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Banks miss out as Chinese firms do DIY deal advice

Logo of Didi Chuxing is seen at its headquarters building in Beijing, China, May 18, 2016.
REUTERS/Kim Kyung-Hoon/File Photo

By Sumeet Chatterjee and Denny Thomas | HONG KONG

When ride-hailing firm Didi Chuxing agreed to buy Uber Technologies Inc's China unit this month, creating a $35 billion business, both firms used in-house advisory teams, meaning the investment banks that normally advise on these deals missed out on an estimated $60 million in fees.

China's cashed-up and ambitious technology firms are increasingly spurning external advisers on acquisitions and investments in foreign companies. China tech M&A doubled last year to nearly $68 billion, but fee volume only rose by around 60 percent, according to Thomson Reuters and Freeman Consulting data.

Paying for advice is still a relatively new concept for Chinese firms, so they tend not to be big fee payers. While large conglomerates in developed markets have hired investment bankers to

beef up in-house operations, they do still also use external advisers. The trend in China is to go in-house exclusively - as executives reckon the cost of external advice outweighs the benefit.

Some Asia-based bankers privately acknowledge that the use of in-house advisers hurts their M&A business, and they want to work more closely with Chinese technology entrepreneurs to win back some of that work. But they point out that the main fee-making opportunities from these companies are in providing banking services, such as cash management and foreign exchange, and when firms plan to list their shares publicly.

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To build their in-house M&A and corporate finance teams, Chinese companies have been plucking talent from Wall Street banks - at a time when some large U.S. and European investment banks are cutting costs and shrinking their Asia footprint.

This hired experience can be invaluable to some Chinese firms new to the international scene.

"As we start to expand internationally, we really need more international people who can play critical roles because we need to be very close to the chairman, and he only speaks Chinese," said Winston Cheng, a former head of Asia technology, media and telecoms banking at Bank of America, who was hired last year as global head of corporate finance at Chinese smartphone and electric car maker Le Holdings, also known as LeEco.

Other Chinese tech companies to scoop up Asia investment bankers in recent months include internet search firm Baidu Inc and search and security business Qihoo 360 Technology Co, a Reuters survey of professional networking service LinkedIn shows.

LeEco's Cheng said he has built a team of 45-50 people, mostly former Wall Street investment bankers, adding that an in-house team is cost-effective and gives companies better control in deal-making. "The internal cost is a lot less than what we would have paid advisers, that's for sure," he said.

LeEco last month announced the $2 billion acquisition of U.S. television set maker Vizio, and it did not employ any outside adviser for its biggest deal to date.

Leaving a high-profile position at a global investment bank to join a technology start-up can involve taking a pay cut, but that pain can be eased with stock options and job stability, bankers and headhunters say.

"They're very interested in going into that because you're going into a company that's looking to grow, compared to many banks that are shrinking," said John Mullally, director of financial services at headhunter Robert Walters in Hong Kong.

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Based on the size of the Didi-Uber deal and the usual percentage paid in advisory fees, banks on both sides would have earned $23-$30 million, according to Freeman Consulting Services estimates.

Uber managed its side of the deal in-house, a person close to the U.S. company said, through Cameron Poetzscher, vice president of corporate development who spent nearly two decades at Goldman Sachs, and chief business officer Emil Michael.

Didi's president Jean Liu also previously worked at Goldman, while Alibaba Group, Baidu, and JD.com have hired senior bankers from Goldman, Credit Suisse, Deutsche Bank and others.

Asian firms still rely on external advisers for M&A deals, especially when crossing borders, said Lam Nguyen at Freeman Consulting, but the list of bankers switching to fast-growing technology clients is growing, especially in China.

"You may be close to one adviser but that adviser may not be close to all the situations you try to get involved with," said LeEco's Cheng, whose CV includes seven years at Goldman before he joined Bank of America.

"You have to manage so many advisers it becomes challenging. Building in-house capabilities allows you to have a much more strategic, focused approach and execution," he said.

(Reporting by Sumeet Chatterjee and Denny Thomas, with additional reporting by Heather Somerville in SAN FRANCISCO; Editing by Ian Geoghegan)