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Venture Investing:
Insights into China's Dynamic Healthcare Industry

Forum Spotlights

Seeking growth and diversification, institutional investors have long included emerging markets exposure in their portfolios. The agenda for Commonfund Forum 2021 included a session dedicated to private equity in the emerging markets. In particular, the session focused on the opportunity set within the healthcare market in China and how hands-on, active management from skilled private investors could lead to attractive investments.

Nisa Leung, Managing Partner and Head of the Healthcare Practice for Qiming Venture Partners, took those participating in the virtual Forum session inside the world of venture investing in today's Chinese healthcare market. Ms. Leung was interviewed by Commonfund Capital members, Aaron Miller, Managing Director, and Associate Director from the Beijing office, Xiaonan Tian. Excerpts from the discussion follow.

Note these Commonfund Forum comments have been edited for clarity and brevity.

To start, tell us a bit about Qiming's strategy and investment focus.

We were fortunate to start investing in healthcare early on. From day one we would do two or three deals a year. But it kept growing and growing and in the last few years, on average, we've done about 20 to 30-plus new investments every year. On top of that, there have been follow-on investments. In healthcare, we have invested in a total of about 100 companies. When we first invested, portfolio companies were usually one- to three-person teams with a unique idea or thesis. Out of the 100 companies I would say about 70 of them have grown to be leaders in various sectors of the healthcare industry. And we've been very successful with IPOs. Last year, we had 12, including 10 in healthcare, and four of them have a valuation of about $15 billion and we own 10 to 20 percent of some of these companies. The rest are valued between $1.5 and $7.5 billion.

COVID-19 and its impact on the macroeconomic environment have been ongoing topics of discussion. Can you give us an on-the-ground perspective of what's happening in the Chinese economy vis-à-vis healthcare?

The first couple of months of 2020 in China were very slow economically owing to COVID. At Qiming, we were busy trying to get supplies from portfolio companies to the front line where they were most needed. We had about 60 portfolio companies representing the diagnostics side, the vaccine side, drug development or services and all were involved in the effort. It was a stark contrast compared to 2003 when we had SARS and China didn't have the ability to develop its own diagnostic tests. Now, within one month of the COVID outbreak over 100 diagnostic tests were developed for use in China.

What's really interesting is that early on there was not enough personal protective equipment (PPE) in China. So, we put together a WeChat group with many portfolio company CEOs and they helped each other get PPE. After China started to have enough PPE, we began sourcing for overseas, for Europe, the U.S. and elsewhere. One of our companies is the leading ventilator provider in China so I made an introduction to Gov. Cuomo's office in New York when it was really difficult to get ventilators.

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>
> *– Nisa Leung*

By the end of Q2, things started ramping up again and we were very surprised to see how the economy gained speed. And on the healthcare side, activity also picked up and, in fact, grew beyond the pre-COVID numbers. For example, in 2020 PCP fundraising was $56 billion, which was 2.3 times what it was in 2019. So, we believe that 2020 will go down in history as the year of COVID, but the disruptions caused by the pandemic faded quickly and investment in Chinese healthcare has truly ramped up.

We've heard quite a bit on both sides of the ocean about China and U.S. decoupling. The storyline is that supply chains won't be as tied to one another, there will be more independence, etcetera. What is your perspective and what have you seen in terms of decoupling?

Decoupling will have less effect on the healthcare sector than on AI (artificial intelligence) or other more sensitive areas. So far, we've been investing in some cross-border companies but because of perceived decoupling we've seen more entrepreneurs moving from the U.S. back to China to start companies. In fact, one of our companies is the leading gene therapy company in China and it is the third company this entrepreneur has founded. The first two were founded in the U.S. and one of them was acquired recently in the U.S. for about $4 billion. Another consideration is that China continues to be a good and less expensive ground for clinical trials. It's also easier to recruit patients. So, if entrepreneurs feel there is somewhat of a decoupling, then they almost have to choose between the U.S. and China. We and they would prefer not to but, if necessary, China may be the choice just because it's cheaper to get to proof of concept. We hope we will have more collaboration so that scientists in both the U.S. and China can work together.

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Can you talk about the story associated with vaccine developer and portfolio company CanSino?

CanSino is a reference to Canada and China. The four founders were buddies in Toronto who were all senior-level executives in leading pharma companies. One day they were at a barbecue and they talked about moving back to China and starting a vaccine company that could really make a difference. So, that's what they did. And when COVID hit, we were on calls frequently as members of the board and we were hearing about their progress first-hand. In early February 2020, the CEO flew to a World Health Organization (WHO) meeting for in-person consultation.

It was interesting to see the team collect very early clinical trial data and going through phase 1 and phase 2 and choosing whether to develop a drug that is more potent but have more side effects or less potent and have fewer side effects. Different from a lot of others like Moderna and Pfizer, CanSino is not a multinational so they don't have the network to do global trials. So, what happens is they basically have to work with a global contract research organization (CRO) to launch clinical trials in multiple countries. That is very difficult. In fact, throughout the process, I stayed in touch and heard about colleagues who would go to Pakistan to do clinical trials, but they would be stuck in quarantine for the first two weeks and when they left to join another clinical trial in another country, they needed to be quarantined all over again.

Another interesting fact about CanSino is that the company did not receive any funding from the Chinese government to develop the vaccine or manufacture it. This is very different from other companies. We were fortunate to be able to list the company on Shanghai's STAR Market in 2020 and raise close to $700 million for vaccine manufacturing.

We know that China's healthcare system is very different from what it is in Western countries. Can you walk us through some examples of how that applies with respect to technology and healthcare?

Three or four years ago when digital healthcare became so hot in the U.S., we looked at many of these companies in China. I kept telling people we should not be investing in the same model as the U.S. because a lot of digital healthcare companies there were helping to improve the productivity of hospitals. In the U.S., about 90 percent of patients go to private hospitals, whereas in China 90 percent go to public hospitals. Public hospitals don't need productivity software as much, so the type of company that we would be funding in digital health is very different. We've probably turned down 200 or more digital health companies that have raised VC funds but ultimately encountered trouble. The digital healthcare companies that we invested in are doing really well. One is WeDoctor, which has developed China's first internet-based hospital. Another of our companies is the largest electronic medical records (EMR) provider in China. We've also invested in companies that are leaders in AI imaging and AI drug discovery.

Where do you see some of the most attractive opportunities going forward?

I think we're going to move more and more toward innovative platform companies that are becoming global. Take Zai Lab; for example, when we invested it was two people and now it's a $15 billion company and growing very rapidly. Zai Lab is now considered the gateway for U.S. companies wanting to partner in China. We're seeing the same thing for Gan&Lee, the leading insulin company in China: everybody in diabetes is going to them for partnership. Same for Tigermed—we were the only VC investor in the company before it went public. Now it has a $22 billion valuation.

What exit avenues are open to Chinese companies seeking to go public?

There are multiple avenues. Chinese healthcare companies could list in Hong Kong (HKSE) and in mainland China where there are various boards to meet the financing needs of companies carrying different profiles, including the Main Board, ChiNext, New Third Board and the most recently launched STAR Market (the Science and Technology Innovation Board). There are also the U.S. stock markets. HKSE made regulatory changes with Chapter 18A taking effect in Q2 2018, which allows pre-revenue biotech companies to list, and it has become a very successful exchange for healthcare companies that are pre-revenue/profit since then. Then in mid-2019, the Shanghai Stock Exchange introduced the STAR Market as mentioned, which also allows pre-revenue companies to list and has become a popular destination for Chinese bio-tech companies since then. For CanSino (dual-listed on HKSE and STAR Market), as I said earlier, we listed at $700 million valuation and two years later it's valued at about $15–$16 billion. We've seen in the last couple of years that the CAGR (Compound Annual Growth Rate) of our healthcare companies after listing is over 100 percent.

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