16 December 2022

BY EMAIL (response@hkex.com.hk)

Hong Kong Exchanges and Clearing Limited
8th Floor, Two Exchange Square
8 Connaught Place
Central, Hong Kong

Dear Sirs

Re: Response to the Consultation Paper on a Listing Regime for Specialist Technology Companies ("Consultation Paper")

The Chamber of Hong Kong Listed Companies is pleased to submit our views and response to the captioned Consultation. First of all, we believe this is a strategic move in the right direction and is something the Chamber has been advocating for since the beginning of the year. We are pleased to see this is happening.

In this submission, we would like to tackle one fundamental question: how should the Hong Kong market position itself against other markets and how can Hong Kong remain competitive and achieve what it sets out to do.

As we pointed out in our earlier paper submitted to the Exchange, Hong Kong should continue to play an active role as a capital formation centre for tech enterprises from the mainland to help achieve the national goal of becoming self-reliance in key technology areas. Hong Kong as a leading international financial centre has an established edge in this respect. But this advantage is not exclusive to Hong Kong. The mainland exchanges are also gearing up their efforts to target tech companies. For certain industries, like semiconductors which are critical to national technology development, the mainland exchanges are the natural choice. Just in early November, Hua Hong Semiconductor Ltd (1347.HK), a Chinese chip manufacturer received regulatory approval for an 18 billion yuan (US$2.5 billion) IPO in Shanghai. Besides reflecting the "going-home" strategy of semiconductors industry, this listing demonstrates Shanghai Stock Exchange has the necessary market depth to absorb a tech transaction of such size. To win in the race for tech listings, Hong Kong needs to be very focused and targeted, eyeing for the types of companies that offers us the best opportunities and advantages.

We agreed with the five specialist technology sectors identified in the Consultation Paper. They represent important technology sectors that would either help define our country's national supremacy, such as quantum computing and aerospace technology, or complement the national objective, such as electric vehicles for carbon reduction, thus enjoying strong growth momentum. Yet, for a tech listing market to be successful, it needs to be vibrant with sufficient number of listings and liquidity. An adequate number of companies is required to attract investors interests, sustain their participation and build an investment eco-system. Whilst we agree to the identified sectors, listings from some of these sectors may be few and far between. We maintain our view that the enterprise software companies (falling under the Next Generation Information Technology sector named in the Consultation) should be Hong Kong' s prime target and will give Hong Kong's tech listing market the best chance of success.

Yet, for this sector, the present proposed HK$8 billion market capitalisation for commercial companies would be a big hurdle. From 2019 to the first half of 2022, 11 companies from the Enterprise Software and AI sectors reaching the revenue between 250m yuan and 400m yuan (compatible with the HK$250m revenue requirement for commercial companies under the HKEX Specialist Tech Listing Regime, or "18C") went public on the STAR Market of Shanghai Stock Exchange with price-to-sales multiples ranging from 12 times to 40 times (See Appendix 1). Of these 11 companies, only five achieved a market capitalisation over 7 billion yuan (equivalent to HK$8.8 billion), which means HKEX would be turning away 54% of potential listings from this sector even if they were to list here.

The Consultation Paper did not explain why HK$8 billion is recommended. One plausible reason is this is the valuation benchmark of Unicorns. However, at the current down-market cycle, many Unicorns find themselves unable to command such a high valuation anymore. According to media reports[1], the top decile of US late-stage start-ups by

[1] https://pitchbook.com/news/articles/venture-capital-valuations-unicorns-crossover-investors

valuation have seen their price plummeted to $680 million in Q3 2022, representing a decrease of pre-value valuation of 54%. The validity of holding on to this threshold is open to question.

To put things in context, HKEX Listing Rules Chapter 18A designed for pre-revenue biotech companies requires only a market capitalisation at listing of HK$1.5 billion, which is less that one-fifths of what is proposed for 18C. This is inconsistent. If allowing only tech companies of high valuation to list is to contain risks to investors, it does not explain why a much lower market capitalisation requirement is set for 18A. Although 18A companies are required to have completed Phase 1 clinical trials, approved by a Competent Authority, for new pharmaceutical (small molecule drug) products or, in the case of new biologic products, having no objection from the relevant Competent Authority for them to commence Phase II (or later) clinical trials, one must not forget that these are only development milestones and do not equate commercial success.

For the biotech industry, the success of a company does not depend solely on the science or technology. It has been reported that biotech companies could fail for a number of reasons.[2] Their founders who are scientists or academics in many cases may lack general and financial management skills, or the ability to identify risks or communicate effectively with staff and the investment market. These may result in delays in clinical trials, inability to keep pace with the clinical landscape, cash burnout, and loss of investors' support.

On the contrary, commercial B2B enterprise software companies have market-driven products or services, established customer base, and demonstrable growth trajectory. They operate on a proven and scalable business model. There is no reason they be regarded as high-risk entities and face extra hurdle of high market capitalisation.

One must not forget that there is no simple co-relation between size and risks. There are numerous cases of large companies collapsing. The most recent one being the downfall of Crypto Exchange FTX. Raising the bar so high does not eliminate risks per se but only exclude many quality companies from accessing our market.

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[2]https://www.biospace.com/article/good-science-doesn-t-guarantee-success-here-s-why-some-biotech-startups-fail/

From a competitive point of view, the Star Market of Shanghai Stock Exchange also allow companies to list with a revenue and market capitalisation test. Their requirements are RMB200 million and RMB1.5 billion respectively. The revenue requirement is similar to what is proposed for 18C but the market capitalisation required is much lower. Companies generating that level of sales can be listed in Shanghai instead of Hong Kong and have earlier access to funding.

Besides, the Shanghai stock markets enjoy much better liquidity. As of December 2022, the market liquidity of Shanghai Stock Exchange was 9 times (the Star Market even traded at 40 times[3]), compared to a mere 79% of HKEX as October 2022[4]. The high liquidity indicates more frequent trades of company shares, which would aid in price discovery and is favourable for post-listing transactions. Hong Kong's liquidity is traditionally lower than the mainland markets and this situation is exacerbated recently by the reduced participation of U.S. capital under geopolitical tensions. This does not weigh in our favour for attracting new listings.

One may think Hong Kong should be targeting companies with higher valuation while letting STAR Market focus on smaller ones. But the fact is Shanghai is strong in listing large companies as pointed out earlier, and Hong Kong does not have absolute advantage in that regard. If Hong Kong maintains its requirements on such an uncompetitive level, we may lose out on both fronts of smaller and bigger companies.

A related question is whether the revamped GEM (which HKEX is looking into) could be the platform for smaller tech companies that does not meet the HK$8 billion market capitalisation requirement. It has always been the Chamber's stance that Hong Kong should have multi-tiered capital markets that provide companies of all sizes, including smaller ones, sufficient market access. It is unfortunate that GEM has not been functioning well in recent years, and whether the revamped GEM can fulfil this purpose remains unclear. At such early stage, little is known about the reform direction and timetable. It is inadvisable for our market to wait on the side line and forgo opportunities of listing smaller but promising tech companies.

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[3] http://www.sse.com.cn/market/stockdata/statistic/

[4] https://www.hkex.com.hk/Market-Data/Statistics/Consolidated-Reports/Monthly-Bulletin?sc_lang=en#select1=0&select2=0

In light of the above, the Chamber agrees that HKEX needs to set its listing requirements of 18C at a competitive level whilst maintaining quality. We recommend that for commercial companies with sales of HK$250 million, the market capitalisation at listing should be adjusted to HK$5 billion. This implies a price-to-sales multiple of 20 times. As shown in Appendix 1, of the eleven companies that listed on STAR Market between 2019 and 2022, the price-to-sales multiples ranged from 7.2 times to 40.2 times, with a median of 20.4 times. Setting the multiple at 20 times allows Hong Kong to capture companies in the upper half of the market.

For the New Generation Information Technology sector, we expect companies seeking a listing would be in operation and revenues-generating, as we have seen in the case of Shanghai, whereas companies in the other identified specialist sectors, where a much higher level of Capex and R&D is required, are more likely to seek listing at pre-commercial stage. For these companies, we do not object to setting the required market capitalisation at the proposed HK$15 billion level.

Third Party Investment

Another issue we would like to bring up is the Third-Party Investment Requirement. The proposed requirement for listing applicants to have two sophisticated independent investors (Pathfinder SIIs) with AUM, fund size or investment portfolio size of at least HK$15 billion (or HK$5 billion for Specialist Technology investment) is debatable as it subjects listing applicants to unfavourable pre-IPO investment terms.

The requirement gives large asset management funds or corporations an upper hand over the listing applicants in the entry price negotiation, or allowing them to impose strict investment terms, such as high profit guarantee, put-back conditions, investors protection mechanisms, to the disadvantage of the applicants. For commercial companies, their growth history and demand of their services or products are good indicators of their business viability. Some of these companies may have already been operating for a number of years without such SIIs, and if they are to seek SII investments 12 months before the intended IPO as a listing prerequisite, they are in an unfavourable negotiation position.

香 港 上 市 公 司 商 會
THE CHAMBER OF HONG KONG LISTED COMPANIES

We believe that existence of Pathfinder SIIs should not be a prerequisite for listing for commercial companies. Even if in the end the Exchange deems it necessary, the level of the AUM threshold needs to be greatly reduced in order to allow more fund houses, corporations or investment entities to be qualified. This allows for example, smaller family offices, who are keen supporters of technology companies, to be able to play the role of Pathfinder SIIs and offer listing applicants more choices. Providing family offices more opportunities to participate in the market is also in line with our Government efforts of attracting them to set up in Hong Kong.

We respect HKEX's need to introduce safeguards under 18C but believe that they must not be overly restrictive otherwise they would become hurdles in the listing process and hamper the success of our Specialist Tech listing market.

The above are the main concerns of the Chamber towards this Consultation. We hope they would meet with your due consideration. We would welcome the opportunity to discuss them with you further.

Yours Sincerely
For and on behalf of
The Chamber of Hong Kong Listed Companies

[redacted]

[redacted]

Appendix

Unit: RMB million

Company name	Stock Code	Year of IPO	IPO MC[1]	Revenue one financial year before IPO	Implied multiplies of P/S
Enterprise Software/AI					
普元信息 Primeton	688118.SH	2019	4,126	338	12.2x
兰剑智能 Blueswords	688557.SH	2020	4,778	392	12.2x
博汇科技 Bohui	688004.SH	2020	7,202	272	26.5x
福昕软件 Fositsoftware	688095.SH	2020	14,888	367	40.5x
慧辰股份 HCR	688500.SH	2020	8,097	383	21.2x
开普云 Kaipuyun	688228.SH	2020	6,046	297	20.4x
步科股份 Kinco	688160.SH	2020	4,792	343	14.0x
燕麦科技 Yanmade	688312.SH	2020	8,778	268	32.8x
品茗股份 Pinming	688109.SH	2021	4,866	380	12.8x
容知日新 RONDS	688768.SH	2021	3,513	264	13.3x
格灵深瞳 DeepGlint	688207.SH	2022	6,929	294	23.6x