

Purpose of the China Private Securities Investment Fund Operations Whitepaper

Through interviews and due diligence with hundreds of domestic private securities investment fund managers and fund service institutions of different sizes, histories and investment strategies, and comparisons to international best practices, the "China Private Securities Investment Fund Operation White Paper" aims to show the current operating status of domestic private securities investment funds and the gap between international best practices. Suggestions on improving fund operations are put forward for reference by fund managers and fund service providers.

Compared with developed countries, China's private securities fund industry has a much shorter history and is under-developed, as shown by its unrefined management practices and retail-heavy investor base. These can lead to risk of malpractice and investment fraud due to minimum or no disclosure of fund operations information by managers, investment fluctuations due to irrational capital inflow and outflow, dominant role of fund distributors in charging high fees without providing compatible services and increasing investor complaints due to unexpected investment under-performance. When evaluating a fund or manager, investors scrutinize the funds' past performance, but tend to neglect the manager's operational capabilities. Only when managers strive to build a compliant and efficient fund operation environment and mitigate operational risks, can the previously mentioned issues be addressed and a healthy private fund sector that truly reflects its investment value be created.

The target audiences of the whitepaper are domestic private fund managers who want to improve their operational risk management capacity and to manage challenges and complications, domestic and foreign institutional investors who want to be better informed and prepared for more thorough manager due diligence process. In addition, the whitepaper also aims to provide valuable insights to asset servicing companies to improve their product offerings.

The paper is organized as follows:

- **Section 1** explains the purpose of this paper, which is to help the industry bring up its overall operation level, and mitigate operational risks for developing a healthy industry.
- **Section 2** reviews the development history of China's private securities investment fund industry and analyzes the allocation value of private securities fund investment.
- **Section 3** reviews the brief history and evolution of the foreign hedge fund industry and illustrates how hedge fund has become an important tool for asset allocation.
- **Section 4** elaborates the importance of operational risk management within private investment funds.
- **Section 5** analyzes the life cycle of China's private investment funds and the operational practice within private fund management.
- **Section 6** compares domestic fund operational practices against international best practices and proposes suggestions for improvement and institutionalization.
- **Section 7** provides recommendations on how to conduct due diligence of China's private investment funds more effectively to avoid investment losses due to operational risks.
- **Section 8** concludes with a summary of our findings and the direction of future efforts.