

## South Korea's New PE Age?

June 5, 2009

By [Kelly Holman](#)

Preeminent buyout firm **Kohlberg Kravis Roberts** scouted for buyout deals in South Korea for years before agreeing last month to purchase Oriental Brewery from **Anheuser-Busch InBev** for \$1.8 billion. The delay could be one of the smartest moves the firm has made in the last decade.

More importantly, the transaction -- announced weeks before North Korea unleashed an underground nuclear blast and threatened further missile launches -- heralds an opening for renewed private-equity dealmaking in South Korea, where LBO transactions took a back seat to strategic M&A in the last few years.

Additionally, a large syndicate of banks that includes **HSBC**, **JPMorgan**, **Nomura** and **Standard Chartered** has emerged to finance OB's acquisition, which gives KKR control of the country's second largest beer maker behind **Hite Brewery Company Ltd.**, and the right for OB to distribute Budweiser, Bud Ice and Hoegaarden beers in South Korea.

"It's not only watershed in ushering in a new era for private equity in South Korea, it's also significant in the number of structuring nuances in the transaction, including the offering of seller paper plus a formulaic provision for InBev to repurchase the business from KKR," says **Stewart Kim**, the managing partner of Los Angeles investment bank **PGP Capital Advisors LLC**.

Indeed. Following the KKR deal, some large South Korean companies have broached the idea of raising capital through stake sales, including to private investment firms.

Diversified industrial conglomerate **Doosan Corp.** announced on Wednesday, for example, that it would sell interests in certain divisions, valued at more than \$632 million, to Asian private-equity firms **Mirae Asset PEF** and **IMM Private Equity**.

KKR's purchase is different from other U.S. buyout firm investments that took place in the early part of the new millennium in South Korea, which were turnaround gambles on distressed Korean institutions.

**Nat Zilkha**, a director in KKR's Menlo Park, Calif., office, says the OB transaction couldn't be more different. "We're buying what we believe is a very strong, healthy and efficiently run company with a management team that we support," he says, adding, "Our thesis for OB is one of growth, as opposed to cost-cutting."

Zilkha says KKR is targeting financially solid companies in South Korea, operating across a broad swathe of sectors such as export-oriented businesses. Its strategy will revolve around "friendly," rather than hostile, transactions.

KKR isn't spooked by North Korea's military posturing or South Korea's quarterly macroeconomic fluctuations.

"We're long-term investors and nothing that's occurred has altered our long-term confidence [in South Korea]," Zilkha says.

Indeed, the latest threat posed by North Korean leader **Kim Jong-il**, who is believed to be transitioning the reins of his government over to his son **Kim Jong-un**, hasn't phased the Far East country's financial community, observers say.

"It has no bearing on it. Investors have taken everything into consideration and North Korea's risk has been incorporated into South Korea's sovereign rating," says **Jong Han Kim**, a partner at **Paul Hastings** who heads the law firm's Korea practice.

**Moody's Investors Service**, for instance, has maintained its A2 rating and stable outlook on the country's sovereign debt.

"While recognizing that the North's flurry of provocations in the past week or so have heightened uncertainties, we also consider that the stable outlook on South Korea's A2 sovereign ratings remains appropriate," wrote **Thomas Byrne**, a senior vice president at Moody's, who authored a special report on North Korea's recent nuclear detonation and missile launches.

Paul Hastings' Kim says, however, that if a large naval battle occurred between North Korea and South Korea in the West Sea or a major DMZ incursion took place, it might rattle private investor interest in South Korea.

If South Korea's KOSPI stock exchange offers any indication, the country's broad market investors aren't overly concerned by the North's latest saber rattling, either. The stock index slid 6% immediately following the country's underground nuclear test a week ago, but it subsequently rebounded.

Meanwhile, KKR took another step in late May to fortify its investment business in South Korea, signing a memorandum of understanding with the **Korea Development Bank** to pursue additional investments in the country.

The move, observers say, is sure to help the private-equity firm win over business executives that may be reticent in dealing with outsiders.

A backlash against foreign investors under the country's prior administration, headed by deceased President **Roh Moo-hyun**, who was known for his protectionist sentiment, seems to have subsided. Moreover, the political climate has changed since President **Lee Myung-bak** took office.

"When he took office in February 2008, he wanted to make [South] Korea a pro-business nation. Political sentiment has really changed in favor of inviting foreign investors back," Paul Hastings' Kim says.

### **Other big players**

KKR's deal isn't the only buyout transaction that took place in May. **Morgan Stanley Private Equity** sold Seoul-based **Ssangyong Corp.** to **GS Holdings Corp.**, also of Seoul, for \$96.4 million.

The spate of transaction-making has Asia's M&A community abuzz. "People are calling this the golden age of Korean private equity," says PGP's Kim, who returned from Seoul last weekend.

At press time, Hong Kong-based investment firm **Affinity Equity Partners** was rumored to be interested in part of KKR's OB stake.

Other large U.S. private-equity firms, too, have taken steps to tap into South Korea's corporate landscape, partnering with the government's pension fund.

The **Blackstone Group** teamed up with the **National Pension Service of Korea** last fall to fund \$4 billion of new investments in South Korea, while the Korean pension plan disclosed that Los Angeles' **Oaktree Capital Management LP** had committed to invest \$3 billion in the country.

Renewed buyout firm interest in South Korea stems from the confluence of several factors, including motivated corporate sellers, a favorable foreign exchange environment, and the resolution of the Korean bank liquidity crisis, according to PGP's Kim.

"A number of private-equity firms that have spent time in China are finding it difficult to do deals in China. In certain industries, investing in Korean firms with a high export rate to China is viewed as interesting," he says.

Some deal flow is expected to come from South Korea's "chaebols," or conglomerates like **Samsung Group**, **SK Group** and **LG Group**. Many multinationals are over-leveraged from having gone on acquisition binges over the last few years and, hence, are expected to divest non-core divisions to pay down debt.

"There are a lot of attractive assets that sit inside some larger conglomerates and also some standalone public companies that present attractive investment opportunities," Zilkha says.

Financial service companies are another potential avenue where private-equity investors may be able to invest capital. **Woori Finance Holdings**, owned by South Korea's government, could attract strong interest from financial investors if plans to shore up its capital base come to fruition.

Another industry that could see deal activity is South Korea's automotive parts business. One company that has been the subject of chatter is Halla Climate Control Corp. Talk about the Korean company -- a division of **Visteon Corp.** -- as a potential acquisition target began swirling after its U.S. parent filed for bankruptcy on May 28, says one source.

The new flurry of buyout deals has taken place after the country's slowing economic growth rebounded. South Korea's GDP growth increased minimally, 0.1%, in the first quarter after a sharp decline in December 2008, according to the **Bank of Korea**.

The improvement should appeal to U.S. financial sponsors keen on entering the nation.

New entrants, though, will face stiff competition from a host of South Korea-focused investors including Affinity, **Macquarie Bank's** Korea Opportunities Fund, **MBK Partners**, **STIC Investments** and **Vogo Fund**.

The U.S. financial sponsor community has shied away from South Korea in recent years after the government officials went after Dallas' **Lone Star Funds** a couple of years ago, following its 51% purchase of **Korea Exchange Bank** for \$1.5 billion in 2003. The Texas investment group was one of a handful of other U.S. private-equity firms that were also pursued by South Korean authorities.

Lone Star, which still owns a majority stake in KEB, was ultimately absolved of any wrongdoing.

Whereas Lone Star encountered tribulation in the country, the **Carlyle Group** has been very successful with a past investment in South Korea. The Washington firm invested \$40 million in South Korea's **KorAm Bank** in June 2000, and then co-invested with JPMorgan Corsair to pump \$395 million of equity into the bank. Four years later, it sold its stake to **Citigroup** for \$2.6 billion, generating an internal rate of return of around 25%.

# Buyouts Bloom Anew

Largest South Korean PE deals over the last five years

TARGET NAME/ACQUIRER NAME	VALUE OF TRANSACTION	DATE ANNOUNCED	DATE EFFECTIVE
<b>Oriental Brewery Co. Ltd.</b> <b>Kohlberg Kravis Roberts &amp; Co.</b>	\$1.80B	May 7, 2009	
<b>C&amp;M Co. Ltd.</b> <b>Investor Group</b>	\$1.40B		March 27, 2008
<b>Hynix-Non Memory Chip Op</b> <b>Citigroup Venture Capital</b>	\$0.82B	June 6, 2004	Oct. 6, 2004
<b>Himart Co. Ltd.</b> <b>Affinity Equity Partners Ltd.</b>	\$0.69B	Feb. 4, 2005	April 6, 2005
<b>Haitai Confectionery &amp; Foods</b> <b>Investor Group</b>	\$0.58B		Jan. 12, 2005

Source: Thomson Reuters

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