Part B Consultation Questions

Please indicate your preference by checking the appropriate boxes. Please reply to the questions below on the proposed change discussed in the Consultation Paper downloadable from the HKEX website at:
https://www.hkex.com.hk/-/media/HKEX-Market/News/Market-Consultations/2016-Present/November-2020-MB-Profit-Requirement/Consultation-Paper/cp202011.pdf

Where there is insufficient space provided for your comments, please attach additional pages.

Capitalised terms have the same meaning as defined in the Consultation Paper unless otherwise stated.

1. Do you agree that the Profit Requirement should be increased by either Option 1 (150%) or Option 2 (200%)? Please give reasons for your views.

   ☐ Yes

   ☑ No

   You may provide reasons for your views.

Please see appendix A

2. Besides the proposed increase in the Profit Requirement, is there any other alternative requirement that should be considered? Please give reasons for your views.

   ☑ Yes

   ☐ No

   You may provide reasons for your views.

Please see appendix B

3. Do you agree that the Exchange should consider granting temporary relief from the increased Profit Requirement due to the challenging economic environment? Please give reasons for your views.

   ☑ Yes

   ☐ No

   You may provide reasons for your views.

4. If your answer to Question 3 is yes, do you agree with the conditions to the temporary relief as set out in paragraph 55? Please give reasons for your views.

   ☐ Yes

   ☑ No

   You may provide reasons for your views.

- End -

Appendix A

Reply to question 1 (words in italics are basically extracts from the Paper):

Primary objective of the consultation paper (the "Paper") is to increase the Profit Requirement, reasons being that certain issues arose which the Stock Exchange believes were due to the increased Market Capitalization Requirement which was introduced in 2018. *A number of the Small Cap Issuers failed post listing to meet the profit forecasts they had filed...which gave rise to concerns about the reasonableness of their valuation, resulting in significant decrease in such issuers' share prices and thereby losses to the investing public......and whether their valuations were simply reverse engineered...in order to manufacture potential shell companies for sale after listing given the perceived premium attached to the listing status*. The Stock Exchange also alleged that *there had been suspected abusive behavior such as manufacturing of an artificial shareholder base and was concerned whether the relevant investors were independent*. Paragraph 7 of the Paper then says that *a key underlying cause of the aforementioned issues is the misalignment of the Profit Requirement with the revised Market Capitalization Requirement. Accordingly, the Stock Exchange believes that increasing the Profit Requirement either by way of Option 1 or Option 2 can effectively address the aforementioned issues as stated in the Paper*. It appears to be a very straight forward solution, but actually it is not.

Social Responsibility

Foremost, I would like to voice or echo the importance of social responsibility, in particular for those who are in power or with authority.

The Paper has analyzed that *taking Option 1 and Option 2, on average, would have eliminated 62% of the Profit Requirement Applications and might be expected to have similar impact on future potential applications* but then said *the aggregate market capitalization at the time of listing of all Ineligible Applications under Option 1 that have been listed only accounted for 3% of the aggregate market capitalization of Main Board users between 2016 and 2019 (both inclusive).....and so increasing the Profit Requirement will not have a material impact on the overall capital market. The Stock Exchange went on suggesting that those early development companies and small or mid-sized companies can go listing on GEM instead*.

Based on the Census and Statistics Department of the HKSAR, the latest seasonally adjusted unemployment rate of Hong Kong in the fourth quarter of 2020 was 6.6%, being the highest in 16 years, even surpassing the 5% as recorded in 2009, being the year of "financial tsunami ". Although the Paper does not specifically state when the consultation conclusions will be implemented, based on previous experience of their implementation schedule, it will probably be sometime in the second half of the year. If so, it is highly likely that based on the analysis of the Paper on the impact of "small cap issuers" as mentioned in the last paragraph, it will be a hard-hit on the employment situations of the small and mid-sized corporate finance houses, law firms, audit firms, valuers, financial public relations firms, printing houses, etc, thereby further increasing the overall unemployment rate in 2021 and at least a few years ahead. Further, without availability of the fund-raising platform on Main Board, the early development companies as well as the small or mid-sized companies will obviously be less competitive against the "bigger brothers" in their respective industries or some will even be driven away from the industries.

Right now, Hong Kong people, and Hong Kong itself, are experiencing unprecedented challenges economically and politically. My simple question is why the consultation was even put forward in the first place under the current extremely stormy situation that we all Hong Kong people are facing? Even our SAR Government has been trying to minimize unemployment in various sectors by implementing

Keep-employment Policies and relief measures in the past year or so. Is our Financial Secretary aware of the release of this Paper that will have an unintended consequence of further increasing the overall unemployment rate of Hong Kong? Whilst the Stock Exchange and the Securities and Futures Commission are actively encouraging all listed companies, be it big or small, to take on social responsibility, which is a good thing for sure, I strongly believe that the Stock Exchange, being a listed company on its own, can set a good model to them by deferring the consultation or delaying implementation of the proposals as stated in the Paper. Doing something even if it is good but at the wrong timing can be bad after all.

Free Market and Market Development

The second point I would like to make is fairness to access the capital market of Hong Kong. As discussed above, implementation of the proposal as stated in the Paper will certainly prevent a very large number of early development companies and small or mid-sized companies from accessing the fund raising platform on the Main Board. On the other hand, the Stock Exchange might be very happy to see more and more secondary listings of those mega China enterprises from the US and primary listing of bio-tech companies under Chapter 18A. Together, our Main Board will then become a biased capital market without the participation of small IPO players though Hong Kong might still continue to be the biggest IPO fund raising place in the world. My question is whether getting this Sheer Number One is all for Hong Kong to be claimed a real international financial centre in the world? Of course, it is not.

With Hong Kong's historical and economic development in over 100 years of time, Professor Milton Friedman, Nobel Laureate in economic sciences in 1976, once praised Hong Kong as the freest economy in the world, and that is the main factor of Hong Kong's success in the past economically. We all have to be mindful of the likely adverse impact on our free market if the "Visible Hand" is doing too much and in the wrong direction. While other world major markets like the US are heading towards a more diversified capital raising platform such as the recent introduction of SPAC, our Stock Exchange is trying to move against the world tide by strictly limiting the opportunity of Small Cap Issuers from accessing the Main Board. Large is good and small is bad? No, it is not. According to Bloomberg, SPACs in the US have completed nearly US$26 billion of share sales in January 2021. According to the Financial Times, Singapore is stepping up bid to become Asia's SPAC hub to capitalize on surging investment in the region's tech start-ups. On the contrary, our Stock Exchange is concerned about certain small cap issuers trying to manufacture potential shell companies for sale after listing. For sure, it is important for Hong Kong's capital market to allow fair access to qualified companies of different sizes. *As compared with the profit requirements of the Selected Overseas Main Markets, both Option 1 and Option 2 will result in the Exchange having the highest profit requirement on an aggregated basis for the three years of a track record period.* The Exchange highlighted that profit requirement had not been adjusted in the past 26 years but it has to be discussed with Appendix I "History of the Profit Requirement" in the Paper, which says that consultations on profit requirement have been made in 1994, 2002, 2010, 2016 and 2017. *The Main Board listing eligibility requirements were comprehensively reviewed in April 2010 and it was concluded that the Profit Requirement remained a good indicator of new applicants' future profitability and no change was made to the Profit Requirement. As part of the initiatives to improve market quality, the Listing Committee reviewed the Main Board's listing eligibility requirements again in June 2016. It agreed that the Profit Requirement should be maintained because there were no red flags or strong calls from the market to change the requirement.* In a nutshell, profit requirement has not been a neglected topic in the market and actually has been reviewed by the Exchange from time and time. *Like the comments made by some respondents in the 2017 consultation, the profit requirement is generally a good indicator of a new applicant's future performance and the current level of the profit requirement is on par with the main markets of the overseas exchanges.* In other words, the proposal set out in the Paper is not aimed at making our market more diversified or balanced. Neither is it aimed at making our market more competitive on the listing eligibility requirements and nor it is for making our market more equitable to market participants.

Appendix B

Reply to question 2 (words in italics are basically extracts from the Paper):

The Exchange made the point in the Paper that the misalignment of the Profit Requirement with the revised Market Capitalization is a key underlying cause of those issues and trouble as discussed in paragraphs 4 to 6 of the Paper. The Market Capitalization was increased in 2018 and so to address the issues, the Profit Requirement should be increased by either Option 1 or Option 2. It all seems very logical, but actually it is not when we put it into the context of the current economic situations of Hong Kong and it is what policy makers have to take concerns before making decisions. Policy makers have established a certain system, setting up rules of the game or competitive criteria. People in the system will behave in ways trying to win among the players and then keep surviving. Some might choose to act in a rather naughty way and some will act obediently all based on the rules as allowed, legally and socially. Taking either Option 1 or Option 2 is similar to changing rules of the game in the system but with the consequence of penalizing both the "bad" guys and the "good' guys. Why is increasing the Profit Requirement the only direction to solve the misalignment? Why isn't adjusting the Market Capitalization an option to the Exchange? Is it because the HK$500 million was determined in 2018 and so it could not be touched? Increasing the Profit Requirement 1.5 times or 2 times of the existing level is exorbitant from all angles except for the pure reason of aligning it with the $500 million market capitalization requirement. I suggest the profit requirement be increased but at a lesser scale and at the same time the market capitalization requirement be adjusted downward.

The Exchange suggested in the Paper that those small cap issuers could still access the capital market by listing on GEM. However, by reviewing the Exchange's Fact Books 2018, 2019, HKEX Market Statistics 2020 and GEM Market Statistics, we can see the unimpressive performance of GEM. From 2017 to 2020, the number of GEM listing has kept decreasing to just 8 new listings in 2020 compared with 138 on Main Board (excluding transfer of listing from GEM). In 2020, the equity funds raised in IPOs on GEM is approximately HK$ 550 million, representing just about 0.14% of that raised on Main Board. Also in 2020, the equity funds raised in post-IPOs on GEM is approximately HK$ 3 billion, representing just about 0.87% of that raised on Main Board. Obviously, there are inherent issues existing on GEM that have dampened its ability to be a good choice of fund raising platform for early development companies and small or mid-sized companies and this has to be thoroughly reviewed and discussed among all market participants. All in all, with the objective of offering suitable fund raising platform for these small cap issuers, most of which are in fact companies based in Hong Kong, a more comprehensive consultation is a much better option than purely aiming at increasing the Profit Requirement alone as suggested in the Paper.