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Q & A

Asia Alternative's Ma on New Fund, Distributions From Chinese Growth Portfolio

Melissa Ma, cofounder of fund-of-funds manager Asia Alternatives LLC, spoke with Sabrina Willmer about how the firm raised $908 million for its third fund of funds, beating its $800 million target. Ma also discussed where the fund's money will go and where the firm has seen a slowdown in distributions.

Q: How did you beat your target in a fundraising environment that has been especially tough on funds of funds?

A: Our strategy in Asia and value-add to our LPs helped. The firm was founded in 2006 on the premise that the best way to make money in Asia is to invest in local companies, private companies and companies focused on domestic consumption – private small to mid-size companies making goods and products for Chinese consumers. The same thing applies to Japan and Korea. If you start with the premise that these are local backyard businesses, then you have to be local yourself and partner with local managers. The only way to be local is to be on the ground working with people who have invested for a while in local markets. This approach has come to fruition.

Q: How have you become local?

A: First of all, today our team is 29 people, to be over 30 by end of year. We have built a team to be a mini-United Nations of Asia. We started with offices in Hong Kong and Beijing in 2006. At the beginning of this year, we opened another office in Shanghai. As a testament to our desire to be seen as local, in September of last year, the Shanghai government awarded our firm a qualified foreign limited partner license. We were the first investor to have ever received the license. With that license, we can apply for a quota that allows us to convert up to a certain amount of dollars to RMB.

Q: How much will you convert?

A: We can't make public the amount we will make for the initial quota. We do expect to have RMB investments in Fund III. It will still be a small minority portion of the fund because that market is still very young. We think it is very important because we think that some of the future talent in private equity may come from RMB funds. These investments will be qualified, meaning that there are still certain sectors we can't invest in as a foreigner.

Q: What is your investment criteria?

A: We take a risk-adjusted return approach. We don't do top-down targets but more of a bottom-up process where we underwrite market segments. Portfolio construction will change quarter by quarter.

Q: How open are you to new managers?

A: We already have quite a number of new managers. Most of our capital is going with existing managers.

Q: Do you have criteria for fund size?

A: The fund sizes we target vary greatly because as a fund of funds we are trying to create diversification. We will invest in everything from early stage VC where we do the first institutional A round capital all of the way up to buyouts. What matters is whether or not fund size is appropriate for that strategy and the resources of the firm.

Q: Where do you see the best investment opportunities at the moment?

A: It looks like Fund III will be predominately North Asia, which means Greater China, Japan and Korea. These countries are where we have some of the most experienced managers and have seen better cash returns to investors over the past few cycles. A decent portion of capital will go to small and midmarket buyouts and growth capital. Almost all of our managers are domestic independent GPs.

Q: What terms are most important to you?

A: The most important terms are the ones that directly align my interests with the GPs. The rubber really hits the road when it comes to the legals. At the end of the day it is a relationship business. It is a package of terms that gives you a net effect of alignment so we are not prescriptive on any one term. Of course we pay attention to fee structure and waterfall mechanics. I can't emphasize how much the waterfall can change your returns. Key-man and no-fault divorce clauses are also a focus.

Q: Some limited partners have expressed concern about lack of distributions out of Asia fund of funds. How have distributions been from your managers?

A: We have had a steady flow of cash distributions coming back and expect that to continue for Fund I and II. What we have seen over the last few quarters is a slowdown in distributions from the China growth portfolio. The public markets are still the predominant exit mechanism there. The Chinese stock market is trading at historic lows where companies are growing at 20 percent to 30 percent but they are trading at the teen level. As a result, companies are choosing not to IPO and shares are not being taken off of the table for companies that are public. Where we have seen a slowdown in distributions it has been due to the volatility of the stock market. That has been experienced over the last three quarters in China and India. Again I don't lose sleep over it because companies are fundamentally strong. Chinese consumption has held up pretty steadily.

AT A GLANCE

Hometown: Oxford, Miss.

Education: Harvard University, Harvard Business School

Professional Background: Hellman & Friedman, McKinsey, Goldman Sachs

Hobbies: Movies, Cooking, Swimming, doing anything silly with my son

Favorite restaurant: Ye Shanghai