

Allianz Global Investors Asia Pacific Limited

23 March 2018

Corporate and Investor Communications Department
Hong Kong Exchanges and Clearing Limited
12/F, One International Finance Centre
1 Harbour View Street
Central
Hong Kong

By email to: response@hkex.com.hk

Re: Emerging and Innovative Companies CP

Consultation Paper:

A Listing Regime for Companies from Emerging and Innovative Sectors

Response by Allianz Global Investors

Allianz Global Investors (AllianzGI) welcomes the opportunity to respond to the public consultation on a Listing Regime for Companies from Emerging and Innovative Sectors. The views expressed in this document represent our position as an investment manager and an investor in companies listed on the Hong Kong Stock Exchange.

Allianz Global Investors is a diversified active investment manager, managing EUR 498 billion¹ in assets for individuals, families and institutions around the world. We invest for the long term across a range of different investment strategies, and pay close attention to growth prospects, return on capital, good governance, market positioning and quality of franchises of companies we invest in. Consistent with our investment philosophy, we routinely engage in dialogue with investee companies. Our investment views are influenced by the outcomes of these engagements and are linked organically to the proxy voting process, forming a consistent stewardship approach.

General comment

AllianzGI is not supportive of any structures that allow control over publicly listed companies which is disproportionate to the economic interests and cash flow rights of investors. Consistent with our response to the HKEX consultation on its "New Board Concept Paper" in 2017, we do not support the proposal to

¹ As of December 31, 2017.

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allow listing of companies with Weighted Voting Rights structures on the Main Board of Hong Kong Stock Exchange.

It is our view (based on many years of experience of our investment professionals) that controlling interest is much more likely to deliver expected returns to minority shareholders where the economic interests of majority and minority shareholders are aligned and the investment risk is allocated proportionately - i.e. through adherence to the "one share, one vote" principle.

Furthermore, we believe that the definition of "good quality" company must include equal rights for and the alignment of interests of all shareholders - companies unable to pass this basic test will always be seen as a higher risk investment.

In this context, we note that there is no strong evidence that WVR structures in high growth/innovative sectors provide companies with a better environment for long-term planning and execution (with much academic research suggesting otherwise). Importantly, while WVR do not guarantee positive outcomes for minority shareholders, they significantly reduce their ability to address any misalignment of interests that may occur over time and deny investors the tools they can use to put things right if they go wrong.

We have reviewed HKEX's proposals as regards the qualifications for listing of WVR-structured companies and the safeguards designed to protect investors. While we commend HKEX's attempts to find solutions that would make investment in companies with non-standard governance features less risky for investors, we remain skeptical as to whether the proposed measures are sufficiently robust to offer an appropriate protection to minority shareholders.

We also note that some of these criteria/safeguards rely substantially on the judgement of and enforcement by HKEX, which is not very reassuring given the conflicts of interests arising from the stock exchange's dual role as a standard setter/regulator and a commercial entity.

Arguably, it is the commercial considerations that are driving the current "race to the bottom" among stock exchanges, HKEX including, who appear increasingly under pressure to relax standards and weaken investor protections in order to attract more listings from companies. It is of grave concern to us as an investor that companies should be allowed to have access to lower cost capital through public equity markets without upholding high standards of governance and taking on responsibilities that serve and protect the interests of investors in public markets.

Biotech Companies

We are supportive of the proposals related to listing of early stage biotech companies.

Issuers with WVR Structures

Our comments on specific proposals concerning qualifications and safeguards to be applied to new listings of WVR-structured companies are below.

Suitability for listing: It is not clear from the consultation paper what will happen in instances where a WVR-structured company that was originally considered suitable for listing based on the "innovative"

nature of its business, ceases to be seen as innovative, i.e. when other companies adopt a similar business model and technology. Will the HKEX require that such a company abolish its WVR structure or be delisted? How often will business models and technology used by WVR-structured listed companies be assessed by the HKEX? These provisions need to be built into the listing rules as time-span of "innovation" is getting increasingly shorter and many companies will likely cease being "innovative" in a few years following the listing.

External validation: HKEX must define what a "meaningful" third party investment is. We also believe that the 6-month period within which a sophisticated third party investor is required to retain an aggregate 50% of their investment is too short and a period of 2 to 3 years would be more appropriate. Same holding period should apply to a parent company, where a new issuer is a spin off.

Minimum and maximum economic interest at listing: The control offered by WVR-structures should reduce proportionately to any reduction in an underlying economic interest of WVR beneficiaries after listing.

Ongoing requirements for WVR beneficiaries: The restrictions on WVR beneficiaries' ability to pass the control to another party or to allow the WVR-structure to outlive the founder-directors of innovative companies is a welcome development.

Nevertheless, we would prefer to see a clear sunset provision for any WVR structure. Any such sunset provision should be arbitrary and no longer than 5 years from the IPO date or departure of the management team at the IPO, whichever is shorter.

Protecting non-WVR shareholders' rights to vote: A proposal to allow non-WVR shareholders to cast at least 10% of the votes that are eligible to be cast on resolutions at general meetings makes no difference to the outcome of any such vote and offers no protection to non-WVR shareholders - it is a meaningless provision. As a minimum, non-WVR shareholders must have sufficient voting power to be able to block special resolutions at general meetings, which require 25% of voting rights.

The matters where decisions may only be made on a one-share one-vote basis should also include:

- Approval of capital issuance/repurchase authorities
- The schemes of arrangement or reconstruction
- Any matters requiring the passing of a special resolution
- Any instances where shareholder approval is required under the Listing Rules for "connected transactions" and substantial acquisitions/disposals and other material transactions.

Grandfathering: The ongoing obligations should apply to all companies with WVR structures, if allowed to the Main Board. A transition period should be allowed.

Corporate WVR beneficiaries: Corporate entities should not benefit from the WVRs. Where high growth/innovative companies are a spin-off from the parent company, the parent company should be incentivized to retain a substantial interest in the business and control the spin-off via economic interest rather than WVRs.

Secondary Listings of Qualifying Issuers

Secondary Listing of Qualifying Issuers: Overseas Issuers should only qualify for a secondary listing on the Main Board of HKEX under concessionary route if the rules and regulations in their home jurisdictions and/or primary listing jurisdiction require governance standards and offer protections to investors that are equivalent or superior to those required under the HKEX Listing Rules. HKEX should issue a comprehensive guidance as regards home/listing jurisdictions and classifications of issuers that would be allowed to follow a concessionary route in Hong Kong.

Where an issuer is exempt from the rules and regulations of their primary listing market, they should only be allowed to list in HK under the dual-primary listing route that is subject to all requirements in Hong Kong (e.g. an issuer listed in the US under the "Foreign Private Issuer" classification is exempt from many rules applied to domestic US companies - such a company should not be allowed to list under the concessionary route).

Automatic waivers: Automatic waivers under HKEX rules with regard to requirements concerning connected transactions, notifiable transactions and the Corporate Governance Code should only be granted where the rules and regulations in the primary listing jurisdictions are equivalent to those in Hong Kong and already offer equivalent protections to investors. Where rules and regulations in the primary listing jurisdictions are weaker than those in Hong Kong in terms of investor protection mechanisms, automatic waivers should not be applied

VIE structures: Please see our comment on Grandfathering of existing issuers with WVR structures. We agree that a legal opinion confirming that the VIE structure complies with PRC laws, rules and regulations is essential.

Foreign Private Issuers: Companies exempt from more rigorous US obligations under their Foreign Private Issuers status should not be automatically allowed a concessionary route to secondary listing in Hong Kong. A concessionary route may be granted if they can prove that their governance standards and investor protection mechanisms - all enshrined in the articles of incorporation or legal requirements in the home jurisdiction - are equivalent or superior to those required by HKEX. Otherwise, such companies should apply for a dual-primary listing and meet the requirements of HKEX Listing Rules. A requirement to disclose differences between Hong Kong requirements and company practices is not sufficient to protect investors (particularly non-professional retail investors).

WVR companies: All overseas companies with a WVR structure seeking secondary listing under the concessionary route in Hong Kong should satisfy all requirements for WVR-structured companies on listing and comply with all ongoing WVR safeguards after listing. These safeguards should apply to all companies, including Non-Greater China Issuers and Grandfathered Greater China Issuers, without exception.

Migration of the bulk of trading to Hong Kong: Should the bulk of trading in shares of companies migrate from the primary listing market to Hong Kong, the companies should be considered as dual-primary listed and all HKEX rules and regulations for dual-primary listed companies, including all the respective safeguards for WVR-structured companies, should apply without exceptions. Such companies should be given an appropriate grace period to adjust to the new regime.

Takeovers Code: The Code on Takeovers and Mergers and Share Buy-backs should apply to all companies listed on HKEX Main Board without exceptions.

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We note that the HKEX proposals come at a time of heightened attention to investors' role as stewards of the companies they invest in with the goal of better aligning incentives between long-term investors and corporate issuers. WVR structures and other concessions that reduce shareholder rights and undermine investor protections are not conducive to greater stewardship by investors as they restrict the ability of shareholders to hold management to account, and prevent the market for corporate control to act as a disciplining hand on management, thus effectively disenfranchising external shareholders and preventing them from fulfilling their commitment to act as good stewards on behalf of their clients.

AllianzGI believes that the proposals outlined in the consultation paper threaten the quality of Hong Kong's equity market, whereby any benefits will likely prove short-lived and be enjoyed by a relatively small group of issuers and intermediaries, while the costs will be long-term and damaging to the overall market, with negative externalities both locally and regionally.

We hope our comments are helpful. Should you have any questions or need further information, please do not hesitate to contact us.

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