

## ***FSDC Industry Exchange Series***

# **Fuelling Startup Success: Attracting and Cultivating Homebased Alternative Investment Funds**

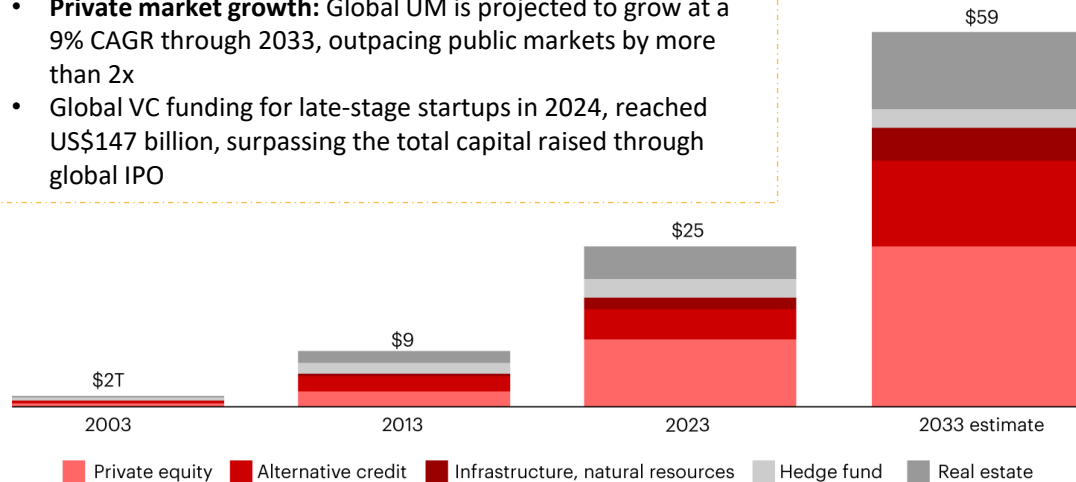
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# Fully integrating into the asset and wealth management proposition to catalyse a scalable innovation economy

## Private markets: fueling growth and late-stage funding

Global AUM of alternative investments (US\$ trillion)

- **Private market growth:** Global UM is projected to grow at a 9% CAGR through 2033, outpacing public markets by more than 2x
- Global VC funding for late-stage startups in 2024, reached US\$147 billion, surpassing the total capital raised through global IPO



Sources: Bain analysis

- **Rise of Alternative Investments:** Venture capital (VC), private equity (PE), and private credit (PC) are increasingly vital in shaping the AWM landscape, enabling family offices and ultra-high-net-worth individuals to diversify risk and create long-term value.
- **Hong Kong's Competitiveness:** Align with global financial trends by leveraging its strong public markets and expanding its offerings in alternative investment strategies
- **Hong Kong's AWM Sector Strength:** Manages over HKD 31.1 trillion (USD 4.0 trillion) in assets, with 65% from international sources, positioning the city as a key gateway for channelling capital into high-growth sectors and connecting global investors with regional opportunities

## The strategic value of startups and innovation

**Economic impact:** In 2023, global startup ecosystems were estimated to have created US\$ 7.6 trillion in value

- Private markets (PE, VC, PC) fuel growth by offering bespoke, risk-tolerant capital tailored to startups' needs at different stages:
  - PE & VC – powering startup growth and providing mentorship and professional networks
  - PC – catalysts of market efficiency and funding businesses beyond traditional banking (funded US\$333 bn globally in 2022)



**Catalysts for change:** Startups drive innovation, address societal challenges, and transform industries. Key sector trends include:

- **Healthtech and biotech** thrived during COVID-19 with telehealth platforms and vaccines
- **Greentech** startups gained momentum due to global sustainability demands, with late-stage cleantech startups raising 2.5x more funds in 2023 vs. 2020
- **Generative AI** startups accounted for 18% of global VC funding in 2023

### Hong Kong's role:

- Aim to develop into an innovation and technology hub, where financing is a critical component
- Hong Kong has an emerging ecosystem valued at USD 59 billion, with the highest number of unicorns among such ecosystems in the past decade, yet the city falls short of ranking as one of the global top 40 ecosystems

### Key challenges facing the startup and alternative investment ecosystems in Hong Kong:

- **Funding landscape imbalance** and diversification needs in the startup scene
- **Commercialisation** for startups and its implications for the broader ecosystem
- **Regulatory challenges**
- **Nurturing, retaining, and attracting talent** for fostering innovation



# Summary of proposed policy recommendations

## A modern approach to cultivating 'homebased' startups and funds, and a global ecosystem

- The concept must **evolve beyond traditional geographic boundaries** to reflect the realities of **global innovation and investment**
- **Startups** - hiring local talent, running research and development in the city, teaming up with regional businesses. In addition to cultivating local startups, reinforcing Hong Kong as a unique platform for international and Mainland startups seeking regional or global expansion
- **Investment funds** - recognise the role of foreign and international funds that establish their operations in the city to manage activities across the region/ commit to significant economic contributions
  - *E.g. establishing fund management offices, investing in local startups, and strengthening the financial ecosystem*

As private markets continue to evolve, a well-balanced ecosystem, featuring a diverse set of financial products across asset classes and a clear understanding of their inherent dynamics, is essential for navigating their potential

### I. Instilling stakeholder confidence through higher certainty

- **Recommendation 1:** A strategic and forward-looking policy vision to promote Hong Kong as a global hub for startups and alternative investment funds

### II. A robust foundation for alternative investments

- **Recommendation 2:** Introducing tailored regulatory regime for PE, VC, and PC
- **Recommendation 3:** Modernising tax and regulatory frameworks to support alternative investments

### III. Accelerating growth through innovation, expanding participation and ensuring long-term societal benefits

- **Recommendation 4:** Optimising public funds – driving growth in PE, VC, and PC
- **Recommendation 5:** Driving innovation growth through reimagined funding and technology transfer
- **Recommendation 6:** Diversifying through the inclusion of specific alternative investment options in the MPF scheme

# Proposed recommendations

## Instilling stakeholder confidence through higher certainty

### *1. A strategic and forward-looking policy vision to promote Hong Kong as a global hub for alternative investment funds*

- **Strategic vision/ call to action:**
  - Position Hong Kong as a global leader by leveraging financial strengths and connectivity to Asian markets
  - Provide a unified framework that could incorporate subsequent recommendations
  - Clearly articulating Hong Kong's long-term commitment to lead in innovation and entrepreneurship
- **Core pillars/ messages:**
  - Position Hong Kong as a regional and international VC/ alternative investment funds hub to strengthen its role as a leading AWM hub
  - Foster an innovation-driven and risk-taking culture among local
  - Encourage a mentality focused on addressing global challenges and demands to foster a more outward-looking, internationally competitive innovation ecosystem
  - Attract global talent and innovation
  - Capitalise on Hong Kong's global connectivity



# Proposed recommendations (cont'd)

## A robust foundation for alternative investments

### 2. Tailored regulatory regime for PE, VC and PC

- **Explore the potential of a tailored licensing regime tailored for PE, VC, and PC firms to enhance operational efficiency**
  - Benchmarking other foreign examples, as a complementary pathway, while allowing firms well-served by the existing SFO framework to continue without disruption
- **PE/VC – focus on long-term strategic investments in private companies, prioritising value creation**
  - Current SFO framework requires Type 1, 4 and 9 licenses
  - Definition of “securities” includes shares and debentures of non-Hong Kong private companies but excludes those of Hong Kong-incorporated private companies, causing complexity for firms with global portfolios
- **PC – specialised activities like direct lending, distressed debt management fall outside SFO scope**; currently required type 9 license is designed for a securities portfolio
- **Key Benefits:** Streamline compliance for PE, VC, and PC firms by addressing their unique risk models and reducing regulatory burdens (e.g. exemptions to be granted for VC fund managers with specific conditions met)

### 3. Modernising tax and regulatory frameworks to support alternative investments

- **Refine tax treatment for co-investment structures**
  - Adjust the threshold to “more than 50%”, allowing SPEs with a majority interest held by tax-exempt funds to qualify for full tax exemption
- **Expand the Unified Fund Exemption regime to include single-investor funds/ fund-of-one**
  - Recognise single-investor funds for tax purposes would provide fund managers with the ability to design bespoke solutions
- **Promote and strengthen the appeal of Hong Kong-domiciled fund vehicles**
  - OFC and LPF
  - Provide further incentives for fund managers

# Proposed recommendations (cont'd)

## Accelerating growth through innovation, expanding participation and ensuring long-term societal benefits

### 4. *Optimising public funds – driving growth in PE, VC, and PC*

- **Strategic use of public funds:** Adopt a **dual-track approach** by committing public funds as cornerstone investors in PE/VC and leveraging co-investments to drive PC market growth, addressing critical funding gaps and fostering innovation
- **Align investments with strategic goals:** Link public funding to **Hong Kong's economic priorities** by supporting local businesses, attracting world-class fund managers, and focusing on key areas to enhance long-term competitiveness
  - **A clear commitment to advancing the city's economic development**, such as establishing or expanding regional headquarters in HK, investing in local companies and startups, and nurturing local talent in key sectors.

### 5. *Driving innovation growth through reimagined funding and technology transfer*

- **Reimagine funding mechanisms:** Introduce a three-pronged funding strategy focusing on R&D, testing/certification, and adoption incentives to help start-ups bridge the gap between research and commercialisation, driving innovation growth and private investment
- **Strengthen Technology Transfer Offices (TTOs) at universities:** Enhance TTO operations by integrating external expertise, fostering global collaborations, and adopting market-driven strategies to improve the commercialisation of academic research and scale innovations effectively
- **Sector-specific strategies for innovation and global impact:** adopt sector-specific strategies that channel funding and technology deployment into high-growth industries, **biopharmaceuticals being one such example.**

### 6. *Diversifying through the inclusion of specific alternative investment options in the MPF scheme*

- **Enhance MPF investment options:** Building on the current consideration of listed private equity funds, the MPF's investment options could be prudently expanded to include select alternative assets. Over time, carefully exploring additional asset classes such as private credit may further enhance portfolio diversification



Thank you!