HKEX LISTING DECISION

HKEX-LD107-2017 (published in May 2017)

[Streamlined and incorporated into the Guide for New Listing Applicants in January 2024]

Summary	
Parties	Company A to Company M – Main Board and GEM listing applicants whose listing applications were rejected by the Exchange in 2016
Issue	To provide guidance on why the Exchange rejected certain listing applications
Listing Rules	Main Board Rule 2.06 and Chapter 8 GEM Rule 2.09 and Chapter 11
Related Publications	HKEX-GL68-13, HKEX-GL68-13A, HKEX-LD92-2015, HKEX-LD100-2016 and HKEX-LD107-1
Decision	The Exchange rejected the listing applications

PURPOSE

1. This Listing Decision in the Appendix sets out the reasons why the Exchange rejected certain listing applications from 1 January to 31 December 2016. For the reasons listing applications were rejected before this period, please refer to the listing decisions and guidance letters stated in "Related Publications" above.

APPLICABLE LISTING RULES

2. Chapter 8 of the Main Board Rules and Chapter 11 of the GEM Rules set out detailed eligibility requirements which a new applicant must fulfill and state that both the applicant and its business must, in the opinion of the Exchange, be suitable for listing.

3. Main Board Rule 2.06 and GEM Rule 2.09 state that suitability for listing depends on many factors. Compliance with eligibility requirements under the Listing Rules does not itself ensure an applicant's suitability for listing. You may refer to HKEX-GL68-13 and HKEX-GL68-13A which provide guidance on the factors that the Exchange would take into consideration when assessing whether an applicant and its business are suitable for listing under Main Board Rule 8.04 (GEM Rule 11.06).

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Appendix

Rejection cases in 2016	
Company	**Reasons for rejection**
Company A and Company B (Main Board Applicants)	Company A was a financial services provider in the PRC. Under the relevant laws and regulations, operation of the largest of Company A's business segments (with revenue contribution of over 90% of Company A's total net profit) was subject to licensing. However, Company A did not obtain such license and the relevant income was considered as generated from non-compliant sources. Company B was a logistics company in the PRC. During the track record period, Company B's operating expenses were partly financed by an interest-free loan from its controlling shareholder ("**Shareholder's Loan**"). As the Shareholder's Loan was interest-free, it was not on normal commercial terms. These listing applications were rejected on eligibility grounds as each applicant did not meet the minimum profit requirement under Main Board Rule 8.05(1)(a) after (i) excluding income from non-compliant sources; or (ii) imputing notional interest expenses on the Shareholder's Loan.
Company C (a GEM Applicant)	Company C was a provider of vehicle services in Hong Kong. It applied for a spin-off listing on GEM by way of an introduction. As there would be no offering, it relied on its forecasted P/E ratio to demonstrate it would meet the minimum market capitalisation requirement of HK$100 million under GEM Rule 11.23(6). Company C originally submitted a forecasted P/E ratio of over 125 times. In response to the Exchange's comment on the basis of its forecasted P/E ratio, Company C adjusted its forecasted P/E ratio to over 40 times, which still met the minimum market capitalisation requirement under GEM Rule 11.23(6). The reduced market capitalisation was determined based on the historical P/E ratios of two companies that were not directly comparable with Company C and the assessment involved various assumptions and judgement. In particular, one comparable company was loss-making and Company C estimated this company's P/E ratio based on its valuation two years ago (when it was profitable) and adjusted the ratio by the percentage decrease in the Hang Seng Index thereafter. The other comparable company was listed on an overseas exchange and only one of its segments was similar to Company C's business. Furthermore, Company C's assessment did not account for the differences between historical and forecasted P/E ratio. In view of the significant changes of its forecasts and the fact that such assessment is highly subjective and discretionary, the Exchange was of the view that Company C had not satisfactorily demonstrated its ability to meet the eligibility requirement and therefore rejected the listing application.

Rejection cases in 2016	
Company	**Reasons for rejection**
Company D (a GEM Applicant)	Company D was a software solution provider in Hong Kong. The listing application was rejected on eligibility grounds since after its most recent financial year, one of its two controlling shareholders ceased to be a controlling shareholder and the management was no longer influenced by the same controlling shareholders. Although there was no packaging concern, the Exchange decided that Company D was not able to meet the ownership continuity and control requirement under GEM Rule 11.12A(2), since the sponsor did not demonstrate that influence over the management by the remaining controlling shareholder was not materially different than by two controlling shareholders. As such, an investor cannot assess how Company D will be managed under the sole influence of the remaining controlling shareholder based on the previous financial results.
Company E (a Main Board Applicant)	Company E was a microcredit company in the PRC. During the track record period, certain loans and guarantees provided by Company E to its customers did not follow local policies applicable to microcredit companies. Although such policies were not mandatory, Company E's business license was subject to revocation if such policies were not followed. In light of such consequences, the Exchange regards that these policies should have been followed as a matter of best practice. Also, the amount of such non-compliant loans was material (constituted 62% to 99% of the gross amount of total loans granted during each year of the track record period) and Company E would not be able to meet the minimum profit requirement under Main Board Rule 8.05(1)(a) if income from such non-compliant loans were excluded. The listing application was rejected on suitability grounds taking into account the consequences of the policies and the materiality of the difference in interest income if the policies had been followed.
Company F and Company G (Main Board Applicants)	Company F was an integrated excavation service provider in Asia. It sold unprocessed ore from Country A to the PRC during the track record period. Due to regulatory changes which prohibited the export of unprocessed ore, Company F planned to process the ore before selling them after listing. Company G was a trading company in the PRC. It outsourced the production of food for sale in the PRC during the track record period. Company G planned to change its business focus to the production and sale of a new product after listing. These listing applications were rejected on suitability grounds due to extreme uncertainty on the sustainability of their businesses, as follows:

<table>
<tr><th colspan="2">Rejection cases in 2016</th></tr>
<tr><th>Company</th><th>Reasons for rejection</th></tr>
<tr><td></td><td>(i) the change in business model and/or product mix of these applicants would be a material change in their business model, cost structure, profitability and risk profile;

(ii) the applicants' management had no experience in operating the new business, which was fundamentally different from their existing business; and

(iii) the applicants could not demonstrate that their new business is sustainable.</td></tr>
<tr><td>Company H
(a GEM Applicant)</td><td>Company H was a distributor of two brands of consumer products in Singapore.

This listing application was rejected on suitability grounds because there was extreme uncertainty on the sustainability of Company H's business based on the following factors:

(i) it solely relied on its bank facility to maintain a positive cash balance;

(ii) it had high gearing and net current liability positions;

(iii) its brands had small and declining market share;

(iv) it had deteriorating financial performance after the supply of a major product was terminated by the manufacturer; and

(v) the plan to turnaround the business required it to shift its business focus to its second brand, that had even smaller market share and less market prominence, after the track record period.</td></tr>
<tr><td>Company I and Company J
(Main Board Applicants)

Company K
(a GEM Applicant)</td><td>Company I was a property management company providing property management services to one single housing estate in the PRC.

Company J was a printing company in the PRC.

Company K was a licensed software developer in Hong Kong.

These listing applications were rejected on suitability grounds due to their extreme reliance on a single estate, customer or product (as the case may be), as follows:

(i) during the track record period, over 90% of each applicant's revenue was generated from its largest customer and/or key</td></tr>
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Rejection cases in 2016	
Company	**Reasons for rejection**
	product (as the case may be); (ii) while the applicants relied on their respective customers for the revenue generated during the track record period, the reliance was not mutual and complementary, i.e. their respective customers were not reliant on them; and (iii) Company J and Company K operated in an evolving technological and/or regulatory environment. However, Company J and Company K lacked experience in selling new/upgraded products and failed to attract new customers during the track record period to reduce the reliance, and failed to demonstrate they can do so after the track record period. Company I failed to demonstrate that it can reduce its reliance on its one single housing estate after the track record period since it did not bid for any other estate during the track record period.
Company L (a Main Board Applicant)	Company L was a utility provider in the PRC. The listing application was rejected on suitability grounds since during the track record period, a number of Company L's senior management had been convicted of bribery in relation to Company L's construction contracts and Company L also failed to obtain the relevant construction permits before the commencement of construction/ operation of the material plants. In view of such misconduct and non-compliances, Company L's directors were not considered suitable under Main Board Rules 3.08 and 3.09 and therefore, Company L was rendered not suitable for listing.
Company M (a GEM Applicant)	Company M was a restaurant operator in the PRC. The listing application was rejected on both eligibility and suitability grounds due to the following factors: *<u>Inability to meet the minimum cashflow requirement under GEM Rule 11.12A(1)</u>* (i) during the track record period, a significant portion of Company M's income was derived from unconditional grants from local government which were not directly related to its restaurant business. The Exchange considered the grants not to be derived from Company M's ordinary and usual course of business and it was unable to meet the minimum cashflow requirement under GEM Rule 11.12A(1) after deduction of such grants; and

Rejection cases in 2016	
Company	**Reasons for rejection**
	Unsustainable business model (ii) Company M’s financial performance was deteriorating during the track record period as it failed to manage the impact of its increase in operating costs. Despite the implementation of cost-saving measures (such as a centralized kitchen) in the last year of the track record period, the deteriorating trend continued and management failed to demonstrate that they had the ability to turn around the business after the track record period.