

**For discussion
on 17 December 2024**

**Legislative Council
Panel on Commerce, Industry, Innovation and Technology**

Innovation and Technology Industry-Oriented Fund

Purpose

This paper seeks Members' views on the proposal for setting up a \$10 billion Innovation and Technology Industry-Oriented Fund (ITIF).

Background

2. In order to develop innovation and technology (I&T) industries, the Government has all along attached great importance to enhancing support for I&T start-ups and accelerating the transformation of research and development (R&D) outcomes, while facilitating the upgrading and transformation of traditional industries through I&T, developing emerging industries and formulating plans for future industries, thereby promoting new industrialisation and generating new quality productive forces.

3. The current-term Government is committed to adopting an industry-oriented approach and has, on that basis, formulated and implemented a series of policies and measures to deepen collaboration among the Government, industry, academia and research sectors, so as to promote the development of I&T industries and new industrialisation, and construct a new real economy. For instance, the Government launched the \$10 billion Research, Academic and Industry Sectors One-plus Scheme last year, which aimed to unleash the potential of local universities in the transformation and commercialisation of R&D outcomes, and facilitate relevant collaboration among the Government, universities and industries. This year, we have also launched the \$10 billion New Industrialisation Acceleration Scheme, which aims to provide funding support for enterprises engaging in industries of strategic importance (i.e. life and health technology, artificial intelligence (AI) and data science, and advanced manufacturing and new energy technologies) to set up new smart production facilities in Hong Kong.

4. Despite the above, the long-term development of I&T industries, particularly in relation to the promotion of the transformation and industrialisation of R&D outcomes, requires substantial capital investment, a need that can hardly be met solely by Government contribution. It is thus necessary to leverage the support of market capital. Reference may be made to the successful experiences of Mainland authorities, e.g. ministries and commissions such as the National Development and Reform Commission, the Ministry of Science and Technology and the Ministry of Industry and Information Technology, which have all set up industry-oriented funds to give play to the guiding and leveraging roles of government funding, in order to channel more social capital to invest in industries and support the development of emerging and future industries. Moreover, our country is, at present, proactively encouraging the development of “patient capital” to support industry development. In general, industry-oriented funds not only take into account financial returns, but also the contributions of long-term investment to the local economy and society, as reflected by their dovetailing with the government’s industrial policy, attracting quality enterprises to set up footholds, developing industries and industry chains, fostering the development of ancillary industries, promoting economic and employment growth and so on. According to the Zero2IPO Research, a Mainland research institute on equity investment, an aggregate of 2 086 government guidance funds had been set up in the Mainland as at 2023, with a target size of about RMB 12.19 trillion and a commitment size of about RMB 7.13 trillion.

Proposal

5. To dovetail with the national strategy of developing “patient capital”, the HKSAR Government will revamp our approach in I&T industries investment, and draw on the successful experiences of the industry-oriented funds in the Mainland, in a bid to introduce an industry-oriented fund in Hong Kong that is tailored to local conditions, and in turn further promote the effective collaboration among the Government, industry, academic, research and investment sectors. The key to setting up the said industry-oriented fund is to specify the respective roles of the Government and the market, and continue to adhere to market-oriented operation. In particular, the Government needs to put in place an investment framework, specify the industries to be focused on, and formulate the rules and procedures for the selection of professional management institutions (“fund managers”), so as to create a conducive environment and conditions for the active participation of the investment sector. We hope that market forces can be fully harnessed to support the growth of “patient capital” and scale up investment with the focus placed on specified industries of strategic importance, thereby promoting the sustainable development of I&T and new industrialisation-

related industries in Hong Kong to showcase the principle of “a capable government and an efficient market”.

6. The Chief Executive announced in the 2024 Policy Address that the Government would set up a \$10 billion ITIF to form a fund-of-funds to channel more market capital to invest in specified emerging and future industries of strategic importance, with a view to building up the I&T ecosystem in a systematic manner.

Fund Structure

7. The ITIF, to be set up under the Innovation and Technology Fund (ITF), aims to cover the following five thematic areas, namely (i) life and health technology; (ii) AI and robotics; (iii) semi-conductors and smart devices; (iv) digitalisation, upgrading and transformation; and (v) future and sustainable development. According to the current plan, one or more sub-fund(s) will be set up under each area. The Government will participate as a Limited Partner (LP) of the sub-funds and make contributions to each. Taking into account that the ITIF will operate in a market-oriented manner, we will flexibly adjust the number and final size of the sub-funds subject to the actual market response and development of the industries. That said, the total amount of contribution of the Government will not exceed \$10 billion.

8. As for the management of the sub-funds, fund managers selected through an open application will become General Partners (GPs) of the sub-funds and shall be responsible for setting up the sub-funds in the thematic areas in the form of a limited partnership fund. They shall also raise market capital (including from strategic investors and others) for the sub-funds, manage the daily operation of the sub-funds, as well as invest in suitable projects in accordance with the investment framework.

9. In order to proactively guide market capital to participate, the Government will introduce to investment institutions or investors the vision and investment framework of the ITIF, solicit their investment tendencies, and to encourage them to grasp opportunities to invest in Hong Kong I&T industries. The Government hopes that the sub-funds under each thematic area will attract a group of potential “strategic investors” to commit a certain amount of capital and become LPs of the sub-funds, so as to enhance the effectiveness of the scheme.

10. The Government hopes that through the fundraising ability of the fund managers and the participation of strategic investors, the overall fund size of the sub-funds under the ITIF will reach at least \$40 billion. In other words, the capital committed by the market will be at least triple of that of the Government.

11. The Government will, in accordance with the Companies Ordinance, establish special purpose vehicle(s) (“SPV”) for the operation of the ITIF. The SPV will disburse investment funds under the ITIF and receive proceeds following the disposal of relevant investments. The proposed fund structure is at Annex.

Market funding and fund management

12. To more effectively manifest the guiding and leveraging roles of the fund, the participation of strategic investors and professional fund managers is of great importance. The Government intends for investment institutions or investors with credibility, financial resources, a willingness to invest and legitimate funding sources to resoundingly respond to fundraising for the sub-funds, and, as LPs, contribute a certain amount to one or multiple sub-funds. Strategic investors and other market investors will participate in sub-funds as LPs, and all relevant parties must adhere to the various regulations that the Government stipulates with regard to the ITIF, including the management structure, funding arrangement, operation of the sub-funds in different aspects and so on, in order to protect the Government’s interests.

13. As for the professional fund managers of the sub-funds, they are, on the one hand, responsible for raising market capital, and, on the other hand, charged to closely adhere to the objectives of the industry fund in choosing projects conducive to building up I&T industry chains in Hong Kong. To this end, the Government will formulate stringent selection procedures and requirements, ranging from professional qualifications and fund management experience, to past instances of successful fundraising and availability of potential investments etc., with a view to choosing qualified and capable institutions to manage the sub-funds. Meanwhile, we will also formulate arrangements that correlate with the operation and reasonable expectations of the market in areas such as injection of funds, management fees for fund managers, investment requirements, investment and exit periods, etc., in order to create favourable conditions that entice the proactive participation of the market.

Investment Targets

14. The ITIF’s investment portfolio will focus on five thematic areas, namely, life and health technology; AI and robotics; semi-conductors and smart devices; digitalisation, upgrading and transformation; and future and sustainable development.

15. The ITIF will channel more social capital to invest in I&T companies of high potential and at the growth stage, so as to achieve the target of making early

investment in small businesses and hardcore technology. Besides, the ITIF will, through diversified investment projects, and by investing in industry chain leaders or top-notch enterprises, as well as enterprises at different stages of development, facilitate I&T industry development in Hong Kong. Efforts will also be made to attract enterprises based on the practical situation to complement and strengthen the targeted industry chains, and promote co-operation between enterprises at various nodes of the industry chains, with a view to developing industry chains equipped with Hong Kong's competitive edge.

Investment Framework

16. With a focus on industry development, the ITIF will be industry-centric and will be implemented with reference to market practice. To ensure that funds will be allocated to projects that can practically drive industry development, the Government will formulate investment requirements to facilitate fund managers to, in accordance with the investment framework, make and execute investment decisions from a professional investment angle. LPs will not participate in the day-to-day management of sub-funds.

17. Apart from setting up thematic areas for the sub-funds to focus on various strategic industries, we preliminarily suggest stipulating the following investment requirements for each fund manager of the sub-funds:

- (i) 100% of the fund size must be invested in companies related to Hong Kong's I&T and new industrialisation-related industries as well as their industry chains;
- (ii) At least 50% of the fund size must be invested in Hong Kong companies, or non-Hong Kong companies which will set up their headquarters or regional headquarters in Hong Kong, or non-Hong Kong companies which will set up key segments (e.g. international R&D centres) in industry chains related to I&T or new industrialisation in Hong Kong; and
- (iii) At least 30% of the fund size must be allocated for the establishment and operation of production and manufacturing bases in Hong Kong, covering pilot production lines, testing procedures, etc.

18. The ITIF may invest in enterprises of various scales and stages of development. The duration of each sub-fund is preliminarily set at a maximum of 12 years (including extension periods), with an investment period of up to six years. The fund may not be used in investing in listed shares and investments

relating to cryptocurrency, gambling or real estate business.

19. We must emphasise that the ITIF will be based on market-oriented operation. Accordingly, the Government will, on the premise of preserving the Government's and the public's interest, maintain flexibility in formulating and adjusting relevant details, so as to take into full account market conditions, and aim to, through highly effective cooperation among the Government, industry, academia, research and investment sectors, implement the proposal so as to drive the development of I&T and new industrialisation-related industries.

Expected Benefits

20. The proposed \$10 billion ITIF is expected to commence its investments progressively from 2026-27 and attract market capital of about \$30 billion to invest in targeted industries. Having regard to relevant experience of the Mainland and other regions, our vision is to leverage on the guiding effect of the ITIF to entice a variety of market capital other than the ITIF to actively invest in I&T industries through different forms of investment, thereby bringing the overall industry investment size to \$100 billion in the coming decade.

21. In addition, benefiting from the market-oriented operation, investment projects screened and participated by sub-fund managers should be able to yield certain financial returns. From a macro perspective, the proposal will facilitate the growth of "patient capital" in Hong Kong, which will help attract quality enterprises to set up footholds in Hong Kong, nurture I&T enterprises, develop industry chains equipped with Hong Kong's competitive edge, and promote the thriving development of targeted industries. In the long run, industry development will increase tax revenue, enhance employment, and drive the development of ancillary industries. All these are conducive to the diversification of Hong Kong's economy, and will bring about more opportunities for the local financial market and support our continuous development as an international financial centre.

Monitoring and Review Mechanism

22. We will set up a Steering Committee for the ITIF ("Steering Committee"), comprising representatives from the commercial, I&T and investment sectors as well as the Government's relevant representatives, to advise on the operation of the ITIF, its fund management, investment targets, investment framework, selection of fund managers, monitoring and review matters, etc. Members are required to declare their personal interest when voting at the Steering Committee

meetings. In the event that the matter on which voting is required relates to a particular member or the organisation to which the member belongs, the member concerned should refrain from voting.

23. We will review regularly the operation of the ITIF to ensure that funding is properly disbursed and spent, and seek advice from the Steering Committee where appropriate. We will also put in place proper monitoring and review mechanisms, for example, a limited partnership agreement, which sets out the responsibilities and obligations of the sub-fund managers, shall be signed between the Government (through SPV) and the sub-fund managers and all other investors. The limited partnership agreement will incorporate proper terms and conditions to protect the interest of all investors (including the Government). Fund managers shall decide on the suitable investment projects, and submit regular management reports to the Steering Committee for monitoring purposes.

Next Steps

24. Subject to Members' support, the Government will invite submission of expression of interest from interested investors and companies interested in participating in the selection of ITIF sub-fund managers. Corresponding changes may be made having regard to the views received.

Financial Implications

25. We will seek approval from the Finance Committee (FC) of the Legislative Council to create a new dedicated subhead with a commitment of \$10 billion under the ITF in order to set up the ITIF, and to inject funds in five to six years from 2026-27. Any returns, including dividends and realised profits from exits of the investments concerned, will be deposited into the dedicated account(s) of the SPV established for the ITIF.

26. We will set up a Secretariat¹ responsible for the administrative work related to the ITIF.

Implementation Timetable

27. We plan to invite submission of expression of interest from interested investors and companies interested in participating in the selection of sub-fund

¹ We will explore hiring professional service providers (such as legal or investment consultants) to assist with the work of the Secretariat.

managers pursuant to the ITIF proposal in the first half of 2025. Upon receiving the FC's approval to set up the relevant new dedicated subhead under the ITF, the Innovation and Technology Commission will set up the ITIF, establish the Steering Committee, and take forward the open selection of fund managers, with a view to commencing relevant investments progressively from 2026-27 onwards.

Advice Sought

28. Members are invited to comment on the ITIF and support the Government to seek the relevant approval of the FC. We will continue to closely liaise with stakeholders and consult the financial sector as appropriate to refine the modus operandi of the ITIF.

Innovation, Technology and Industry Bureau
Innovation and Technology Commission
December 2024

Fund Structure of the Innovation and Technology Industry-Oriented Fund

