicly funded AIDS programme, which distributes free drugs to roughly 160,000 patients.

**GOING OFFSHORE** Industrial research and development is rapidly going global, according to a survey by the Paris-based Organisation for Economic Co-operation and Development.

The survey says that 16% of industrial research is now performed by overseas affiliates; the concentration of such ‘offshore’ research is highest in Ireland and Hungary, and lowest in Japan.

The economic think-tank says that of the largest economies Britain has the most internationalized industrial-research system by three separate criteria. China has become the third-largest research nation in the world, and surpassed Japan as the country with the second-largest research workforce.

**CANCER CASH** California biotechnology company Genentech cruised to a record-breaking third quarter on booming sales of anti-cancer drugs. Its net income increased by 56% from the third quarter in 2004, and for the first time, US sales of the company’s cancer drugs exceeded \$1 billion.

The strong growth was led by US sales of Avastin (bevacizumab), a colon-cancer drug that starves cells of their blood supply. US sales of Avastin grew by four-fifths, to \$325 million, compared with the same time period in 2004. Sales of Herceptin (trastuzumab), a genetically targeted breast-cancer drug, grew by 70% to \$215 million.