52 Capital Partners, LLC

The 52 Institute™

Quarterly Industry Insights

Q2 2019

52 Capital Partners, LLC is a "**growing force** in international M&A transactions."

Business Today, 2018

“We are at a **new normal** for U.S.-China relations economically.”

David P. Willard
52 Capital Partners, LLC
Founder & CEO

Bloomberg News, 2019

The **new model** for delivering strategic advice.

The 52 Institute™

The 52 Institute™

Since the founding of 52 Capital Partners, LLC in May 2018, the firm has undertaken extensive proprietary research of key developments and trends across M&A markets in North America and China. Through The 52 Institute™, we focus on developing a deeper understanding of the global economy for our clients. Our research team analyzes consequential trends affecting corporate decision-making, investment considerations and M&A strategies in North America and China.

As the proprietary research arm of 52 Capital Partners, LLC, The 52 Institute™ aims to provide senior management teams, Boards of Directors and Founders with key industry insights and facts on which to base management decisions. Our research combines an array of core disciplines, ranging from finance and economics to management and statistics. We serve our clients by fully leveraging our firm's intellectual capital and thought leadership at The 52 Institute™. We deliver timely perspectives to our clients on topics pertinent to important strategic challenges and issues faced by corporations, investment firms, founder-led enterprises and entrepreneurial ventures. The 52 Institute™ is a web-based ecosystem highlighting our independent, proprietary insights. We employ a repertoire of analytical tools, harnessing economic theory and managerial expertise. Our methodology at The 52 Institute™ allows us to examine key microeconomic industry trends to better discern broader macroeconomic trends impacting corporate decisions and strategies globally. Our proprietary research at The 52 Institute™ covers over two dozen industry verticals. 52 Capital Partners, LLC is a private partnership and funds all research undertaken at The 52 Institute™; it is not commissioned by any government, business or other institution.

For further information on The 52 Institute™, please visit us at: www.52capitalpartners.com/the-52-institute.

Collaboration with 52 Capital Partners, LLC

52 Capital Partners, LLS is an independent strategic advisory firm, deeply committed to assisting North American businesses achieve long-term success. Our principal goal is to function as our clients' most trusted boutique strategic advisor in connection with our clients' most consequential mergers and acquisitions and other strategic transactions. We bring unparalleled expertise to our clients across industries and functions. We work closely with management teams to drive winning M&A strategies, catalyze innovation and achieve successful transformation through accretive transactions in key markets.

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Preface

Quarterly Industry Insights

52 Capital Partners, LLC is committed to serving our clients by delivering timely research on key industry verticals. Our research team at The 52 Institute™ engages in proprietary research across industries to identify important trends and developments affecting businesses and their M&A strategies. While, as a firm, we are quintessentially boutique, the lens through which we assess opportunities for our clients is global and spans virtually all key industries internationally.

The *Quarterly Industry Insights* constitutes an important ongoing initiative at The 52 Institute™. Over the course of each calendar quarter, our research team at The 52 Institute™ conducts a wide-ranging analysis of important trends and developments across key industries.

For each *Quarterly Industry Insights* report, the research we undertake is both focused and rigorous. We harness best-in-class analytical tools and methodologies. We utilize data-driven quantitative models. We employ proprietary methods to generate insights that possess both analytical rigor and intellectual honesty. We focus especially on industries which are most directly immersed in cross-border M&A opportunities in North America and China and in the Asia-Pacific region, more generally.

Data, logic and integrity guide our every action in conducting research for the *Quarterly Industry Insights*. Following the completion of each calendar quarter, The 52 Institute™ releases the *Quarterly Industry Insights* report to our clients and to the broader public.

Our objective in producing the *Quarterly Industry Insights* is to assist our clients in assessing important trends and developments that have the potential of meaningfully impacting our clients' strategic decision-making and risk assessments of M&A opportunities in key international markets.

David P. Willard
52 Capital Partners, LLC
Founder & CEO

San Mateo, California
July 2019

Executive Summary

M&A Opportunities, Industry Consolidation and Robust Growth
Q2 2019 yielded compelling new opportunities for North American businesses and investment firms in China and the broader Asia-Pacific region. China sustained robust economic growth in Q2 2019 despite domestic policy measures aimed at reducing excessive leverage across the country's financial system. These measures have not resulted in material deflationary movement in China.

Elevated asset prices and tighter credit spreads generally sustain mergers and acquisitions activity in China. At the same time, domestic regulatory developments and adverse macro-political dislocations can reduce China's M&A volume, including both intra-China M&A transactions and cross-border M&A transactions possessing a commercial nexus to China. Heightened volatility in China's financial and capital markets—coupled with ongoing trade tensions between the United States and China—continue to contribute to uncertainty among North American multi-national companies and private investment firms with respect to consummating cross-border M&A transactions with a nexus to China.

While the contours of ongoing U.S.-China trade negotiations remain in flux, we believe a completed U.S.-China trade deal in Q3 2019 likely would both mitigate near-time downside risks to U.S.-China economic relations and increase appetite among market participants to engage in U.S.-China cross-border M&A deal-making during the remainder of CY 2019.

Q2 2019 M&A activity and investment trends in China reflect an apparent move in the direction of greater industry consolidation in China. Q2 2019 China M&A transactions materialized across major industry verticals in the region, particularly within consumer, food, healthcare, biotechnology, industrials, telecommunications and mining. Those M&A transactions generally reflected buyers' sustained appetite for attractively valued assets and businesses for which fewer regulatory impediments emerge in the China market.

China's domestic regulatory considerations remain a principal concern among China M&A participants with respect to implementing strategic corporate planning and effectuating M&A deal execution strategies. Q2 2019's notably active verticals within China M&A were industrials and chemicals. These industries remained the busiest in China. Sustained appetite for targets within industrials and chemicals also contributed to significant M&A activity in the Asia-Pacific region, more generally.

As part of its ambitious "Made in China 2025" initiative (中国制造2025年, *zhongguo zhizao 2025 nian*), the Chinese government has formally implemented a policy of committing resources and personnel in order to boost China's capabilities in 10 important industries: electric cars (电动汽车, *diandong qiche*), information technology (信息技术, *xinxi jishu*), artificial intelligence (人工智能, *rengong jineng*), agricultural technology (农业技术, *nongye jishu*), aerospace engineering (航空航天工程, *hangkong hangtian gongcheng*), new synthetic materials (新型合成材料, *xinxing hecheng cailiao*), biomedicine (生物医药, *shengwu yiyao*), advanced electrical equipment (先进电气设备, *xianjin dianqi shebei*), high-end rail infrastructure (高端铁路基础设施, *gaoduan tielujichu sheshi*) and high-tech maritime engineering (高科技海事工程, *gao keiji haishi gongcheng*).

China M&A transactions in Q2 2019 reflected this policy focus. Deals occurred across a broad range of industry verticals in Q2 2019, reflecting sustained M&A appetite across the Chinese economy, notwithstanding ongoing domestic regulatory risks and sustained volatility in capital markets stemming from continued U.S.-China trade tensions. Key verticals with notable China M&A transactions in Q2 2019 included consumer, food, healthcare, industrials, automotive, industrials, biotechnology, telecommunications and mining.

July 2019

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Opportunity Amidst Uncertainty

Elevated U.S.-China trade tensions may continue to hamper cross-border M&A activity within China during CY 2019. Given continued concerns around data privacy risk, foreign technology transfers and intellectual property risk in China, M&A activity in software and technology is likely more acutely exposed relative to other verticals for the remainder of CY 2019.

In the current market environment, cross-border M&A deal-making in China generally requires greater levels of patience and innovation with respect to both deal execution strategies and deal structuring.

However, a robust pipeline of M&A opportunities in China still abounds. The appetite to consummate M&A deals in China generally remains strong. Many North American private investment firms remain active in China. Private market valuations in China, particularly in non-technology verticals such as industrials, consumer and manufacturing, remain comparatively attractive. We observe a robust pipeline of strategic growth opportunities in China and the Asia-Pacific region.

Against this backdrop of sustained appetite for cross-border M&A with China, concerns among M&A participants linger with respect to heightened regulatory scrutiny of cross-border transactions involving China.

Concerns span both China's domestic regulatory environment and U.S. regulatory reviews of cross-border transactions that bear a probability of implicating U.S. national security, necessitating review by the Committee on Foreign Investment in the United States (CFIUS).

We believe Q3 2019 likely will yield comparable levels of Chinese buyers in the North American M&A market relative to levels observed in Q3 2018.

Bi-lateral tariffs and other defensive regulatory measures in the United States, as well as domestic capital controls in China, may continue to exert downward pressure on cross-border M&A activity from China-based buyers in the United States.

Notwithstanding near-term risks to cross-border M&A activity with China, an acceleration of market-oriented reforms to China's financial system and capital markets may yield greater opportunities for North American businesses in China in Q3 2019 and for the remainder of CY 2019.

The current macro environment reflects heightened levels of uncertainty with respect to the near-term prospects for U.S.-China economic relations.

An ongoing bi-lateral trade war persists in the wake of new tariffs and other protectionist policy measures. Economic sanctions proliferate. In addition, investment activity and cross border capital flows proceed with greater caution. Heightened volatility affects financial networks and capital markets in both countries, particularly in the wake of new tariffs levied.

Amidst this amalgam of uncertainties, now is the time for North American senior management teams and Boards of Directors to develop smart strategies in order to compete successfully and thrive in this "new normal" for U.S.-China economic relations and cross-border M&A opportunities with a nexus to China and the greater Asia-Pacific region. In the current environment in China and the Asia-Pacific region, we especially observe compelling M&A growth trends in several industry verticals: consumer, automotive, business services (especially digital payments technology), semiconductors and food.

Consumer

Compelling demographic trends in China and the Asia-Pacific region support robust long-term growth prospects for consumer businesses.

Relatively young populations in Southeast Asia continue to drive increased demand for consumer products. We expect this trend to continue during CY 2019 and into CY 2020.

In addition, policy shifts in China have relaxed restrictions linked to the country's long-standing "one-child" policy; this has increased the probability of greater population growth in China, particularly within the country's easternmost provinces that most directly benefit from the new policy measures.

General health awareness and a growing number of state-directed wellness programs in China are also creating greater incentives for multi-national consumer businesses to deploy more products and services into the country.

Finally, consumer businesses, while not completely immune from regulatory scrutiny in North America and China in an M&A setting, generally possess products and business models with characteristics that are less likely to implicate domestic capital control restrictions in China or sensitive considerations of national security. This bodes well for the industry's sustained outlook in China. Against this overall backdrop, we remain optimistic about the growth prospects for consumer businesses undertaking investments and M&A transactions in China and the Asia-Pacific region, more generally.

Among sub-sectors within consumer goods in China, we find especially compelling characteristics among North American businesses that produce athletic footwear for the China market. China is the largest and fastest-growing sportswear market worldwide. With a general increase of disposable income across key demographic segments in China, Chinese consumers are looking for new, sleek athletic wear.

E-commerce has become a platform for companies to establish a presence in China's rapidly-growing online marketplace for luxury goods, including athletic footwear with premium pricing. In terms of traditional offline sales, companies are still able to penetrate China's mainstream, expanding to in-store marketplaces. The country's growing consumer base and overall sports awareness together buttress the probability of greater M&A opportunities in China for North American athletic footwear companies.

We believe ripe opportunities exist for North American businesses to increase global market share by capitalizing on acquisitions of small- to medium-size athletic footwear business in China that offer compelling returns on invested capital.

Automotive

China's car market is the largest and most dynamic market world-wide, measured in terms of total number of vehicles and long-term demand growth rates.

The continued expansion of China's major metropolitan areas has fueled increased demand for automobiles. That demand has especially manifested itself in fast-growing sectors of autonomous vehicles, electric vehicles (EV), ride-sharing vehicles and related services and car rentals.

Among the array of compelling fundamentals within the car industry in China, the country's car market offers robust revenue growth prospects and comparatively attractive M&A valuations for North American multi-national corporations and investment firms.

We believe there is a strong probability that autonomous vehicles, buttressed by China's fast-expanding sector for, and investments in, artificial intelligence (AI) technologies, will gain the majority share of China's automotive market within the next five to ten years.

In addition, China continues to hold the world's largest and most advanced market for electric vehicles (EV). We observe emerging China EV players to present compelling opportunities for strategic acquisitions by larger North American players with ambitions in China and the broader Asia-Pacific. Outside of the EV market, opportunities with car-sharing businesses abound in China. The number of new car-sharing businesses in China has increased year-over-year by 160%, reflecting Chinese consumers' appetite for alternatives to conventional modes of transportation in China's cities. We observe a number of compelling M&A targets within the car-sharing segment as well as opportunities for potential strategic partnerships with larger institutional players. China's continued policy focus on the development of domestic energy alternatives, including solar and electric innovations applicable to the automotive industry, likely will continue to support the emergence of new EV players and robust M&A activity within the space.

Car rental companies in China also enjoy industry tailwinds, with ripe M&A opportunities emerging for enhancing market share in the country and tapping into growing demand driven by a more mobile population in terms of business travel and domestic tourism. Rapid urbanization in China continues to fuel greater domestic tourism among Chinese citizens, yielding the growth of car rental sites in and around China's major airports, train stations and seaports. Digital solutions in the form of growing online platforms also are allowing consumers in China to access more readily car rental services, strengthening the sector's growth prospects and the probability of increased strategic M&A activity and domestic consolidation among small- to medium-sized players.

Business Services

The digital economy increasingly defines the business services landscape in China. Growth within China's business services industry continues to be driven by advancements principally within the fast-growing mobile payments market in China.

The mobile payments market in China remains dominated by two main strategic players, WeChat and Alipay, which collectively hold over 90% of the country's market share. The broader Asia-Pacific region's digital payments sector also is growing rapidly, with large players and new start-ups vying for position within a highly dynamic and fast-evolving industry.

Particularly within Southeast Asia, we believe businesses will continue to benefit from robust consumer demand prospects within a region that is increasingly embracing online payments and digital wallets. Innovation-based enterprises in Southeast Asia have begun to create new mobile payment solutions, offering consumers greater options and attracting greater investment and strategic partnerships from foreign multi-national companies.

Large North American multi-national corporations have penetrated the Asia-Pacific region in terms of new operations, investment, services and joint-ventures; however, the mobile payments landscape, including ancillary business services enterprises that support the sector, remains extremely competitive, with a variety of companies vying to establish a market-leading position.

We believe M&A valuations among mobile payments businesses in China and the Asia-Pacific region are comparatively more attractive relative to valuations observed in industrialized economies in North America, Asia (ex-China), Europe and Latin America.

In addition to growth and M&A opportunities within the mobile payments market, we observe ripe opportunities for acquisitions of CRM businesses in China. China's growing user base presents expansion opportunities for customer portfolios of major multi-national companies with CRM-focused operations or strategic ambitions in China. Increased connectivity, including high-speed CRM connections operated on WeChat's premier Content Distribution Network, offers a greater number of opportunities for strategic scaling, enhanced marketing and customer acquisitions within China's robust CRM market.

Semiconductors

China and the Asia-Pacific region present a growing number of M&A opportunities for semiconductor businesses.

We observe that sustained appetite for new M&A activity in the region continues despite lingering concerns over licensing risks, intellectual property misappropriation risks, regulatory approval risks and data privacy considerations.

The semiconductor industry possesses strong growth prospects in the region, with Asian businesses capturing an additional 5.2% of global market share measured on the basis of year-over-year data.

Specialized mobile system-on-chip (SoC) producers reside in the lower-middle market in China. Many of these SoC producers possess private market valuations that make the companies prime targets for acquisition by strategic players or private equity firms. In addition, strategic partnerships with these SoC producers are an increasingly viable option in the absence of sufficient buyer appetite for wholesale buyout or integration. Tablet SoC producers maintain unique competitive positioning within China and the Asia-Pacific region, while personal computer SoCs likely will continue to benefit from at-home production trends and continued growth within the industry.

Food

China and the Asia-Pacific region present compelling opportunities for North American companies and investment firms to capture growth advantages in the region. Growing consumption among the region's middle class and consumers' more robust, health-focused appetites continue to drive higher growth prospects and revenue generation for food enterprises and ancillary service providers that support the industry.

Demographic trends and related data show an acceleration in the consumption of coffee, cocoa and cocoa-based products within China and the Asia-Pacific region. Coffee consumption in China is rapidly expanding, with consumer demand growing at an annualized rate of approximately 16%. This trend is further solidifying China's middle-class coffee culture. In addition, it offers an attractive array of M&A opportunities for North American multi-national companies and investment firms seeking outsized returns on invested capital.

With respect to cocoa companies, the Asia-Pacific region possesses a largely fragmented distribution channel. As a result, many strategic players may identify more compelling opportunities in expanding their cocoa portfolios through partnerships with, or acquisitions of, successful small-cap distributors with an established presence in desired target markets.

Finally, we observe that snack food and condiment companies likely will be able to capitalize on growth advantages in China due to the country's more discerning consumer base and health-conscious educational institutions. For snack food companies, penetration of local distribution channels remain the most viable go-to-market strategy for foreign firms. The same holds true for condiment companies. Expansion of snacking portfolios to healthy snack products represents a strategy that is well-positioned to capitalize on consumer purchasing trends in China. We observe growing demand for high-quality baby food in China due to the country's more health-conscious demographic and growing middle class.

Authors

David P. Willard
Founder & Chief Executive Officer

David P. Willard is the Founder & Chief Executive Officer of 52 Capital Partners, LLC. Mr. Willard is responsible for all major aspects of the firm's executive management, strategy, client development, investment process and thought leadership. He has executed and participated in consequential M&A transactions and other significant deals at firms in the United States, Europe and Asia, including Goldman, Sachs & Co. and Cravath, Swaine & Moore LLP, closing 53 transactions totaling over $150 billion in aggregate deal value. Fluent in Mandarin, Mr. Willard is among a select group of Western business leaders to recognize fully over two decades ago the significance of China's growing interconnectedness with the global economy.

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52 Capital Partners, LLC

Trust.

Integrity.

Partnership.

52 Capital Partners, LLC

Our Firm

52 Capital Partners, LLC is an independent advisory firm that provides strategic advisory services to the senior management teams, Founders and Boards of Directors of corporations, investment firms, family-owned enterprises and entrepreneurial ventures faced with transformational or complex transactions in North America and China. We harness our expertise on China matters and our breadth of experience in investment banking, mergers and acquisitions and principal investing to deliver high-impact, solutions-based advice on our clients' most consequential mergers and acquisitions and other strategic transactions in North America and China. We are headquartered in Silicon Valley.

Our advice will always be independent and discreet, and we act in the best interests of our clients at all times. We advise a broad range of leading multi-national corporations, investment firms, family-owned enterprises and entrepreneurial ventures. We are committed to serving our clients and executing accretive transactions to grow their businesses—enabling new innovations, fostering job creation and catalyzing earnings growth.

Our Philosophy

We provide excellence in client service, without regard to short-term profit. We communicate with our clients under strict privacy and confidentiality. We invest deeply in cultivating long-term relationships with our clients based on trust, integrity and partnership. We accept an engagement only when a client's values are aligned with ours and we believe our advice will yield meaningful value to our client's interests. We serve clients based in North America.

Mergers and Acquisitions

We possess a deep understanding of the many challenges faced by North American corporations, financial institutions, founder-led enterprises and entrepreneurs with respect to undertaking and navigating mergers and acquisitions in North America and China. We provide our clients with high-impact strategic advice on M&A transactions at all stages of a deal's life cycle. We are committed to serving our clients on engagements where our strategic China expertise, our international network and our resources can meaningfully advance our clients' interests in navigating the complexities of the cross-border M&A market with China.

Strategic Transactions
We advise our clients on a broad range of cross-border strategic transactions and investments in China and North America. We deliver strategic advice in connection with cross-border private investments in China and North America, as well as significant commercial transactions such as joint ventures, minority growth investments, venture capital investments, asset purchases and recapitalizations in China.

Private Equity Advisory
We advise North American private equity firms in connection with leveraged buyouts, minority growth investments, recapitalizations and portfolio companies' strategic expansion to markets in China and the Asia-Pacific region.

Intellectual Property Advisory
We advise North American management teams and Boards of Directors to mitigate their companies' intellectual property risk in China when they deploy new capital, products or services into China. Our clients' intellectual property portfolios and assets are indispensable to our clients' success in the marketplace. We advise our clients in connection with major licensing arrangements, royalty agreements, trademark matters, copyright issues, patent transactions and other significant intellectual property transactions in North America and China. We deliver solutions-based advice to our clients to ascertain intellectual property considerations at all stages of executing cross-border mergers and acquisitions and other major transactions in China.

Risk Management Advisory
We deliver high-impact strategic advice to our clients to assist them in effectuating risk management decisions in connection with mergers and acquisitions, strategic transactions, investments and other important strategic initiatives in North America and China.

Special Situations
We provide strategic business advice to multi-national corporations and investment firms in connection with special situations, including distressed mergers and acquisitions and other complex transactions.

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