HUAXING GROWTH CAPITAL

Market Review and Business Update: 2017 and 2018 Year-to-Date

OVERVIEW

Drivers of Investment Returns in China's Private Markets

At the Asian Venture Capital Journal's recent China Forum, limited partners and general partners homed in on several drivers of investment returns.

First, **clarity of focus** is essential in China's quickly evolving market. We believe the pace of change favors specialists who can spot nascent trends and future category leaders. We remain focused on China's 'new economy,' which has allowed us to consistently pick the ultimate winners in various tech subsectors. O*ur four investment committee members are supported by six sector leaders, which gives us both broad and deep coverage of new economy trends and businesses*.

Another imperative is **access to the best deals**. Huaxing Growth Capital stands out in this regard. Our network of new economy executives, investors and budding entrepreneurs provides us with access to the most competitive deals. *In 2017, we distilled thousands of potential investment cases into 25 deals*.

Value creation was another theme. GPs must be active owners and add value to their portfolio companies. Here too we enjoy unique strengths. Our sector focus and proprietary market research give us an unrivaled ability to advise companies on executive hiring, strategic planning, raising capital and reaching the next phase of their growth.

And finally, GPs need to be **prudent and flexible in finding exit opportunities**. There is growing liquidity in secondary markets. *Over half of the exits from our first USD fund were via secondary sales*. At the same time, we are closely tracking regulatory developments that could offer attractive public market exit opportunities in mainland China and Hong Kong.

Our 2018 Agenda

Huaxing Growth Capital plans to make larger initial investments and take a more active role in developing portfolio companies. We began 2018 having made progress against the plan and with an optimistic outlook based on three factors:

- *We have a clearly defined strategy*. We focus on growth-stage investments in China's technology, media and entertainment sectors. We apply a thematic overlay to guide us toward leaders within subcategories of those sectors.

- *The outlook for 2018 is strong*. Macro trends such as greater consumption, advances in artificial intelligence and the digitalization of manufacturing and offline industries are expanding the opportunity set for our strategy. Rapid innovation in both business models and technology as well as policy support further bolster tech sector prospects.

- *We are competitively positioned to capitalize on opportunities*. We have ample "dry powder" and an unrivaled deal pipeline informed by proprietary research and our historical proximity to China's entrepreneurial talent.

We believe our strategy is uniquely suited to capitalize on the rapid disruption in consumer and B2B verticals, internet "ecosystems" oriented around China's largest tech firms, and the vast scale at which innovations come to market. We look forward to providing future updates on our business and market views.

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BUSINESS HIGHLIGHTS

Highlights from 2017 and beginning of this year include:

- We completed **25 investments** worth **$350 million USD**, establishing 17 investments in new companies and making eight follow-on investments in existing portfolio companies. In addition, we were able to make **seven full or partial exits** through secondary sales.

- New investments included the artificial intelligence platform company **SenseTime**, the AI and Big Data enterprise software developer **MiningLamp Software** and the electric vehicle maker **NIO**. In addition, we executed on our property technology thesis by investing in **Ziroom**, an O2O apartment rental and service provider, and **Tujia**, the online platform for short-term rentals.

- Several portfolio companies held successful **initial public offerings**. Three took place in the United States (**Bilibili, LexinFintech** and **Jianpu Technology**), one in Hong Kong (**WuXi Biologics**) and two in China's A-shares market (**Longshine Technology** and **Qihu360**). The online consumer finance platform LexinFintech listed on the Nasdaq enjoyed a first-day trading rise of nearly 20%.

- We held a successful first closing of our **latest investment fund**, raising over 4 billion RMB.

- **Ke Wei** joined Huaxing Growth Capital as a partner and Investment Committee member. He joined from General Atlantic where he was a partner and led investments in consumer-oriented technology companies in China.

PURSUING A THEMATIC INVESTMENT STRATEGY

Huaxing Growth Capital pursues a thematic investing approach to uncover business models that will benefit from long-term trends in industry transformation, technology innovation, and rising standards of consumption and lifestyle amenities in China. We expand on our investment themes below.

Industry Transformation

Several structural factors of China's economy have created a vast scope as well as growing urgency for digitalization and other advanced technologies to improve the efficiency and productivity of the countries' assets.

Despite the headlines on the growth of services and consumption in China, the country's economy remains heavily industrialized with large fixed-asset investments that are aging and at risk of becoming less competitive globally. Implementation of automation is low. Many small and medium sized enterprises have yet to embrace internet technologies to improve operations. And logistics costs are nearly double the rates in other developed economies, when viewed as a proportion of gross domestic product.

What's more, demand for advanced industrial technologies will grow ever more acute because of the projected declines in China's working age population, rising labor costs, customized demands, and intensity of competition in many industries. Examples of our investments in this theme include Zhaogang, Meicai, Lianjia, NIO and CHJ Automotive.

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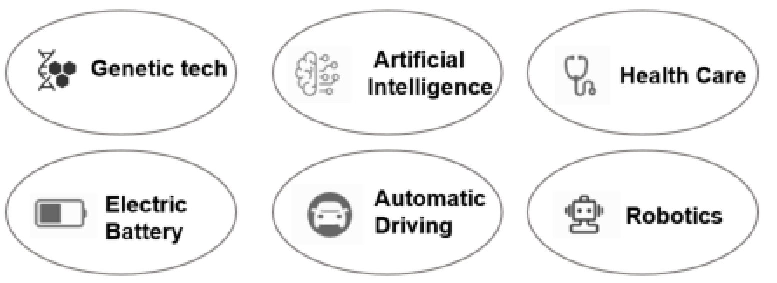
Structural factors of China's economy have created a vast scope as well as growing urgency for technologies to improve the efficiency and productivity of the country's major economic assets.

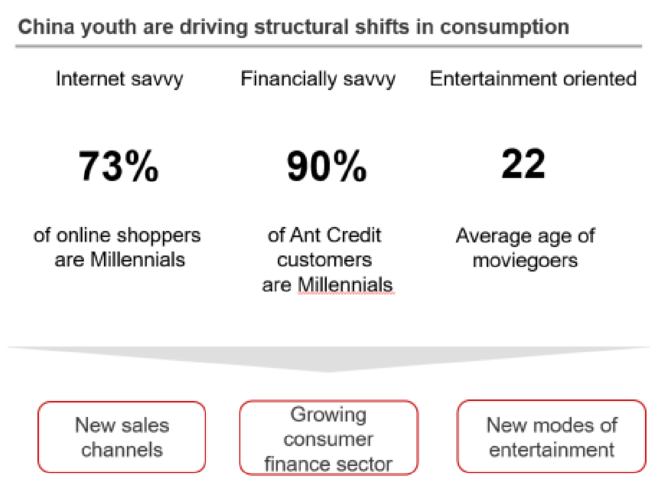
Technology Innovation

Driven by big data accumulation and a rapid rise of computing power, new information technologies are showing the potential to dramatically reshape industries from healthcare to transportation, and they require less time to commercialize. China has become a leading force in developing many advanced information technologies such as artificial intelligence thanks to the quick adoption of mobile and online services that provide location, transaction, online search, and other digital data to train machine learning systems and neural network on a scale that other countries cannot match.

Top 5 Sectors in New Tech Commercialization (MIT Tech Review)



Examples of our investments in this theme include SenseTime, MiningLamp Software and Netis Systems.



Consumption Upgrade

Technology will play a leading role in creating compelling products and services for China's emerging middle class as the next generation of consumers aspires to better lifestyle. The opportunity set in China is unlike typical emerging market consumption themes because of China's vast scale, aggressive consumer adoption of new technologies and continuing gains in aggregate income, particularly that of millennials.

As consumption patterns change, we seek investments in companies that use technology to offer unique, customized and higher quality products and services for leisure, gaming, education and the country's growing interest in personal health, among other areas. Additionally, we seek to capitalize on innovations in sales channels and the blending of online and offline customer engagement, as with the "new retail" concept. Examples of our investments in this theme include Meituan, Kuaishou, Zhangmen Education and JD Finance.

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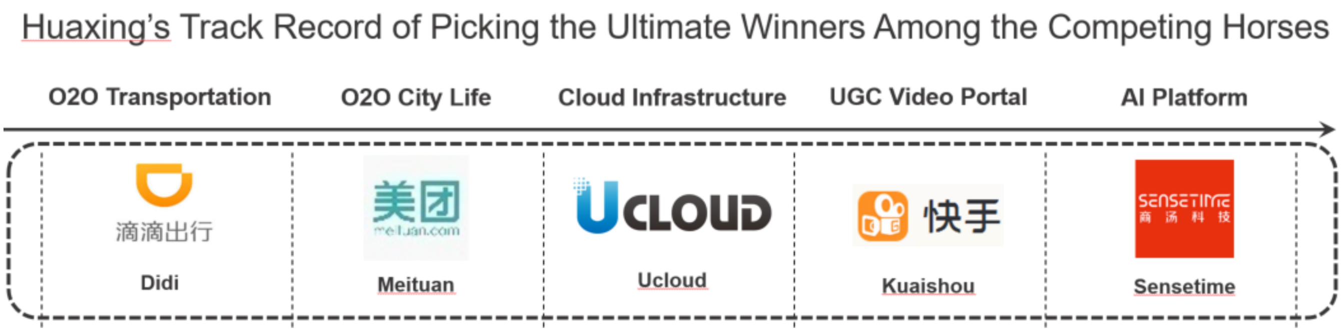
INVESTMENT EXECUTION

Below we describe how we execute the investment themes above.

Invest in sector leaders

As China's markets become more competitive, they can resemble a zero-sum game where gains disproportionately accrue to leaders until they are able to consolidate the market. We therefore believe it is crucial to identify companies with the greatest potential to emerge as sector leaders. This approach has led us into investments with China's most valuable companies, as shown in the graphic below.



Make larger investments. Lead or co-lead financing rounds.

Huaxing Growth Capital has evolved to a scale where it expects to make larger investments than in the past, in the range of $20 million to $70 million, often with an accompanying board seat, and to lead or co-lead a majority of the deals in which it participates.

Focus on growth-stage investments

This approach helps us to invest in companies before their growth reaches an inflection point beyond which the potential for outsized returns diminishes. Growth stage investments will continue to represent the majority of our investments.

Adding Value to Portfolio Companies

We look to make meaningful contributions to our portfolio companies' growth and development by arranging follow-on funding, assisting with staffing, providing strategic advice and plugging them into our global network of institutional investors, corporate venture capital arms and other entrepreneurs. Examples of our work with portfolio companies include:

- We advised the bike-sharing firm Mobike on strategic options and brought in Meituan as a strategic acquirer.
- We advised the ride hailing firm Didi Chuxing on its industry consolidation strategy and merger with Kuaidi, and later advised management on its relationships with Tencent and Alibaba.
- We helped the online video platform Kauishou analyze industry dynamics and the competitive landscape. We subsequently worked with the company to recruit Tencent as a strategic investor.
- We helped the consumer finance company LexinFintech raise capital from a large strategic investor and a large insurer, and later advised the company on its IPO plans.

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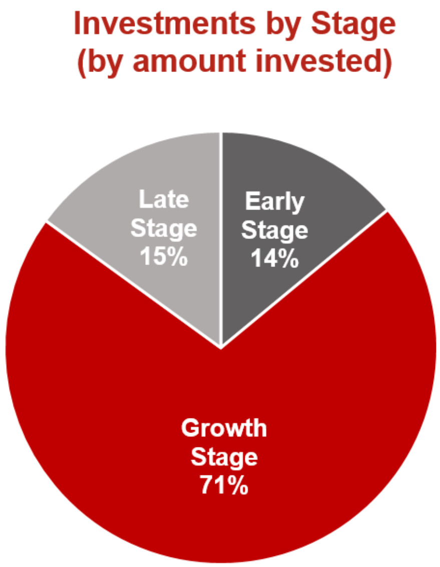
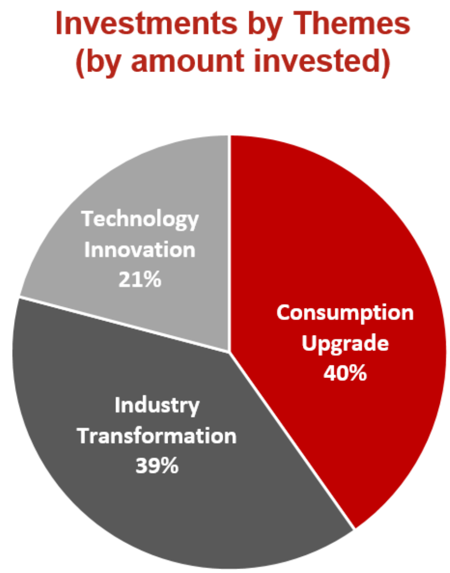
PORTFOLIO SNAPSHOT

Today, our total assets under management across RMB and USD funds is the equivalent of approximately $3 billion. The charts below show the development stages and the themes that we have invested.





Some of our top performing portfolio companies include Didi Chuxing, Lianjia, Meituan Dianping and SenseTime.

A Note on Valuations

Valuations have been a source of concern among investors over the past 24 months as China's private markets have continued to see inflows of capital. We are conscious of these concerns and the effect on valuations as greater amounts of capital come into the market. We maintain highly selective investment critria, constantly stress-test our assumptions, and invest where we have a high degree of conviction that the valuation appropriately reflects a company's growth trajectory.

An under-appreciated factor in assessing Chinese tech startup valuations is the need for them to "own their market." Market share gains often feed on themselves and the economics disproportionately accrue to leaders who benefit not just from network effects, but also by aligning with China's Baidu-Alibaba-Tencent internet ecosystems that are gateways to vast swaths of digitally active consumers.

Emerging leaders in consumer-oriented subsectors such as video streaming or online property listings can quickly amass dominant positions and push smaller players to the fringes. Staying "small but beautiful" as a niche player can be a fraught business strategy in China's fast-evolving new economy. As a result, sector leadership often justifies what might seem like a valuation premium to the uninitiated investor.

We believe that our portfolio companies are appropriately valued, if not conservatively valued, relative to their growth prospects and the dynamics of the markets in which they operate.

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MARKET OPPORTUNITIES

Several areas appear ripe for investments in the year ahead. Following our thematic investment strategy, we see strong investment opportunities in *consumer services*, *traditional industries with low internet penetration rates* and *enterprise services*. Below we expand on our views in these categories.

Consumer Services

We see a growing opportunity in upgrades to services in retail, education, healthcare, personal finance and entertainment. For example, there are attractive innovations that can help retail oriented firms develop niche brands and provide more cost-effective and personalized services. In addition, we are closely monitoring opportunities to invest in innovations that can improve user experience by decentralizing sales to make purchases more convenient, whether online or in brick-and-mortar locations. Also, we see great potential in the growing trend of 'socialized e-commerce' where social media platforms play an important role in purchasing decision-making and can increase customer stickiness and lifetime value.

Traditional Industries with Low Internet Penetration

Unlike the consumer sector, many traditional industries such as textiles, agriculture, logistics and maintenance, repair and operations (MRO) businesses have not yet embraced internet technology. Our research shows that internet penetration in these industries is extremely low (below 3%). This represents a huge potential for operational efficiency improvements. We have already begun to invest according to this thesis, with companies like Meicai and Zhaogang. However, we believe there is still an ample opportunity set.

Specifically, we are paying close attention to technologies that can shorten the supply chains and reduce related costs. In addition, many traditional industries that are fragmented and lack uniform standards for the quality and characteristics of products stand to benefit from adoption of internet and information-based technologies.

Enterprise Services Through Advanced Technology

We have a general view that enterprise services and technologies represent a significant growth opportunity in China. There are several reasons for this view. First, much of the innovation in China has favored consumer-oriented businesses, which is reflected in our portfolio. Approximately 80% of our investments have centered on consumer applications. Second, unlike Western markets with established enterprise software companies, China currently has no dominant players in the sector. This presents an opportunity given the amount of development and genuine innovation in areas like artificial intelligence and deep learning that are taking place in China.

We continue to see opportunities in commercial applications of big data analytics and AI, in particular for robotics, speech recognition, anti-fraud and risk management, enterprise security and data center operations. In addition, we see potential opportunities in blockchain applications and semiconductor development. As these opportunities come to fruition, we expect enterprise and B2B investments to occupy a much more significant portion of our portfolio.

Corporate Spinoffs

Aside from the structural and tech-driven investment themes above, we are seeing opportunities in the growing number of spinoffs of businesses from China's large corporations. Many firms, especially in the tech sector, have incubated and developed large-scale operations to serve their core business. As these projects mature, they are becoming candidates for outside investment. Examples of this trend that have provided investment opportunities for Huaxing Growth Capital include the spinoff of JD Finance from the e-commerce giant JD.com.

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