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INSIGHTS

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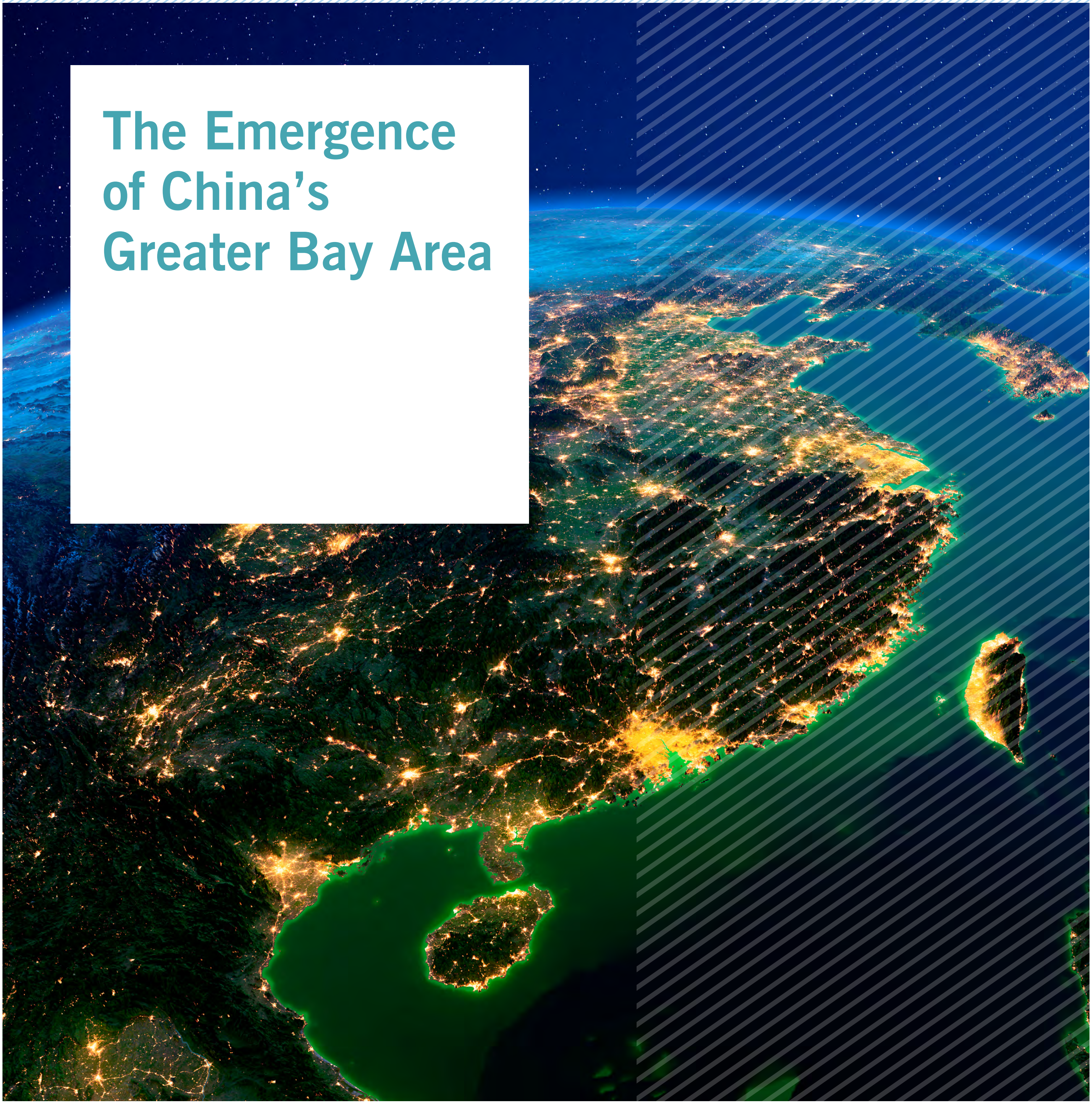
The Emergence of China's Greater Bay Area



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Duncan Zheng joined Investcorp in 2020 from Pagoda in Beijing where he was a Co-Managing Partner since 2012. Previously, Duncan worked as a Principal at Triton, based in Germany. He also served as a Senior Advisor to the China Investment Corporation's Global Private Markets Department in Beijing. Prior to that, Duncan worked for the US buyout firm Hicks Muse Tate & Furst. Duncan started his career in the Global Consumer & Healthcare Group at Salomon Smith Barney in New York.

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Executive Summary

If the Chinese economy were to be compared to an airplane, it would have two main economic engines – one being the Yangtze River Delta ("YRD") with Shanghai & Hangzhou in its center, and the other being the Pearl River Delta ("GBA" or the "Greater Bay Area") with Hong Kong and Shenzhen in its center. While Beijing acts as the plane's cockpit, steering the overall direction of the country, China's economic dynamic and commercial success is largely powered by, YRD and GBA.

China's Greater Bay Area - with a population larger than Germany's and an economy sized between that of Canada and the UK- is a vivid illustration of the country's four decades of economic reform and rapid development that transformed a historically important trading region into one of the world's most connected and integrated manufacturing and technology centers today.

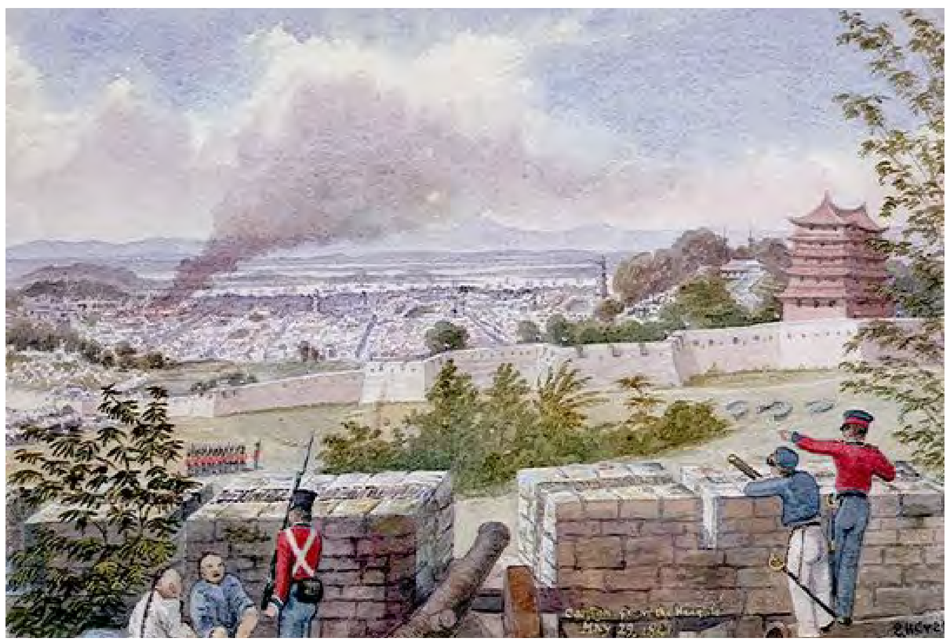
As China is undergoing a once-in-a-decade government reshuffle during 2022, Investcorp PE Chinais looking to provide insight on one of China's most important economic engines and an outlook on its promising future, as the country looks to refocus its priority on economic growth under the soon-to-be- announced leadership starting in 2023.

“The superior man, when resting in safety, does not forget that danger may come. When all is orderly, he does not forget that disorder may come. Thus his person is not endangered, and his States and all their people are preserved.”
Confucius

Historical Background

In 1839, after months of stalled negotiations, the Chief Superintendent of British Trade in China, Charles Elliot, wrote a letter from Canton (Guangzhou) to Queen Victoria recommending the use of military force to ensure that the ports of Canton, Macau and Hong Kong stay open for opium that the British East India Company was importing from its plantations in the Indian Bangal territories.

A year later, in June 1840, a British naval force found shore at Macau and bombarded the port. In the ensuing conflict, the Royal Navy used its superior ships and guns to inflict a series of decisive defeats on the Qing Empire’s antiquated defense force. This conflict, which was later referred to as the First Opium War (1839-1842), was the culmination of decades of trade imbalances between the Qing Dynasty and Western powers such as Britain, the United States and others - whereby opium was banned in Britain but forcefully brought into China through the Southern ports surrounding Canton.



British bombardment of Canton from the surrounding heights, 29 May 1841.
Watercolour painting by Edward H. Cree (1814–1901), Naval Surgeon to the Royal Navy.

Canton, or Guangzhou, is the capital city of province Guangdong with the Pearl River running through its center and entering the South China Sea. This region, also called the Pearl-River-Delta, used to be one of two most important trading hubs in China, together with the YRD surrounding Shanghai. While the Yangtze-River-Delta region marks the beginning of the Silk Road that spanned from China to the Middle East into Europe, the Pearl-River-Delta surrounding Canton was the gateway to and out of Cathay (China) known to Europe since the 13th Century following the travels of the Venetian merchant Marco Polo.

Fast-forward to today, the Pearl-River-Delta stands again at the forefront of China's next phase of economic development as the strategic importance of the region was emphasized in the 2017 "Greater Bay Area Strategy" with a series of long-term policies designed to build the GBA into the world's leading bay area for living, commerce, innovation and societal developments.

In this issue of the Review, the Investcorp PE China Team will provide an introduction to the GBA region with its multi-faceted economic background and exciting opportunities ahead.

202 BC - 220 AD
Han Dynasty

Maritime Silk Route originating from Guangdong promoted trade between China and South Asia, West Asia, Europe and North Africa

1346 - 1644
Ming Dynasty

Guangzhou was the only port for foreign trade in China at that time as seaborne trade was generally forbidden by the Imperial Courts

1840 - 1842
The Opium Wars

Qing Dynasty lost Hong Kong and Macao to Britain and Portugal by losing the Opium Wars

1987 Onwards
Start of China's Reform & Opening-Up

1992
Deng Xiaoping's Southern Tour

Deng Xiaoping visited Shenzhen, Guangzhou and Zhuhai, further cementing the leading role Guangdong plays in economic reforms

1997 & 1999
China Resumes Sovereignty over Hong Kong and Macao, Ending 100+ Years of Colonial Rule

2000 - 2015
From "Factory of the World" to "Innovation Center of the World"

Emergence of globally leading companies in technology, healthcare, finance, real estate, transportation and other high-value sectors

2017 - Now
Creation of the Greater Bay Area

With less than 1% of land and 6% of population of China, the Greater Bay Area generated USD 2 trillion in GDP in 2021, representing 11% of China's total GDP

Deng Xiaoping's address to the City Government of Shenzhen (in the 1980's)

"Reforms and opening-up policies have to be bold, have to be daring, cannot be timid. When you see something is right, bravely embrace it"

On a GDP per capita basis, China's GBA is still only a fraction of its Western bay area counterparts and has much room to grow

The GBA Today

A Comparison Between China's GBA and Other Major Bay Areas in the World

	GBA	Equivalent to	San Francisco Bay Area	New York Metropolitan Area	Tokyo Bay Area
Land Area (sq. km)	56,098	1.5x Switzerland	17,887	21,479	36,898
Population (mm)	85.7[1]	Germany	7.7[3]	19.1[2]	44.3[2]
GDP ($bn)	1,928.7[1]	Canada	525.8[2]	1,501.1[2]	1,991.6[4]
Real GDP Growth (%)	4.4[3]	USA	4.0[3]	1.2[3]	1.4[4]
Per-Capita GDP ($)	22,501[1]	Portugal	128,573[3]	78,586[2]	45,084[4]
Air Passenger Throughput (m Passenger-Times)	101.5[2]	1/2 of EU	25.8[2]	40.8[2]	40.8[2]
Air Cargo and Airmail Throughput (m Tonnes)	7.7[2]	World No.1	1.1[2]	1.8[2]	2.7[2]
Port Container Throughput (m TEUs)	81.6[2]	World No.1	2.5[2]	7.6[2]	8.4[3]

Source: Government statistical departments in the relevant jurisdictions, HKTDC Research, Wind, Statista.
Note: 1. 2021 figures; 2. 2020 figures; 3. 2019 figures; 4. 2018 figures.

The GBA is arguably one of the few regions where, within an hour of transit, a company can access the fullest scope of capital, talents, technology, production, logistics, marketing and consumers, all in one place.

For example, a multi-national company can establish its local marketing and sales headquarters in an influential city such as Guangzhou and set up its technology R&D center in talent heavy Shenzhen. The firm would then outsource its manufacturing to suppliers in Dongguan, Foshan or Nansha where there is the highest concentration of electronics, machinery and consumer products companies in the world. MNCs would be given the opportunity to operate an integrated logistics chain

through domestic hubs in Zhuhai or international ports in Hong Kong and Macau, while obtaining domestic or international financing through Shenzhen and Hong Kong, as well as participating in global trade fairs at the Guangzhou Fair or in one of the many resorts in Macau. This would be made possible by the region's high living standards enabled by world-leading education, healthcare and ESG-compliant infrastructure.

Case Study of Shenzhen: how it developed from a fishing village into a globally leading technology center

In 1992, more than a decade after the introduction of the reform and opening-up policies, China's then leader Deng Xiaoping undertook his famous "southern tour" ending in the city of Shenzhen. By then, Shenzhen had already experienced a decade of rapid economic and urban development as China's first Special Economic Zone, where it benefitted from its proximity with international trading hub, Hong Kong, while still being connected to mainland China. This allowed Shenzhen to develop from a rural fishing village of a few thousand people into an 18 million mega metropolis today (China's third largest city after Shanghai and Beijing) and nurtured a long list of world- leading companies such as Tencent, Huawei, BYD, Mindray etc.

Against the backdrop of China's reform and opening-up policies, Shenzhen was given a pioneer role in testing new reform policies that would increase societal efficiency while taking into consideration China's specific economic characteristics. The city continuously implemented a plethora of bold reform policies to reduce bureaucratic

hurdles and created sustained innovation and productivity. In addition, new privatization policies pertaining to land use, residential and commercial real estate, financial services and human resources etc. were proven highly successful and became policy models for other regions across China. Through these market-oriented reforms, Shenzhen became a major economic engine attracting continuous inflow of domestic and international capital, talent, technology and innovation.

"The most important learning from the Shenzhen experiment is to have the courage to be audacious. Without this daring spirit, a risk-taking mindset, and an infectious conviction, one cannot forge a good path or achieve great new things."
Deng Xiaoping

Thanks to four decades of continuous experimentation and policy reforms, today Shenzhen boosts one of the highest concentrations of multi-billion-dollar private enterprises in China, and became a role model for other cities to adopt those reforms

Tencent 腾讯	招商银行	HUAWEI	BYD	SHEIN	mindray	中国平安 PING AN	中信证券 CITIC Securities
$424bn	$139bn	$100bn+	$98bn	$80bn	$54bn	$42bn	$40bn
SF EXPRESS 顺丰速运	万科	华润置地	dji	商汤 sensetime	ZTE中兴	鹏鼎控股 AVARY HOLDING	HEYTEA
$36bn	$31bn	$31bn	$25bn	$20bn	$15bn	$10bn	$9bn
金地商置	TRANSSION HOLDINGS	OCT 华侨城	CHINAGAS 中国燃气	SUNWODA	CIMC	大族激光 HAN'S LASER	华大基因 BGI
$9bn	$8bn	$7bn	$6bn	$6bn	$6bn	$4bn	$4bn
OFILM 欧菲光	怡亚通 Eternal Asia	大悦城 JOY CITY	Nonfemet	华强集团	龙光地产 LOGAN PROPERTY	神州数码 Digital China	Hytera
$3bn	$2bn	$2bn	$2bn	$2bn	$2bn	$1bn	$1bn

Note: figures denote latest market capitalization or valuation in billions of USD

Land & Housing Reforms

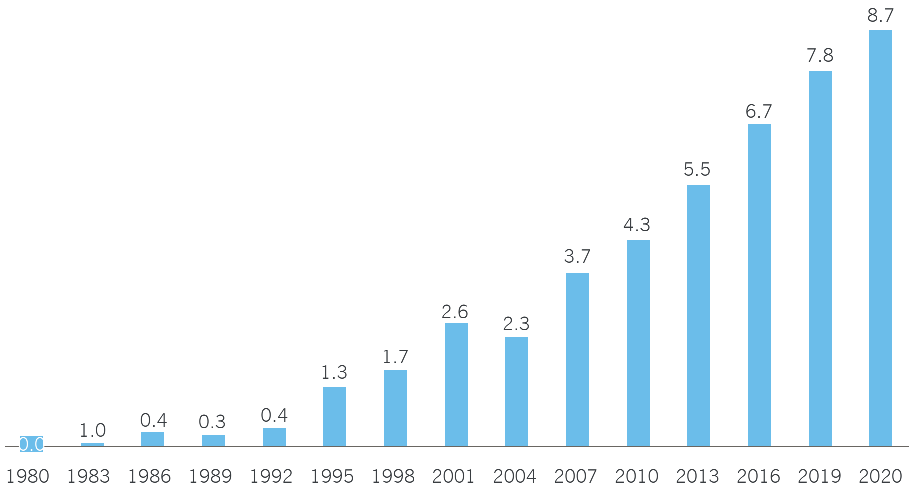
Before 1981, all urban land belonged to the State while land in rural areas was collectively owned by local agricultural production entities. Shenzhen took the lead in reforming the land use system by separating the national ownership of land from rights of use and implementing auction systems for all commercial and industrial land to enable more market-driven and efficient allocation of land resources. Shenzhen also implemented comprehensive housing system reform to achieve housing commercialization. These reforms helped to establish a modern real estate market that transformed China's urban landscape.

Today, Shenzhen is considered China's most valuable real estate market alongside Shanghai. Both cities experienced four decades of continuous real estate growth, particularly throughout the pandemic. Some data suggests that with an average price above USD 30k/sqm for premium residential real estate, Shenzhen has surpassed Shanghai by 10-20% and Beijing by over 30% due to the city's strong employment market, high concentration of profitable companies, high living standards and being in the center of the GBA enabling access to Hong Kong, Macau and Canton within 30-60 minutes.

Attraction of Foreign Direct Investment ("FDI")

Shenzhen was one of the first municipalities in China to open up to foreign direct investment. In order to attract international capital, Shenzhen put in place various fiscal and non-fiscal incentives and preferential policies, including the streamlining of administrative approval processes, preferential fees for land or facility use, concessionary tax rates and tax exemptions, and flexibility in recruiting non-residents. The influx of foreign capital enabled Shenzhen to develop its economy under the lens of international law and market-driven logic while elevating the capabilities of a generation of public service leaders who would later implement these proven methodologies in other parts of China and replicate Shenzhen's success.

Strong influx of FDI to Shenzhen since opening-up ($bn)



Source: Ministry of Commerce, CEIC.

Financial System Reforms

Shenzhen has been spearheading the reform of the financial system to better serve a market-oriented economy and to provide sustainable economic vitality. It led the reform of the state-owned asset management system, building and improving asset supervision and operation systems, allowing financing sources to allocate capital according to market forces. It also introduced licenses to allow foreign banks to enter the market, establishing regional joint stock banks and creating the Shenzhen Foreign Exchange Trading Center as well as the Shenzhen Stock Exchange or "NASDAQ of China" today.

In 2021, Shenzhen went a step further by granting the Qianhai district of the city the special status of "international forex center", enabling a streamlined process for domestic and international currency conversions, facilitating onshore and offshore investments. This has catapulted Qianhai to the forefront of venture capital and private equity investing.

Talent Attraction & Technological Innovation

Shenzhen led the implementation of measures to develop a regional venture capital industry which incubated a slew of highly successful technology driven companies over the last three decades. Beijing's Zhongguancun technology district used to be called China's Silicon Valley, however, due to Shenzhen's more market-oriented policies and its proximity to the international financial center Hong Kong, Shenzhen is now described as China's true Silicon Valley, home to hundreds of multi-billion dollar technology companies and thousands of billion dollar supplier and services companies in this ever expanding technology ecosystem.

Shenzhen not only attracted millions of highly educated and skilled technology engineers but also established one of the strongest legal environments in China (IP protection) which helped Shenzhen become a globally competing R&D center.

Coupled with preferential tax policies and government subsidies for next generation technologies such as 5G/6G applications, autonomous driving, high-end sensors and semiconductors, AR/VR etc., the city today spears China's transformation into an innovation and AI-enabled economy.

The Greater Bay Area Strategy

The Guangdong-Hong Kong-Macau Greater Bay Area encompasses nine cities of the Pearl River Delta in Guangdong Province (Guangzhou, Shenzhen, Zhuhai, Dongguan, Foshan, Huizhou, Jiangmen, Zhaoqing and Zhongshan), and two Special Administrative Regions of the People's Republic of China (Hong Kong and Macau). The links between Hong Kong, Macau, and the Pearl River Delta have been broadening and deepening since the onset of China's reforms starting in 1978, but particularly since China regained sovereignty over Hong Kong (in 1997) and Macau (in 1999).

The GBA was of the world's most dynamic economic regions over the last four decades and contributed immensely to China's overall economic growth. The region has gone from an economic backwater to an economic powerhouse with global importance in manufacturing, trade, logistics, tourism, finance and R&D. By 2021, the GBA reached a population of 86 million people (size of Germany) and a GDP of around US$2 trillion (size of Canada) which would have made it the 10th largest economy among the world's national economies.

The economic, social, interpersonal and inter-governmental linkages have helped the region grow and develop rapidly while substantially improving living standards. Today, the GBA is moving past being the "factory of the world" to becoming the "next generation innovation center" leading the way of cutting-edge technologies not just in China but on par with the world.

The completion of key infrastructure connections (e.g. the high-speed train line connecting downtown Hong Kong to downtown Shenzhen in only 18 minutes and Guangzhou in another 20 minutes, or the Shenzhen - Hong Kong - Macau cross ocean bridge) and the establishment of various development policy packages (e.g. "Leading Group for GBA Development" and "The Outline Development Plan for the Guangdong-Hong Kong-Macau Greater Bay Area") are providing sustainable growth impetus to the region.

These developments are creating significant opportunities for both domestic and international businesses and investors. These opportunities arise from the sheer economic size and growth rate of the region, creating a virtuous cycle of increasing connectivity among people and cities, further attraction of capital and companies, leading to a continuous rise in technological and industrial value chains.

Land Area, GDP and Population of the 11 Cities in the GBA (2021)

Source: Wind, Hong Kong Census and Statistics Department

China's GBA is arguably one of the most well-connected urban clusters with the world's most advanced infrastructure buildouts

The region is composed of the most economically developed part of Guangdong, the largest Chinese province in economic terms: Hong Kong, a leading international finance and trading center, and Macau, a world leading leisure & entertainment destination. The region also includes the world's leading airport for international air cargo (Hong Kong), the world's fourth, fifth and eighth largest container port cities (Shenzhen, Guangzhou and Hong Kong), one of the world's leading IPO centers (Hong Kong) and China's second largest RMB IPO center (Shenzhen).

The region's development has accelerated with the completion of several major infrastructure projects, such as the Hong Kong-Zhuhai-Macau Bridge, highspeed train connecting Hong Kong-Shenzhen to Beijing and Shanghai and the new maglev train running from Guangzhou through Nansha and Dongguan to Hong Kong, which are drastically augmenting the region's internal and external connectivity.

Source: Baidu.Com

GDP Ranking in 2021: GBA is Among the World's Top 10 Economies

Rank	Economy	2021 GDP ($bn)
1	United States	23.00
2	China	17.46
3	Japan	4.94
4	Germany	4.23
5	India	3.04
6	France	2.94
7	United Kingdom	2.76
8	Italy	2.10
9	Canada	1.99
10	**GBA**	**1.93**
11	South Korea	1.80
12	Russia	1.78
13	Australia	1.63

Source: Countryeconomy, Statista, IMF, Government statistical departments in the relevant jurisdictions

The region's accelerated development has also created a large and affluent consumer market, nurtured a world-leading technology ecosystem which consists of industry leaders such as Tencent, Huawei, Mindray, and catapulted Hong Kong and Shenzhen to leading positions in USD and RMB capital markets.

Shenzhen

Guangzhou

Hong Kong

Macao

Zhuhai

Dongguan

Foshan

Zhongshan

Hong Kong-Zhuhai-Macao Bridge

China's Macroeconomic Environment

China is the world's largest economy by purchasing power parity and the world's second-largest economy by nominal GDP and consumer expenditure.[a] Until 2021, China was one of the world's fastest-growing major economies with GDP growth rates averaging 9% over the past three decades, and the only world major economy that recorded positive GDP growth rate in 2020 amid the COVID-19 pandemic[b]. Such rapid expansion was largely supported by the country's economic reforms, demographic dividend and policies that lifted over 700 million people out of poverty. Over the past few years, China's economic growth slowed from a double-digit rate to between 5-6% as the government is now prioritizing high quality sustainable long-term growth and 2060 carbon neutrality goals. Nevertheless, China is expected to continue outperforming most major economies, driving by its technological innovation and ample policy headroom.

China will usher in its next 5-year leadership and economic development plan in November 2022

Growth profile will be different and growth quality will improve

As the macroeconomic environment continues to find stability, China's growth profile is also evolving from investment-driven to technology and consumption-driven. In particular, capital-intensive growth propellants such as fixed asset investment and exports are unlikely to boost growth as much as they did in the past decades, although some rebalancing is manifesting in these segments. In turn, domestic growth driven by technological innovation and consumption of goods and services is taking center stage. In recent years, China has put great emphasis on self-sufficiency in critical technology and plans to further increase national spending on technology R&D. Benefiting from strong consumer income and household spending growth, China's consumer economy was still growing at 10% year-on-year during 2015-2018 against a backdrop of overall slowdown in economic growth.[c]

China's growth quality is also improving, resulting in a more balanced and sustainable growth profile. Reducing investment, especially in oversaturated and polluting sectors, while promoting innovation and consumption should help divert capital to areas where supply has not caught up with demand. Rising consumption demand could also stimulate job creation in the tertiary sector, which typically offers higher wages than the secondary industry, thereby reinforcing income growth and helping to absorb the potential impact from sectors facing macro challenges. China also aims to close the gap in advanced technologies (e.g. high-end semiconductors, sensors, automation technologies, materials, biotechnology, etc.) and compete with the US over core technologies such as 5G/6G, semiconductors, robotics and high-end manufacturing.

In 2022, while GDP growth is expected to slow down reflecting a less favorable global outlook and the government's continued deleveraging efforts, the momentum is expected to pick up later in the year and leading into 2023, aided by more supportive fiscal and monetary policies. For example, the PBOC has started reducing bank reserve ratio and benchmark interest rates, as well as lowering the hurdles of lending to small and medium-sized enterprises (SMEs) and the real estate sector. Government policies are aiming at resolving social imbalances and systemic financial risks and transitioning from post-pandemic recovery to high-quality long-term growth.

[a] Source: World Bank, Euromonitor
[b] Source: World Bank
[c] Source: National Bureau of Statistics of China

China aims to find a balance between disruptive technological innovations and their associated societal implications, while putting more emphasis on long-term sustainable growth drivers such as climate-tech, hard-tech and life sciences, etc.

In 1Q 2022, the government announced a series of supportive policy directives reaffirming the leadership's continued commitment to the development of high value-added private enterprises, innovative technology companies, real estate and associate sub-sectors, environmentally sustainable manufacturing, socially responsible financial institutions among others. Overall, these announcements were well received by the domestic and international markets and underpinned China's commitment to the world to strive for environmentally sustainable economic development.

Clearer Government Directives on Supported Strategic Sectors

Jan. 16. Presidential speech on the logic behind recent regulatory measures to correct negative societal impacts from monopolistic behaviors by certain technology conglomerates, and 7 directives on China's digital economy advancement in the coming years:

1	**Increase Capabilities in Developing & Owning Core Technologies**	Better utilize China's advantages of state-supported fundings, largest market size and fairly advanced existing technology base to quickly develop and own core technologies and innovation capabilities
2	**Accelerate Next Generation Digital Infrastructure Build-Outs**	Better utilize China's continuously expanding 5G networks and country wide digital data central networks to create omni-networks between ground stations and satellites with cloud and AI capabilities for an advanced comprehensive digital infrastructure; this will strengthen China's development of globally leading software companies to fuel the advancement of wide ranging industries
3	**Further Integrate the Digital Economy with the Real Economy**	Advance the digitization, connectivity and AI-capabilities of the manufacturing, services, agriculture and other key real economy sectors to improve scalability, efficiency and specialization of these industries; don't digitize for the sake of digitization but to achieve real innovations
4	**Key Focus on Tackling Missing Core Technologies**	Mobilize and concentrate resources to tackle key missing technologies in the areas of semiconductors, printed circuits, next generation displays, communication equipment, smart sensors and hardware etc. to elevate a group of champion companies from China that are globally leading in these core technologies, while also firmly control the supply & value chain of these technologies in key technology clusters across the country
5	**Regulatory Monitoring and Compliance to Go Hand in Hand with Fast Development**	Continually monitor and regulate on anti-competitive behaviors that harm societal interests or cause monopolistic cornering of markets, protect consumer interests and state tax revenues
6	**Further Perfecting A Digital Economy Governing System**	Comprehensively develop oversight, regulatory and enforcement bodies to cover R&D, production, operation and funding aspects; to ensure core technologies and leading companies are controllable
7	**Partake in Global Standard Building of Next Generation Technologies**	Pro-actively voice China's standpoints and views on cutting edge technological developments, while adapting global standards to China's domestic realities and needs; increase digital economy awareness at all levels of government officials to better assist local economic development needs

Supported Technology Sub-Sectors

Software

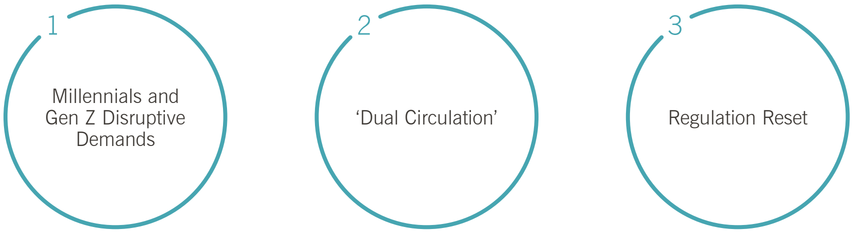
	IVC PC
• AI for Business Decision-Making	商汤 sensetime; TERMINUS 特斯联
• Robotic Process Automation	
• Asset Management Digitalization	
• SaaS	Linkedcare 领健

Hardware

	IVC PC
• Industrial Robotics	
• Semiconductor	nreal
• Electric Vehicle Upstream (e.g. Lithium Battery, Sodium-ion Battery)	CiDi
• Green-Tech Solutions	

Note: Indicative as per latest available market information.

Key Megatrends Driving China's Long-Term Growth



Millennials (born in 1980-1995) and Gen Z (born in 1996-2010) have a global population of 1.8 billion and 2.5 billion respectively. In particular, Gen Z forms the largest generation segment of the global population. In China, the number of Millennials and Gen Z is estimated to be 350 million and 250 million, respectively. Gen Z is becoming the key growth engine of global consumption, which is also the case in China. Gen Z's distinctive characteristics: they embrace diversity, value creativity and authenticity; they are digital natives; they are vocal and want to be heard.

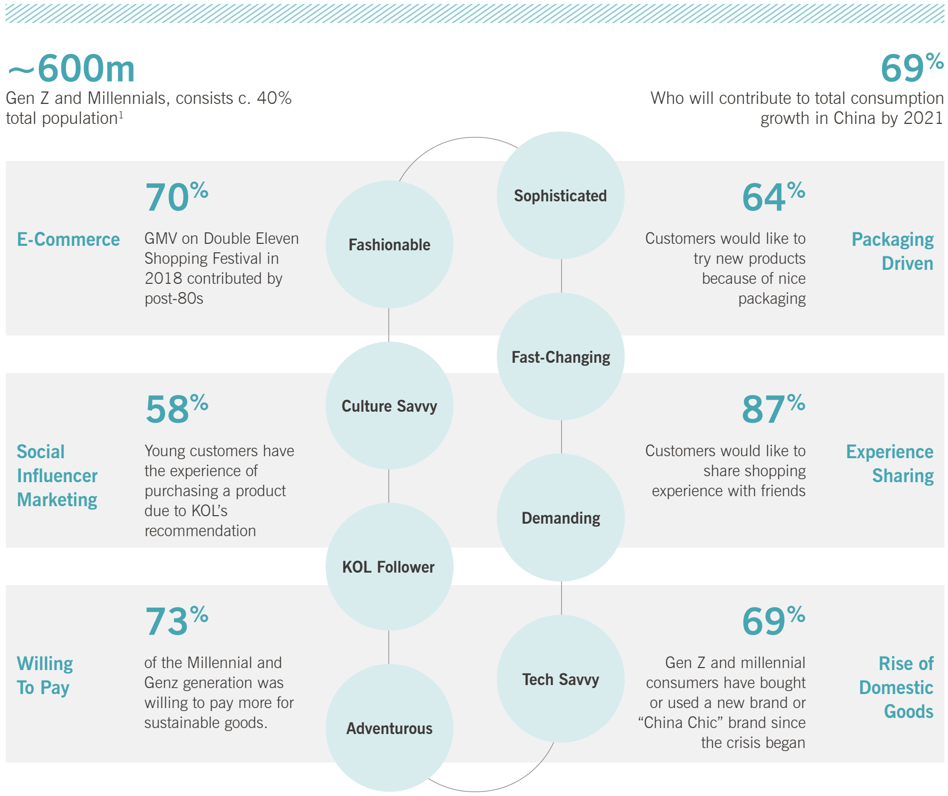
Gen Z trend towards online media and virtual consumption, with strong exposure to live streaming, video games, and social media. As digital natives, Gen Z has a constant demand for expedited and intuitive user experience, with preference for mobile-based services for digital payments and e-commerce over traditional off-line

transactions. Gen Z values physical fitness, healthy diets, mental well-being and healthy lifestyles. In addition to personal well-being, social consciousness is also a key part of Gen Z's identity. Their awareness in public welfare and the environment is driving trends in responsible sourcing, renewable energy, and eco-friendly consumption.

In China, Gen Z is becoming the core driving force of consumption growth. Gen Z consumers usually have a strong individualistic streak with strong family support. They are tech-savvy and enjoy researching and comparing products before making purchasing decisions. They are also less attached to brands and are constantly on the lookout for innovative and novel products. They highly value experience, aesthetics and quality.

They are less price conscious compared to previous generations and are willing to pay for what they like and value.

Having experienced China's economic boom over the last three decades, Gen Z has a strong sense of national identity and pride in supporting domestic brands (over 100,000 new domestic brands were launched on Tmall from 2018-2000 alone). In addition to these B2C trends, a plethora of B2B business models have emerged at the product and channel levels to satisfy the ever-changing demand of the new generation. There is a long runway on innovation and investment opportunities in the B2B side throughout the entire supply chain, including enterprises, logistics and financial services.



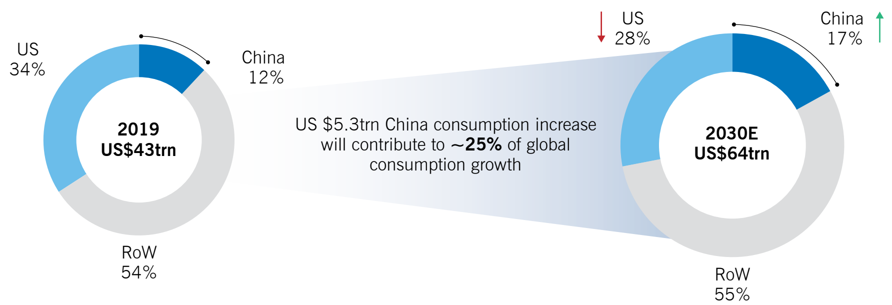
China's economic growth has been largely reliant on investments since 2008 (reliant on exports prior to the global financial crisis) as the government's post-crisis stimulus policy mainly focused on capex in infrastructure, real estate and manufacturing. The rapid capital accumulation over the years has resulted in an unusually large capital stock for its income level which leaves limited scope for additional expansion.

Consumption, on the other hand, represents a low share of the economy when compared to investments and other developed economies. An aging population, together with improving public and private provisions and financial development are expected

to drive the rise of households' share of national income. The fall of household savings ratio going forward allows consumer spending growth to outperform economic growth for the foreseeable future. In the past five years, China's domestic consumer market has grown dramatically in size and increasingly driving the overall economy. According to the World Bank, China's consumption market is expected to double and contribute to 25% of the global consumption growth over the next decade.

Megatrend 2 – "Dual Circulation"

"Dual Circulation" has been the new model of development in China since the start of the pandemic, aimed at forming a development layout that focuses on the domestic market as the foothold of economic growth, whilst letting the domestic and international markets boost each other. "Dual Circulation" has now been elevated into the new economic framework for China's medium and long-term development. "Dual Circulation" refers to 1) domestic circulation, and 2) international circulation. Taking into consideration the external and geopolitical environment, priority efforts focus on stimulating domestic



demand and domestic growth drivers to improve economic resilience and self-sufficiency as a first step. Efforts are also being made to deepen reform on the supply side by creating a unified and open domestic market and better matching capabilities and resources to the local needs.

Government initiatives work hand in hand with market forces to achieve an optimal balance between self-sufficiency (domestic circulation) and global cooperation (international circulation) to drive long-term sustainable growth. Policies targeted towards encouraging openness and strengthening engagement with global markets, as well as enhancing domestic economic growth, will be promoted.

The purpose of "Dual Circulation" is to help China better position itself in the long run to withstand global uncertainties and less benign external environment, characterized by global economic downturn, rising protectionism, heightened geopolitical tensions, and a shrinking international market. In particular, the sharpening of geopolitical competition has caused a general resistance to globalization in the West. China entered a new paradigm in which it will have to counteract a global economic environment that is less conducive to free trade, capital and technology flows. To better address and manage these changes, China will utilize resources more efficiently to drive its economy by stimulating domestic demand, upgrading consumption, and further investing in technology and innovation efforts. Notwithstanding the above, China remains a strong supporter of globalization and will continue to deepen its cooperation with foreign markets while opening up its own.

China's social-economic shift and its rising middle class continue to be a main growth driver for the domestic market. According to a recent report issued by the Development Research Centre under China's State Council, China's per capita GDP is forecast to reach US$14,000 by 2024, and China's market will be bigger than that of the United States by 2025, with at least 560 million middle-income consumers. China's ever-expanding consumption market presents huge opportunities for both domestic and foreign enterprises.

Against this backdrop, the Chinese government announced the "Dual Circulation" strategy which will focus on fully utilizing domestic resources to drive the domestic economy. Meanwhile, China will continue to open up its domestic market and to cooperate with global markets. Based on the dual circulation initiative, China is expected to focus on areas highlighted below:

Proposed Areas of Focus

On the Domestic Side	On the International Side
1. Cementing China's position as a manufacturing powerhouse by building modern, efficient, integrated end-to-end supply chains and industrial clusters, especially in the areas of high-tech and advanced manufacturing	1. Promoting trade and investment liberalization and facilitation, optimizing the business environment, and offering "national treatment" to foreign investors
2. Strengthening technology levels and speeding up innovation and breakthroughs in core technologies	2. Innovating and experimenting liberalization measures and preferential policies via pilot free trade zones and ports and special economic pilot zones, e.g. the Greater Bay Area, the Hainan Free Trade Port, etc.
3. Increasing investments in infrastructure, including rural amenities, urban subways and inter-city transit systems, high-speed expressways and railroads, 5G base stations and new and clean energy sources	3. Strengthening economic and trade cooperation with countries and regions along the "Belt and Road", as well as engaging more deeply with ASEAN countries and other developing countries
4. Enhancing capabilities and reducing reliance on the global economy in key strategic areas, such as energy, technology, and food	4. Upholding the multilateral trading system and actively participating in the negotiation and formulation of international and regional economic and trade agreements, as well as steadily reducing tariff levels
5. Creating a level playing field by minimizing the government's intervention in microeconomic activities and ensuring better integration of the roles of the market and the government in resource allocation	5. Expanding the imports of high-quality goods and services to meet domestic demand
6. Improving the overall wealth of its peoples, enlarging and enriching the middle class, redistribution of wealth via policies and support measures, e.g. subsidies, social security reforms and tax cuts	

By building up a more resilient and robust domestic economy while integrating itself with the global market, China will be able to better develop and leverage its core competencies, move up the value chain, better position itself strategically for long-term sustainable growth, and play a key role in orchestrating global supply chains.

Megatrend 3 – Regulation Reset

For decades China has relied on its manufacturing advantages to support domestic economic development. The country is now increasingly seeking to shift to an innovation-based, technology-driven and environmentally sustainable growth paradigm. With an ambition to become a global leading innovation engine, China has announced a series of policies and regulations that highlight critical technologies for which it will boost R&D spending and aim for technology autarky. At the same time, China also pledged to continue regulatory oversight on the domestic consumer-based Internet sectors, to address long-overdue societal imbalances exacerbated by the excessive expansion of Internet giants in the absence of societal surveillance over the last decade.

Behind the regulation reset are China's new objectives: (i) technological independence, (ii) anti-monopoly and (iii) common prosperity.

(i) Technological independence - the government aims to achieve technology self-reliance with breakthroughs in core technologies by 2035. It has launched supportive policies including tax reliefs and R&D subsidies to encourage investments in sectors such as next-generation AI, semiconductors, 5G, cloud computing, new energy vehicles and biotechnology.

(ii) Anti-monopoly - with a goal of ensuring fair market competition, the government will continue its efforts against monopolistic behaviors. Such efforts, which include anti-trust regulations, will provide a more level playing field for innovators to grow and create more attractive opportunities for investors in the relevant sectors.

(iii) Common Prosperity - China's 14th Five Year Plan calls for 'notable and substantial progress' towards common prosperity by 2035. The plan aims to achieve a more equal society with better social welfare and promote further household income growth. It also aims to narrow the gaps between different income groups, between urban and rural areas, and among different regions. Common prosperity is not plain egalitarianism. We believe the plan will support overall labor income growth, sustainable growth of SMEs and services sectors, and ultimately keep sizing up the middle-class segment in China.

The GBA Stands to Benefit from these Megatrends

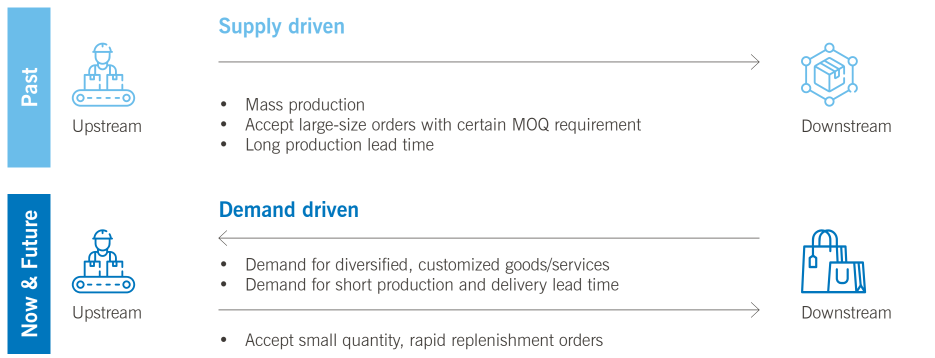
With these mega trends in mind, there will be significant opportunities in the B2B and B2C fields in the GBA. The B2B market in the GBA is still highly fragmented and distinctly different from the B2C market which innovates around consumers, products and channels. B2B business operators need to satisfy the ever-changing consumer demand by refining product and channel management, supported by enterprise, logistics and financial services at one level and technology (AI, blockchain, Cloud and Data) infrastructure at another.

B2B services	Enterprises services	Logistics services	Financial services
B2B infrastructure	Technology	ABCD	(AI, Blockchain, Cloud services, Data)

Digitization and innovation in B2B businesses in the GBA is rapidly growing, with different paces in various supply chains, verticals and support services. No single service provider dominates all market segments for the time being.

Key Drivers of Innovation in GBA's B2B Business:

(i) Changes in consumer expectation drive B2B business transformation - Chinese consumers today are empowered by mobile technology and have lifestyles and consumption habits that are different from those of previous generations. To differentiate themselves from competitors, many B2C operators are exploring innovative ways to enhance their supply chain capabilities to cater to customer demand faster, with higher precision and increasing use of AI. Competition is driving the business transformation in their B2B partners.



(ii) Government support for B2B innovation and acceleration of industrial upgrading

Pain points facing the traditional B2B business in China:

- Aging labour force and increasing production costs
- Provision of low value-added services along the global value chain without owning the core technologies, earning a very thin margin
- Homogeneous competition in local market
- Severe international competition in the globalized era

To climb from the bottom of the global value chain, B2B business operators have to explore innovative models and transform from being OEM to become ODM or OBM

A number of regulations promulgated in the recent years are conducive to the development of B2B business in China

Made in China 2025

By The State Council, 2015

Guiding Opinions of the State Council on Deepening Integration of Manufacturing Industry and Internet

By The State Council, 2016

Integration and Development Plan of Informatization and Industrialization

By Ministry of Industry and Information Technology, 2016

Guiding Opinions of the General Office of the State Council on Vigorously Advancing the Innovation and Application of Supply Chains

By The General Office of The State Council, 2017

(iii) Technological advances lead to digital transformation

The lockdowns due to the COVID-19 outbreak have accelerated technology adoption and digitization of businesses. Many companies strive for balance between their business transformation plans and ROI of technological projects. Companies are also making efforts in enhancing supply chain resiliency and visibility. More stakeholders are willing to collaborate with each other and act fast in order to survive the volatile business environment and quickly respond to changes in consumer demand and regulatory shifts.

More B2B customers expect not only sustainable and quality products, but also excellent producer services. At the same time, more B2B companies invest in product design

DATA

Consumers

Mobile technology

Anytime (24 hours x 7 days); Anywhere (shop, restaurant, home, office, on the road, etc.)

- Product research
- Product reviews
- Order placement
- Consumer financing

Artificial Intelligence | Big data analytics | DATA | Blockchain | Cloud computing

Product Development and Design
- Virtual Design
- 3D scanning
- 3D printing

Manufacturing and Quality Control
- Internet of Things
- Augmented Reality/ Virtual Reality
- Robotics
- Automation

Sourcing/ Distribution
- Online marketplace
- Supply chain finance platform
- Sale/ Inventory management system

Logistics
- Automation
- Robotics
- Augment Reality/ Virtual Reality
- Internet of Things
- Unmanned vehicles
- Sharing platform

Software as a Service (SaaS)
- Customer relationship management
- Human resources management
- Enterprise resources management
- Supply chain management
- (Remote) Office assistance
- Financial management
- Logistics management
- E-contract

DATA

and brand building, with the ultimate goal of climbing the value chain and earning higher margins. There has also been a shift from traditional sales to digital sales by B2B companies. On top of domestic B2B e-commerce, the growth of B2B export e-commerce has also been remarkable. More resources and favorable policy support for B2B e-commerce and export e-commerce are expected.

Further Economic Opening Will Upgrade Various Industries in the 'Inner Ring' and 'Outer Ring' of the GBA

"Inner Ring"

- Hong Kong-around Shenzhen-Dongguan-Guangzhou-Foshan-Zhongshan-Zhuhai-Macao will be the "Inner Ring"
- Most parts accessible in 2hours (or even 1 hour) from other parts of the "Inner Ring"
- This will be a connected regional economy
- It will contain the main administration, tech, advanced manufacturing, high-end service centers

"Outer Ring"

- Heavier industry, labor-intensive
- Support for diversification
- "City clusters" of Guangzhou-Foshan-Zhaoqing, Shenzhen-Dongguan-Huizhou, Zhuhai-Zhongshan-Jiangmen already cooperating to develop the outer ring

Roles

"Old"
- Transport / logistics hub
- Financier
- HQ location
- "Front window"
- Manufacturing investor…

"New"
- Services investor
- Idea generator
- Data center
- R&D center…

Industries

"Old"
- Light manufacturing
- Transport / logistics
- Finance
- Infrastructure…

"New"
- Advanced manufacturing
- Heavy industry
- Consumer services
- Advanced producer services
- New financial services
- Education and medicine
- Cultural and creative industries…

With tens of thousands of innovative, growing, and profitable companies in China's GBA, the Investcorp China team continues to explore attractive opportunities for our global clients

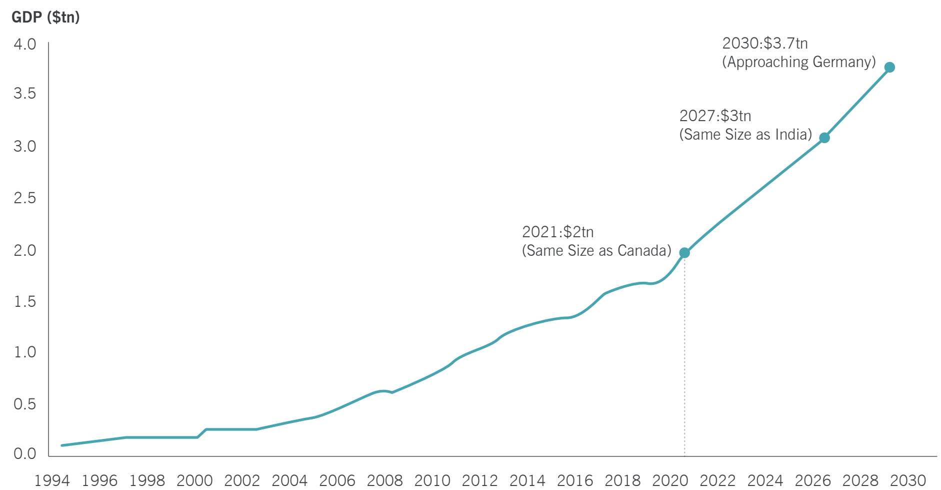
Business Opportunities in the GBA

The GBA has a large and vibrant consumer market of 90-100 million people with approximately US$20,000 GDP per capita (projected to reach US$44,000 by 2030) and growing demand for public and private services and goods.

The GBA also has a diversified industrial composition with respect to: (i) high-tech, mid-tech, and low-tech; (ii) light, medium, and heavy; (iii) final assembly, components, inputs, machinery, equipment; (iv) logistics, finance, advanced producer services, industrial services; and (v) R&D, tech services, creative industries.

All of the above is accessible within a 2-3-hour ring, which makes selling, logistics, fulfilment, marketing and branding much easier and more efficient than most of the other parts of the world while creating exciting new investment opportunities.

The Above Growth Policies Aim to Propel GBA's Economy to the Size of UK or Germany in the Next 5-7 Years.



Source: National Bureau of Statistics of China, IMF, World Bank
Note: The GBA's GDP was calculated by aggregating GDPs of its 13 cities

Conclusion

As the second largest economy contributing more than 15% of the global GDP in 2021 (compared to approximately 20% for the US), China's economic health and prosperity are of paramount importance to the economic and political stability of the globe. The GBA being one of the main economic engines carrying China forward into its next decade of development, is assuming an increasingly critical role in spurring policy reforms, technological innovations and capital formation. Investcorp PE China aims to continue to provide insightful assessments and emerging trend observations from our region to our global readership.

Since 2020, Investcorp has had an on-the-ground team in China. Although our office is in Beijing, the team travels to the GBA on a bi-weekly basis as many of the attractive opportunities we see are based out of Shenzhen, Guangzhou, Hong Kong or the surrounding cities. Together with Investcorp's long-standing business partners, Investcorp have developed proprietary relationships with an increasing number of successful mid-cap companies in the GBA with growing EBITDA and solid management.

Similar to SMEs in the Western hemisphere, many of these mid-cap companies in the GBA also face generational succession issues. They range from skin care products

to medical equipment to industrial services, and are all growing with healthy EBITDA margins. Investcorp sees an opportunity to conduct control buyouts of these profitable companies while retaining the founders to stay on as minority partners, but to incentivize a next generation of professional management teams to unleash these

businesses' potential. By leveraging our partners' supply chain and operations expertise, and Investcorp's global platform with access to highly relevant markets such as the GCC, we believe these GBA-centered mid-cap companies can be grown into significantly larger players.

ABOUT INVESTCORP

Investcorp is a global investment manager, specializing in alternative investments across private equity, real estate, credit, absolute return strategies, GP stakes, infrastructure and insurance asset management. Since our inception in 1982, we have focused on generating attractive returns for our clients while creating long-term value in our investee companies and for our shareholders as a prudent and responsible investor.

We invest a meaningful portion of our own capital in products we offer to our clients, ensuring that our interests are aligned with our stakeholders, including the communities that we operate within, towards driving sustainable value creation. We take pride in partnering with our clients to deliver tailored solutions for their needs, utilizing a disciplined investment process, employing world-class talent and combining the resources of a global institution with an innovative, entrepreneurial approach. In January 2022, Investcorp issued its 2021 Responsible Business Report which outlines its Environmental, Social, and Governance (ESG) highlights for 2021 and specific initiatives the Firm implemented to meet its goals www.investcorp.com/esg/

Investcorp has today 13 offices across the US, Europe, GCC and Asia, including India, China and Singapore. As of June 30, 2022, Investcorp Group had US $42.7 billion in total AUM, including assets managed by third party managers, and employed over 480 people from 50 nationalities globally across its offices.

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