

Hong Kong Revises Listing Rules

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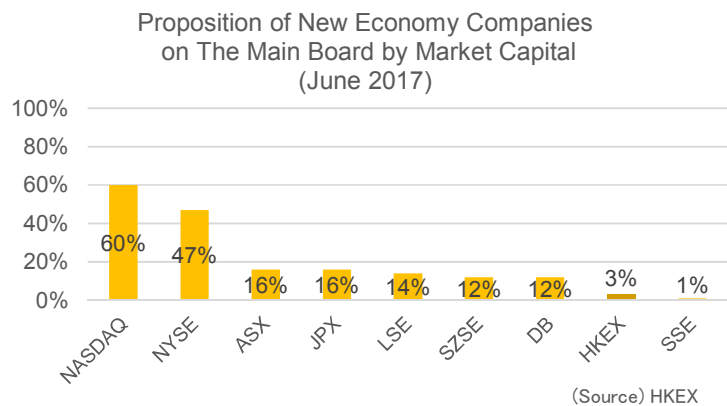
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Hong Kong Exchange and Clearing Limited (hereinafter HKEX) published its consultation conclusions to specify the revision points and schedule of Hong Kong listing rules on 15th Dec., 2017. The conclusions were published pursuant to a review of 460 feedbacks collected from the 2 months' public consultation from 16th Jun., 2017. "It is the most significant market reform in more than 20 years (following the permission to list H shares)", as Charles Li, chief executive of HKEX has remarked. While the revision will tighten listing standards such as minimum market capitalization to discourage the listing of average-quality companies with comparatively lower growth potential, it will also introduce in a new set of mitigated listing standards to attract the listing of qualified new-economy¹ companies on the Main Board. This report will give a brief introduction of the background and the main contents of the revision.

BACKGROUND

Known for their moderate financial requirements at listing and less-burdensome financial reporting obligations after listing in compare with NYSE and NASDAQ, Hong Kong stock exchange has attracted an abundant number of IPOs especially from Chinese companies in recent years. As a result, HK was the world's top IPO fundraising market in both 2015 and 2016. However, along with the IPO expansion, there is an increasing market concern about problems such as immediate price slump after IPO, scarce transaction volume of some stocks, and abuse of GEM-to-Main Board transfer process.

In addition, given the fact that nearly half of the Main Board market capital is contributed by companies in financial and real estate sectors, Hong Kong market lags behind major stock exchanges in Europe and America in its effort to attract new-economy companies. As a result, the proportion of new-economy companies listed on the market remains comparatively low. The memory is still fresh about Hong Kong's losing of a super large IPO several years ago when talks with Alibaba broke off at adjusting the current regulation that forbids a company with class-share structure to seek IPO in Hong Kong. It spurs HKEX to set sights on the reform of listing rules and grapple with future chances to take new-economy companies on board. Despite the initial overture to establish a third market



¹ According to OECD explanation, New Economy describes aspects or sectors of an economy that are producing or intensely using innovative or new technologies. This relatively new concept applies particularly to industries where people depend more and more on computers, telecommunications and the Internet to produce, sell and distribute goods and services.

for new-economy companies, the consultation conclusion has taken the direction to incorporate the mitigated listing standards for qualified new-economy companies into Main Board listing rules.

HIGHLIGHTS

(1) Amendments Taking Effect on 15th Feb., 2018

More stringent listing requirements are to be imposed, especially for those interested in listing on GEM. GEM itself, which was established with the purpose to serve growth companies, is repositioned as a standalone market for all small and mid-sized companies. The route to transfer a GEM-listed company to the Main Board is to be narrowed down accordingly.

[Amendment to Existing Listing Requirement]²

| | | Main Board | GEM |
|------------------------|------------------------------------|---|--|
| Financial requirement | Profit Test | <ul style="list-style-type: none"> Profit of most recent fiscal year ≥HKD 20million, and Gross profit of the past 2-3 years ≥HKD 50million <u>Minimum market capitalization at listing ≥HKD 500million (Before: HKD 200million)</u> | / |
| | Market Cap/ Revenue Test | <ul style="list-style-type: none"> Minimum market capitalization at listing ≥HKD 4billion Revenue of most recent fiscal year ≥HKD 500million | <ul style="list-style-type: none"> <u>Minimum market capitalization at listing ≥HKD 150million (Before: HKD 100million)</u> |
| | Market Cap/Revenue/ Cash Flow Test | <ul style="list-style-type: none"> Minimum market capitalization at listing ≥HKD 2billion Revenue of most recent fiscal year ≥HKD 500million Gross cash flow of the past 3 year ≥HKD 100million | <ul style="list-style-type: none"> <u>Total cash flow of past two years ≥HKD30 million (Before: HKD 20million)</u> |
| Offering Structure | | <ul style="list-style-type: none"> Public float share ≥25% of total number of issued share, and <u>minimum public float value at listing ≥HKD 125million (Before: HKD 50million)</u> Mandatory public offer ≥10% of total IPO size | <ul style="list-style-type: none"> Public float share ≥25% of total number of issued share, and <u>minimum public float value at listing ≥HKD 45million (Before: HKD 30million)</u> <u>Mandatory public offer ≥10% of total IPO size (Before: not specified)</u> |
| Post-IPO Lockup Period | | <ul style="list-style-type: none"> 6 months After the lockup period, controlling shareholder must retain its controlling status for another 6 months | <ul style="list-style-type: none"> <u>12 months (Before: 6 months)</u> <u>After the lockup period, controlling shareholder must retain its controlling status for another 12 months (Before: 6 months)</u> |
| Information Disclosure | | <ul style="list-style-type: none"> Share allocation to related parties subject to advanced report | <ul style="list-style-type: none"> <u>Share allocation to related parties subject to advanced report (Before: not specified)</u> |

[Amendments to Transfer Process from GEM to the Main Board]

- removal of the streamlined process for listing transfer from GEM to the Main Board
- introduction of a mandatory sponsor requirement for transfer of listing from GEM to the Main Board at least 2 months before the submission of the transfer application

² Please refer to the underlined parts for major amendments

(2) Amendments under Consultation

HKEX has also started the process to create new listing rules for the Main Board-listing of new-economy companies. The draft on the new rules will be completed and public consultation will be initiated within the first quarter of 2018 to enable the rule implementation by the late half of this year. According to the report by HKEX, the revision will widen the route to list pre-revenue bio-tech companies, new-economy companies with class-share structure and new-economy companies seeking secondary listing on the Main Board. At creating new listing opportunities, HKEX will also adopt a set of listing criteria to help manage the listing risks.

【Listing of Pre-revenue Bio-tech Companies】

A new chapter will be introduced in the Main Board listing rules to facilitate the listing of bio-tech companies before they earn revenue. However, listing requirements will include a minimum market capital of no less than HKD 1.5billion, and an enhanced working capital of no less than 125% of the issuer's current working capital. A guidance letter is expected to be issued by HKEX to help determine the eligibility/suitability of such listing.

【Listing of New-economy Companies with Class-share Structure】

A new chapter will be introduced in the Main Board listing rules to facilitate the listing of new-economy companies with Weighted Voting Rights. However, a minimum market capital of HKD 10billion at listing is required. In case the issuer's market capital level meets the minimum requirement but stays less than HKD 40billion, an additional minimum revenue requirement of HKD 1billion in the most recent fiscal year will also be applied at listing. A guidance letter is expected to be issued by HKEX to help determine the eligibility/suitability of such listing.

【Facilitating Secondary Listings for New-economy Companies】

The Main Board listing rules will open a new route to secondary listing for new-economy companies with good record of compliance for at least 2 years on the qualified market³, where it is primarily listed. However, the listing requirements will include a minimum market capital of HKD 10billion. In case the secondary issuer is a company with Weighted Voting Rights, or a company with its business centred in Great China region, the minimum market capital required at time of secondary listing will be HKD 40billion.

COMMENTS

Despite that imposing stringent listing rules raises the threshold to list a general company on Hong Kong Stock Exchange, it is an efficient measure to uphold the quality and instil confidence to the market. On the other hand, it is expected that the removal of restrictions that once hampered the listing of high-potential and fast-growing new-economy companies will lead to market diversification and revitalization in future.

Being a world leading IPO market, Hong Kong is struggling to keep its fundraising momentum growing. It remains to be seen whether the revision of listing rules will effectively attract more IPOs of innovative companies in future.

【Disclaimer】

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³ Qualified market refers to LSE Mainboard, NYSE and NASDAQ