HKEX LISTING DECISION

HKEx-LD134-2022 (May 2022)

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

Summary	
Parties	Company X – a Main Board listing applicant
Issue	Whether Company X is suitable for listing in light of (a) the prolonged deterioration of financial performance of its Core Businesses (as defined below); (b) the limited track record of its new services and temporary business improvement; and (c) the failure to prove its business improvement plans
Listing Rule	Main Board Rule 8.04
Decision	The Exchange decided that Company X was not suitable for listing and rejected its listing application

FACTS

1. Company X owned and operated five hospitals focusing on providing basic healthcare services to residents in local communities in China. Company X had submitted its listing application (the "**Original Listing Application**") with the corresponding track record period (the "**Original Track Record Period**"). In response to the Exchange's concerns, Company X subsequently updated its listing application (the "**Renewed Listing Application**") and the corresponding track record period with an additional 12 months of financial information (the "**Renewed Track Record Period**").

Original Listing Application

2. During the Original Track Record Period, Company X generated most of its revenue from its (a) outpatient clinic services (e.g. clinical treatments or day surgery); and (b) inpatient hospital services (together, the "**Core Businesses**"), representing almost 80% of its revenue. The remaining revenue was mainly generated from its sales of pharmaceuticals. Its general physical examination services had only contributed minimal revenue during the Original Track Record Period.

3. During the Original Track Record Period, the business and financial performance of the Core Businesses had been deteriorating significantly mainly for the following reasons:

   (a) ***Breach of Regulations relating to Inpatient Hospital Services*** – two of Company X's hospitals were found to be in breach of certain regulations imposed by the local hospital authorities (the "**Breaches**") for admitting some inpatients and mandating unnecessary inpatient services and treatments which involved higher fees. To prevent future Breaches (which may revoke Company X's hospitals as designated medical institutions for social reimbursement purposes), Company X had tightened its inpatient admission standards for all its hospitals. Since then, Company X recorded a significant drop in the utilization rate of beds in operation, the number of inpatient visits and relevant revenue from inpatient hospital services;

   (b) ***Relocation of Hospitals*** – in view of the land title issues/defects at the original hospital site, Company X had to scale down its operation at one of its hospitals (which contributed over 25% of its revenue), and planned to relocate to a new site, which was more distant from the original site and with only half of the total gross floor area and total number of beds (the "**Relocation**"). The operation of such hospital (the "**Relocated Hospital**") had been scaling down since the stub period of the Original Track Record Period. In addition, the remaining four hospitals were also located on leased properties with land title issues/defects or expiring term. The operations of these four remaining hospitals may also be exposed to potential material adverse impact arising from relocation; and

(c) ***COVID-19 Outbreak*** – the performance of the Core Businesses was further adversely affected since the outbreak of COVID-19 pandemic (the "**Outbreak**") as people were reluctant to visit hospitals amid the Outbreak.

4. In light of the above, the revenue and profitability of the Core Businesses had experienced serious decline over the Original Track Record Period. The Exchange therefore had concerns on Company X's business sustainability.

Renewed Listing Application

5. Company X submitted the Renewed Listing Application covering the Renewed Track Record Period. In an attempt to address the Exchange's concerns, Company X submitted that its business had improved as a result of an increase in revenue from general physical examination services and the COVID-19 nucleic acid tests, each of which contributed around 10% (together around 20%) of Company X's revenue in the last year and the stub period of the Renewed Track Record Period.

6. However, the business and financial performance of the Core Businesses continued to deteriorate. In particular, the Relocation for the Relocated Hospital lasted for almost half a year and since its resumption, it only managed to achieve around one-third of its level of revenue prior to the scale-down of the operation. In addition, two of Company X's hospitals (which contributed more than 40% of Company X's total revenue) were located on properties with leases that had expired or would soon expire. Company X had not provided any concrete renewal plans and the operations of these two hospitals were subject to imminent relocation risks.

7. According to Company X's forecast, it expected that the revenue from the Core Businesses would further decrease by around 10% notwithstanding COVID-19 had subsided in China, and that the revenue from the Relocated Hospital would still decrease by half as compared to that prior to the scale-down of the operation. In contrast, Company X forecasted that the general physical examination services and the COVID-19 nucleic acid tests would further expand and contribute, in aggregate, nearly 30% of the total forecast revenue in the upcoming financial year. However, Company X did not provide any basis in support of such growth estimate (e.g. no legally binding agreements substantiating the anticipated significant increase in general physical examination services).

8. In addition, Company X planned to use a substantial portion of the IPO proceeds for (a) upgrading equipment and hospital facilities aiming at providing more advanced diagnosis services, which it believed could increase the number of relatively more complex surgeries that generally had a higher gross profit margin; and (b) merger and acquisition of smaller hospitals located in areas where healthcare resources were scarce and demand for comprehensive and quality healthcare services was unmet, but no memorandum of understanding or agreement had been reached.

ISSUE RAISED FOR CONSIDERATION

9. Whether Company X is suitable for listing in light of (a) the prolonged deterioration of financial performance of its Core Businesses; (b) the limited track record of its new services and temporary business improvement; and (c) the failure to prove its business improvement plans.

APPLICABLE RULES AND PRINCIPLES

10. Main Board Rule 8.04 states that both the issuer and its business must, in the opinion of the Exchange, be suitable for listing.

ANALYSIS

11. In assessing Company X's suitability for listing, the Exchange considered all the facts and circumstances of the case and had taken the following factors into consideration:

Prolonged Deterioration in Financial Performance of Core Businesses

12. The business and financial performance of Company X's Core Businesses had been deteriorating significantly throughout the Original Track Record Period and the Renewed Track Record Period due to various adverse circumstances including the Breaches and the Relocation.

13. Having considered the fact that the Relocated Hospital had sustained a material business decline as a result of the Relocation, the imminent risk of possible relocation faced by Company X's two other major hospitals (which contributed a significant portion of Company X's revenue) and its lack of concrete plans in renewing the leases or securing other appropriate hospital sites have aggravated the concern that this would materially adversely affect Company X's operation, and in turn its business sustainability.

14. Company X had no specific strategies or plans in improving the Core Businesses. Based on its own forecast, Company X did not anticipate a significant rebound in the Core Businesses during the forecast period recovering to the revenue and profitability level prior to (a) the tightening of the standards of inpatient admission of all hospitals as a result of the Breaches; and (b) the Relocation. The Sponsor had also failed to provide any information to substantiate the sustainability of such businesses.

Limited Track Record of New Services and Temporary Business Improvement

15. Company X claimed that its business had improved in the last year of the Renewed Track Record Period and would continue to improve significantly as a result of the increase in revenue and profit attributable from the provision of general physical examination services and COVID-19 nucleic acid tests. However, provision of the general physical examination services had not been part of Company X's Core Businesses and was only incidental to other core services generating insignificant revenue historically. Company X generated around 10% of revenue from general physical examination services in the last year of the Renewed Track Record Period and there was also no concrete basis to support the projected three-fold increase in revenue to be generated during the forecast period. For COVID-19 nucleic acid tests, as the demand for such test varies over the developments of the Outbreak, the revenue

generated from these tests was temporary and may not be sustainable in the longer term.

Failure to Prove Business Improvement Plans

16. Company X failed to demonstrate how its expansion plan and proposed use of proceeds could improve its business and financial performance. The Exchange has taken the following into account:

    (a) there was lack of sufficient patient demand to justify the upgrade of equipment and facilities for advanced diagnosis services given its deteriorating historical financial performance of its inpatient hospital services and outpatient clinic services, low bed utilization rate and number of patient visits and there had been no sign of recovery. The commercial rationale for such upgrade was also unclear given that Company X's hospitals generally provided less complex treatments and focused on patients in local communities who preferred more affordable healthcare services; and

    (b) Company X had not clearly identified the criteria for and the availability of the targets for merger and acquisition. No memorandum of understanding or agreement had been reached. It remained questionable whether Company X could materialize its expansion plan.

17. In view of the foregoing considerations, the Exchange was of the view that the sponsor and Company X had not satisfactorily addressed the Exchange's concerns on Company X's business sustainability and its proposed use of proceeds.

DECISION

18. Based on the specific facts and circumstances, the Exchange decided that Company X was not suitable for listing and rejected its listing application.

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