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Venture capitalists shun Chinese biotech

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Barriers to foreign investors are impeding the growth of the biotech sector in China.

Recent reports by an Asian business publication indicate the Chinese biotechnology sector is currently underfunded because of a lack of domestic venture capital and insufficient foreign investment. Venture capitalists (VCs) stay away from the country's biotech industry because of a shortage of investment exit strategies, cultural differences in doing business and uncertainties with respect to intellectual property (IP) protection.

A report in the October issue of *Asia Private Equity Review*[1] (Hong Kong) estimates that 81% of the $325 million raised by Asian VCs between June 1999 and June 2003 for biotechnology are invested in US, rather than Asian, firms. In contrast, the US and European biotechnology sectors attracted $2.7 billion and $950 million in venture capital in 2002, respectively, according to databases maintained by BioCentury (San Carlos, CA, USA). China in particular has an "anemic" venture capital pool of about $100 million for biotechnology, says Kathleen Ng, editor and publisher of *Asia Private Equity Review*.

Newsphoto

Biotech companies planning to settle in the Zhongguancun Life Science Park in Beijing, considered China's Silicon Valley, could have trouble raising venture capital.

One problem is that China does not offer the same type of opportunities for an exit, such as an easy initial public offering, as Western countries do, say VCs. "There is not a clear exit, and being a venture capital firm, we care about how we exit," says Jonathan Wang, the vice president of WI Harper (San Francisco, CA, USA), a venture capital firm that has invested in biotechnology startups in both the United States and Asia.

The lack of clear exits comes from the immaturity of exchanges in the region. The country has a stock exchange that was created in 1990 in Shanghai, but it has not developed to the point of rivaling Western counterparts such as Nasdaq (Washington, DC, USA) or the New York Stock Exchange. An alternative exit is to list on the Stock Exchange of Hong Kong which has historical links with the London Stock Exchange. Plans to open alternative exchanges, such as a technology-focused board in Shenzhen, a city neighboring Hong Kong, have been suspended because of banking scandals in the past two years.

Investors may also be reluctant to put their money in a country where patent protection remains murky. Even if China, since joining the World Trade Organization (Geneva) in 2001, has the obligation to protect intellectual property (IP), "there is not a concerted effort in IP protection," says Nancy T. Chang, president and CEO of Tanox (Houston, TX, USA). This was one of the reasons why Chang deferred investing in mainland China, instead funding startups in the United States staffed with Chinese scientists.

Foreign investors also find structural barriers to investing in China despite the high quality of the research and tantalizing potential of billions of Chinese consumers. For example, Chinese law forbids a foreign investor from owning more than half of a company; VCs typically own the majority of private biotechnology companies, and this law may discourage foreign VCs from investing in Chinese firms.

Language and cultural barriers also make it difficult for foreign VCs to comprehend the intricacies of doing business in China where the importance of 'guanxi,' or connections, remains key to doing business. Kien Leong, senior partner with Pacific Venture Design (Shanghai, China), a strategic consultancy company, says domestic VCs may, by comparison, be more comfortable with dealing with grey areas in doing business linked to local habits.

References

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