HKEX New Board Concept Paper

August 2017

Potential alternatives to the New Board

- **IF** the three topics raised in the New Board Concept Paper can be addressed without a new board, than a new listing rule chapter designed for new economy companies, similar to that of the mining companies or a broad based guidance statement, similar to that of the infrastructure projects under Belt and Road initiative will be more desirable

- A new chapter or guidance statement set up under the framework and auspice of existing Main Board listing rules will ensure market integrity and no implied prejudice to early stage/ pre-revenue companies

- The drafting of a new chapter or guidance statement will be faster than setting up of the New Board

- Given most of the companies that employ a dual-class share structure will likely fall under the definition of ”new economy” sectors, one potential possibility is to allow dual-class share structure under the “new economy chapter” as well as to the companies that are already listed on recognized global exchanges – e.g. NYSE and NASDAQ

- Possibly to use the U.S. JOBS Act as an example on defining who can qualify under the new chapter/ guidance statement – using financial metrics (revenue less than US$1 billion in the case of JOBS Act) as opposed to the judgement call of whether the applicant is a ”new economy” company

    - Eliminating the subjective nature of whether the application is “new economy”

    - Allow the listing process to be a combination of regulatory support for entrepreneurs (pathway for early stage/ pre-revenue companies across all industries to go public) and market demand (ability to achieve an US$75 million in listing market cap)

Potential additional risk warning measures

Singapore example

- Additional risk warning page on the inherent riskier nature of dual-class share structure, early stage and R&D companies can be added by issuer that takes advantage of the New Board
- E.g. the Monetary Authority of Singapore (“MAS”) requires additional risk warning if an issuer has certain aspect that it deems necessary to be highlighted to potential Singapore investors
- Issuer will be required to attach an additional “risk warning cover” to the front of the Preliminary Prospectus – before the actual cover, highlighting the nature of the risk and where to look for info
- There is also statement at the bottom implying investor acknowledgment of the risk by subscribing to the shares
- MAS regulations only require the issuer to use the additional risk warning page with domestic Singapore investors. Global investors will receive copies without the additional warning page
- To note is that U.S. listing rules in fact allow for less disclosure if an issuer falls under JOBS Act – although the issuer will require to highlight the associated risks to investors that they are filing under the JOBS Act

You should be aware of certain terms of the [redacted] Corporation Limited (“[redacted]”) transaction, which is described in “*Our History and Development—*[redacted]”.

You will suffer significant dilution to your shareholding if the [redacted] (as defined herein) we have granted, which allows the counterparty to receive our ordinary shares (“Shares”) at a discount to the Offering Price (as defined herein), is exercised.

We have entered into an agreement to issue certain Convertible Bonds (as defined herein) to [redacted]. [redacted]

[redacted]

The value of your Shares may decline if our [redacted] is affected due to [redacted].

[redacted] See “*Risk Factors—Risks Relating to Our Business—*[redacted].

BY SUBSCRIBING FOR OUR SHARES, YOU WILL BE DEEMED TO HAVE APPROVED THE ENTRY INTO THE [redacted] TRANSACTION (INCLUDING THE GRANT OF [redacted] AND THE [redacted] DESCRIBED ABOVE).

Potential additional risk warning measures (cont'd)

U.S. retail account option trading example

- While option trading is open to retail investors in the U.S., retail brokerage accounts are not automatically given the options buying/ selling feature (similar case for account margin feature)

- Retail investors are required to fill out specific option agreement and acknowledge review and understanding of option specific risks before the account's option trading feature is activated

- Option trading feature is then granted in four/ five levels – varies between brokers and depending on the account owner's experience and asset level. For example, Fidelity Investments, one of the largest retail brokerage in the U.S., has five levels of option trading approval:

  - **Level 1:** Covered call writing of equity options

  - **Level 2:** Level 1, plus purchases of calls and puts (equity, index, currency and interest rate index), writing of cash covered puts, and purchases of straddles or combinations (equity, index, currency and interest rate index). Note that customers who are approved to trade option spreads in retirement accounts are considered approved for level 2

  - **Level 3:** Levels 1 and 2, plus spreads, covered put writing (selling puts against stock that is held short) and reverse conversions of equity options

  - **Level 4:** Levels 1, 2, and 3, plus uncovered (naked) writing of equity options, uncovered writing of straddles or combinations on equities, and convertible hedging

  - **Level 5:** Levels 1, 2, 3, and 4, plus uncovered writing of index options, uncovered writing of straddles or combinations on indexes, covered index options, and collars and conversions of index options

- SEHK can require similar acknowledgement of risks from retail investors who are interested in investing in New Board listed companies – brokers can collect risk acknowledgement form prior to activating account for stock purchase

  - Potentially approval can be in levels based on total allowed investment amount of New Board companies – however, any such limits again will imply a "sub par" nature of the New Board companies. Sound arguments will be needed as to why a R&D based biotech company that follows U.S. FDA process and had its technology reviewed by peers is riskier than that of a mountain highway concept project that only has the backing of local government (listed under Belt and Road financial requirements waiver)

Further thoughts on addressing Group II companies funding needs

- U.S.'s JOBS Act and Regulation A+ can serve as case study for helping younger companies access capital. In an effort to ease regulatory burdens on younger companies and facilitate capital formation, President Obama enacted the Jumpstart Our Business Startups (JOBS) Act in 2012. Under the JOBS Act, an "emerging growth company" ("EGC") can benefit from certain IPO listing rules specifically designed for EGCs and may choose to take advantage of exemptions from various reporting requirements applicable to other public companies. EGC is defined as an issuer (both domestic and foreign) with total gross revenues of less than US$1 billion during its most recently completed fiscal year i.e. EGCs are defined by financial metrics and not industry

- JOBS Act also amended regulations for private placements and crowdfunding (Regulation A+). Under the U.S. Securities Act of 1933, when a company offers or sells securities to potential investors, it must either register the offer and sale (i.e. go through the IPO process) or rely on an exemption from registration that permits unregistered public offerings (Regulation A)

  - Regulation A+ allow unregistered public offering of up to US$50 million of securities within a 12-month period. The companies conducting such offerings are required to file annual audited financial statements with the SEC and adopt additional requirements and conditions that the SEC determines necessary

  - Regulation A+ therefore is a less onerous way for private companies to raise smaller amount of private capital while at the same time providing safeguard to investors by requiring companies to file audited financials and certain documents

- There can be a more comprehensive approach to the Private Market than currently proposed in the Concept Paper incorporating some of the JOBS Act and Regulation A+ features

  - If investor matching service is provided, then Private Market can be a platform that allows for private companies to raise up to [HK$45] million within a 12-month period from professional investors under a certain set of SEHK "light-touch" rules that helps govern transparency of the process and exert certain amount of investor safeguard

  - However, setting up a full fledge Private Market with safeguard and services will certainly take time and require additional management bandwidth that SEHK might not be able to fill immediately

Specific issue: amount raised at IPO for early stage/ pre-revenue companies are generally too small for 100 professional investors

Selected precedent U.S. biopharma IPO (US$mm unless otherwise shown)

Pricing Date	Issuer	Crossover round	Pre-$ at IPO ($mm)	Amount raised ($mm)	Post-$ at IPO ($mm)	Step-up from prior round	Current mkt cap ($mm)	File / Offer	Offer / current	Pre-IPO cash ($mm)	Insider participation	Phase at IPO	Lead drug indication	Next Milestone: Event	Next Milestone: Time to (months)
05/16/17	G1 Therapeutics	✓	$355	$117	$472	1.7x	$585	(6%)	24%	$38	34%	P II	Oncology	PII open label data	1 month
05/04/17	Ovid	✓	294	75	369	0.8x	340	(6%)	(8%)	52	27%	P II	Rare neurological disorders (Angelman and Fragile X)	Initiate P II clinical trials	6 months
05/03/17	UroGen Pharma		97	67	164	-	196	-	26%	21	34%	P II / III	Urological pathologies focused on uro-oncology	P II data / Initiate P IIb	12 months
05/03/17	biohaven	✓	414	194	608	1.8x	736	13%	26%	62	32%	P II / III	Neurological diseases (migraine therapy and ataxias)	Topline Ph III data	9 months
04/27/17	zymeworks		266	64	330	-	234	(10%)	(28%)	17	66%	P I	Biotherapies targeting the HER2 protein in cancer	P I data	12 months
04/12/17	Tocagen		90	98	188	-	318	(9%)	61%	8	-	Ph II / III	Gene therapy for brain cancer	P II data	12 months
01/26/17	Jounce	✓	397	117	514	1.4x	549	14%	7%	217	10%	P I / II	Immunotherapy cancer treatments	P I / II proof of concept	6 months
01/25/17	AnaptysBio	✓	212	86	298	1.7x	453	-	50%	51	40%	P II	Inflammatory diseases (peanut allergy, psoriasis)	P II data	6 months
01/25/17	ObsEva	✓	348	97	445	2.8x	200	-	(55%)	39	46%	P II	Women's health (endometriosis and uterine fibroids)	P II data	12 months
10/26/16	Myovant Sciences		686	218	904	-	719	11%	(9%)	-	14%	P II	Uterine Fibroids, Endometriosis, Prostate Cancer	Initiate P III clinical trials	6 months
10/25/16	Ra Pharma	✓	188	105	293	1.9x	463	-	58%	-	21%	P I	Paroxysmal Nocturnal Hemoglobinuria	Initiate P II clinical trials	6 months
10/18/16	CRISPR	✓	495	62	557	-	588	(13%)	4%	247	63%	Pre-IND	Orphan / Gene Therapy	Initiate clinical trials	12 months
09/22/16	AC Immune	✓	543	76	619	-	524	(8%)	(16%)	99	32%	P II / III	Alxheimer's Disease (AD)	Initiate P II / III clinical trials	6 months
09/20/16	novan		123	52	175	0.3x	69	(8%)	(60%)	20	40%	P II / III	Dermatological conditions	File NDA	12 months
08/10/16	Protagonist Therapeutics	✓	106	90	196	1.4x	192	-	(5%)	29	44%	P I / II	Gastrointestinal Disease (IBD)	Initiate P II clinical trials	4 months
07/26/16	Kadmon		463	75	538	-	141	(33%)	(77%)	9	53%	P I / II	Autoimmune, fibriotic, neurogenerative diseases	Initiate clinical trials	6 months
07/19/16	AUDENTES	✓	240	75	315	0.9x	416	-	0%	80	22%	Pre-IND	Orphan / Gene Therapy	Initiate clinical trials	12 months
06/29/16	Syros	✓	235	58	292	1.2x	385	(17%)	18%	62	70%	P I / II	Gene control	Initiate P II clinical trials	6 months
06/21/16	SELECTA	✓	180	70	250	0.7x	280	(7%)	8%	26	57%	P I / II	Immunotherapy	Initiate P II clinical trials	6 months
06/01/16	CLEARSIDE	✓	87	57	144	0.6x	194	(53%)	9%	16	54%	P III	Eye Disease	Preliminary P III data	12 months
05/25/16	REATA		176	70	246	-	571	(27%)	132%	42	48%	P III	Pulmonary hypertension	Preliminary P III data	12 months
05/18/16	Merus	✓	99	61	160	0.6x	301	(33%)	55%	37	59%	P I / II	Oncology	Preliminary P I / II data	12 months
05/05/16	Intellia	✓	524	124	648	2.0x	454	6%	(30%)	76	45%	Pre-IND	Orphan / Gene Therapy	Initiate clinical trials	12 months
04/06/16	aeglea	✓	79	55	134	1.1x	48	(41%)	(64%)	33	64%	IND / P I	Oncology	Initiate clinical trials	6 months
03/22/16	CORVUS	✓	236	71	306	1.0x	207	(6%)	(34%)	4	30%	P I / Ib	Oncology	Initiate clinical trials	6 months
03/02/16	Syndax	✓	156	58	213	0.9x	228	(20%)	(14%)	86	-	P Ib / II & P III	Oncology	Data read out	6 months
02/10/16	avexis	✓	353	106	459	1.0x	2,176	-	291%	70	20%	P I	Orphan / Gene Therapy	Preliminary P I data	6 months
02/10/16	PROTEOSTASIS	✓	103	50	153	0.5x	109	(38%)	(46%)	21	40%	IND	Orphan / Gene Therapy	Preliminary P I data	6 months
02/02/16	BeiGene	✓	598	182	780	-	1,552	4%	62%	121	40%	P I	Oncology	P I data	6 months
02/02/16	editas	✓	477	109	585	1.2x	650	(6%)	(2%)	155	-	Pre-IND	Orphan / Gene Therapy	Initiate clinical trials	12 months
All deals mean			**$287**	**$91**	**$379**	**1.2x**	**$463**	**(10%)**	**13%**	**$58**	**37%**				
All deals median			**$238**	**$75**	**$311**	**1.1x**	**$363**	**(6%)**	**2%**	**$39**	**40%**				
2017 deals mean			**$275**	**$102**	**$376**	**1.7x**	**$401**	**(0%)**	**11%**	**$56**	**32%**				
2017 deals median			**$294**	**$97**	**$369**	**1.7x**	**$340**	**-**	**24%**	**$39**	**34%**				
2016-2017YTD crossover rounds (median)			**$240**	**$76**	**$315**	**1.2x**	**$416**	**(6%)**	**4%**	**$52**	**40%**				
2016-2017YTD no crossover rounds (median)			**$176**	**$70**	**$246**	**0.3x**	**$234**	**(9%)**	**(9%)**	**$17**	**-**				

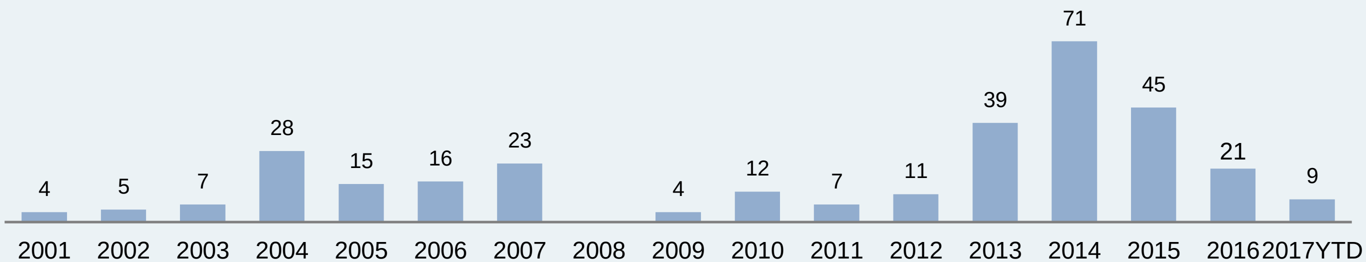
Source: J.P. Morgan. Factset as of 06/09/17, company filings, and press releases

Specific issue: amount raised at IPO for early stage/ pre-revenue companies are generally too small for 100 professional investors

Selected precedent U.S. biopharma IPO (US$mm unless otherwise shown)

Total volume

	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017YTD
Total proceeds raised ($mm)	$353	$799	$453	$1,764	$961	$1,911	$2,070	-	$1,262	$922	$506	$771	$3,174	$5,863	$4,724	$1,821	$915



Mean ($mm / %)	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016	2017YTD
Post-$ mkt cap	$415	$670	$267	$270	$224	$419	$337	$0	$764	$289	$201	$250	$291	$281	$249	$373	$371
Proceeds raised	88	160	65	63	64	119	90	0	316	77	72	70	81	81	105	86	102
File / offer	(10%)	(17%)	(10%)	(26%)	(20%)	(22%)	(15%)	-	(11%)	(38%)	(32%)	(24%)	(14%)	(13%)	(7%)	(14%)	(1%)
Offer / 1-day	12%	(5%)	0%	7%	8%	3%	6%	-	(2%)	(1%)	6%	7%	20%	13%	22%	8%	2%
Offer / 1-month	(13%)	(12%)	(12%)	7%	4%	4%	8%	-	(9%)	(3%)	3%	13%	37%	24%	27%	20%	26%

Source: J.P. Morgan. Company filings, Dealogic, Factset as of 06/09/2017 for deals >$50mm

Specific issue: amount raised at IPO for early stage/ pre-revenue companies are generally too small for 100 professional investors

Selected precedent U.S. TMT IPO (US$mm unless otherwise shown)

			Initial Public Offering				Financial metrics							Valuation					Performance		
							Revenue ($mm)			EBITDA ($mm)		Net income ($mm)									
Issuer	U.S. Issuer	Pricing date	IPO amt ($mm)	Mkt cap ($mm)	% of mkt cap	% sec	2017	2018	% gr	2018	% mar	2018	% mar	Valuation metric	Pricing Multiple	Peer multiple	IPO discount	A/W/B	File/ offer	Offer/ 1-Day	Offer/ Current
WideOpenWest	✓	05/24/17	$310	$1,454	21%	-	$1,196	$1,235	3%	$479	39%	$103	8%	EV/EBITDA (2018)	7.6x	8.0x	(5%)	B	(19%)	(3%)	3%
Appian	✓	05/24/17	86	716	12%	-	157	188	20%	(19)	(10%)	(34)	(18%)	EV/Rev (2018)	3.6x	4.8x	(25%)	W	-	25%	52%
SMART Global	✓	05/23/17	67	228	29%	-	755	862	14%	110	13%	61	7%	P/E (2018)	3.9x	14.3x	(73%)	B	(21%)	22%	39%
Cloudera	✓	04/27/17	259	1,955	13%	-	338	429	27%	(99)	(23%)	(111)	(26%)	EV/Rev (2018)	4.8x	6.1x	(21%)	A	15%	21%	16%
Carvana	✓	04/27/17	225	1,984	11%	-	889	2,438	174%	9	0%	(22)	(1%)	EV/EBITDA (2019)	7.3x	15.6x	(53%)	W	-	(26%)	29%
Yext	✓	04/12/17	133	940	14%	-	165	217	32%	(34)	(16%)	(39)	(18%)	EV/Rev (2018)	4.6x	5.5x	(16%)	A	22%	22%	22%
Netshoes		04/11/17	149	557	27%	-	2,027	2,444	21%	36	1%	(52)	(2%)	EV/Rev (2018)	0.6x	1.0x	(38%)	W	(5%)	(11%)	(0%)
Okta	✓	04/06/17	215	1,543	14%	-	227	318	40%	(73)	(23%)	(85)	(27%)	EV/Rev (2018)	5.5x	7.1x	(23%)	A	21%	38%	56%
Alteryx	✓	03/23/17	145	788	18%	-	118	163	37%	(20)	(12%)	(24)	(15%)	EV/Rev (2018)	4.2x	5.9x	(29%)	W	8%	11%	34%
Mulesoft	✓	03/16/17	254	2,142	12%	-	266	361	36%	(50)	(14%)	(54)	(15%)	EV/Rev (2018)	5.9x	6.5x	(9%)	A	31%	46%	45%
Presidio	✓	03/09/17	263	1,240	21%	-	3,035	3,207	6%	258	8%	135	4%	P/E (2017)	11.4x	15.4x	(26%)	W	(7%)	2%	7%
Snap	✓	03/01/17	3,910	19,673	20%	28%	1,159	2,634	127%	(364)	(14%)	(735)	(28%)	EV/Rev (2018)	7.8x	7.7x	1%	A	13%	44%	3%
Mean			$501	$2,768	18%		$861	$1,208	45%	$19	(4%)	($71)	(11%)				(26%)		5%	16%	25%
Median			$220	$1,347	16%		$546	$645	29%	($20)	(11%)	($37)	(15%)				(24%)		8%	22%	29%

Source: Dealogic, FactSet, Wall Street Research, and Company filings as of 06/16/17 J.P. Morgan.
Note: Market cap represents basic market cap at pricing; Yext and Cloudera FYE Jan 31 used as proxy for CY numbers (e.g., FY 2018 shown as CY 2017); SMART Global FYE metrics shown (FYE of Aug 31); Shading indicates J.P. Morgan bookrun IPOs

Case study: institutional investors at time of IPO for the two China healthcare companies – substantially lower than 100

BeiGene Ltd	
Offering date:	2 February 2016
Offering amount (with shoe):	US$182m
Market cap at IPO (fully diluted):	US$756m

Holders

Holder	Mar-31-2016 Common Stock Equivalent Held
Baker Bros. Advisors, LLC	8,090,422
Oyler, John V. (Founder, Chairman and Chief Executive Officer)	5,989,167
Hillhouse Capital Management, Ltd.	3,055,199
Merck & Co., Inc. (NYSE:MRK)	2,429,197
Fidelity Investments	1,717,060
CITIC Private Equity Funds Management Co., Ltd.	1,507,327
Wang Ph.D., Xiaodong (Co-Founder, Chairman of the Scientific Advisory Board and Director)	1,273,362
Glazer Esq., Donald W. (Independent Director and Chairman of Nominating & Corporate Governance Committee)	586,900
T. Rowe Price Group, Inc. (NasdaqGS:TROW)	452,700
Tavistock Life Sciences	416,879
Temasek Holdings (Private) Limited	380,000
Rock Springs Capital	225,000
TD Asset Management, Inc.	202,620
Venrock	170,000
QVT Financial LP	170,000
RA Capital Management, LLC	170,000
Indus Capital Partners, LLC	170,000
Prince Street Capital Management LLC	135,400
Manulife Asset Management	127,552
Tekla Capital Management LLC	116,707
Light Street Capital Management, LLC	100,000
Visium Asset Management, LLC	99,670
Brown Advisory Incorporated	99,652
Pine River Capital Management L.P.	64,709
Millennium Management LLC	64,087
Stanford Management Company	50,000
Arrowpoint Asset Management, LLC	47,000
Casdin Capital, LLC	32,500
Goldman Sachs Group, Investment Banking and Securities Investments	27,529
Dafna Capital Management LLC	20,000
Ecor1 Capital, LLC	15,766
Yang M.D., Ph.D., Jason (Head of Clinical Development)	15,380
The TCW Group, Inc.	13,177
Yuan M.D., Ruirong (Former Chief Medical Officer and President of Global Clinical Research & Development)	9,997
Morgan Stanley, Investment Banking and Brokerage Investments	8,457
Landscape Capital Management, LLC	6,900
Liang Ph.D., Heng (Chief Financial Officer and Chief Strategy Officer)	4,998
HSBC Global Asset Management (UK) Limited	4,862
BlackRock, Inc. (NYSE:BLK)	4,286
Martin Currie Limited	3,100
Bank of America Corporation, Asset Management Arm	2,593
Baillie Gifford & Co.	1,850
Bessemer Investment Management LLC	1,183
UBS Asset Management	887
Tower Research Capital LLC	149
Catalyst Capital Advisors LLC, Asset Management Arm	85
Citigroup Inc.,Banking and Securities Investments	2

Hutchison China MediTech Ltd	
Offering date:	17 March 2016
Offering amount (with shoe):	US$116m
Market cap at IPO (fully diluted):	US$1.6bn

Holders

Holder	Mar-31-2016 Common Stock Equivalent Held
CK Hutchison Holdings Limited (SEHK:1)	36,666,667
Mitsui & Co. Ltd. (TSE:8031)	3,214,404
M&G Investment Management Limited	1,100,000
Hogg BSc,MBA, Tom Tang (Chief Executive Officer, Executive Director and Member of Technical Committee)	1,106,482
Indus Capital Partners, LLC	651,171
Hargreave Hale Limited, Asset Management Arm	587,500
Capital Group International Inc.	387,646
Cheng BEc, CA, Chig Fung (Chief Financial Officer and Executive Director)	256,146
Schroder Investment Management (Singapore) Ltd	164,526
To BSc, ACGI, MBA, Simon (Executive Chairman, Chairman of Remuneration Committee and Member of Technical Committee)	180,000
Allianz Asset Management AG	166,200
Howell MA, MBA, HonFCGI, Michael W. D. (Independent Non Executive Director, Chairman of Audit Committee and Member of Remuneration Committee)	153,600
SVM Asset Management Limited	139,227
Polar Capital Holdings plc (AIM:POLR)	108,450
Nikko Asset Management Co., Ltd.	105,000
Standard Life Investments Limited	83,295
Shih BSE, MA, EdM, Solicitor, FCIS, FCS(PE), Edith (Company Secretary and Non-Executive Director)	80,370
Baillie Gifford & Co.	-
T. Rowe Price Group, Inc. (NasdaqGS:TROW)	50,000
Jabre Capital Partners S.A.	135,000
Prince Street Capital Management LLC	43,850
Folger Hill Asset Management LLC	-
Nash BSc, MBA, ACGI, Christopher J. (Senior Independent Director, Member of Audit Committee and Member of Remuneration Committee)	36,434
Societe Generale, Securities Investments	8,678
Royal Bank of Scotland PLC (London Branch), Asset Management Arm	30,800
AllianceBernstein L.P.	30,000
BlackRock, Inc. (NYSE:BLK)	12,925
Wellington Management Group LLP	22,640
Schonfeld Strategic Advisors LLC	27,441
Prudence Investment Management (Hong Kong) Limited	20,000
Teachers Insurance and Annuity Association of America - College Retirement Equities	179,349
Oppenheim Kapitalanlagegesellschaft mbH	15,875
Millennium Management LLC	16,287
Petercam Institutional Asset Management (Luxembourg) SA	15,000
Victory Asset Management S.A.	13,500
Gratry & Company, LLC	-
Wu Ph.D., M.B.A, Zhenping (Senior Vice President of Pharmaceutical Sciences)	5,000
Huang BA, BM, BCh, Ph.D., DM, FSB, DSc, Christopher (Independent Non-Executive Director, Chairman of Technical Committee and Member of Audit Committee)	2,475
Northern Trust Global Investments	1,822
Tower Research Capital LLC	630
Catalyst Capital Advisors LLC, Asset Management Arm	115
Assetplus Investment Management Co., Ltd.	100
Merrill Lynch & Co. Inc., Banking Investments	85
Marshall Wace LLP	35,157
Henderson Global Investors Limited	20,000
UBS Asset Management	1,237
Deutsche Bank, Private Banking and Investment Banking Investments	224,802
Morgan Stanley, Investment Banking and Brokerage Investments	5
Nomura Holdings Inc, Securities & Investment Arm	8,600
Nine Masts Capital Limited	5,000
LMR Partners LLP	50,197

Source: Capital IQ. Highlighted rows denote founders, pre-IPO investors and insiders

Overview

Providing listing pathway for WVR and early stage/ pre-revenue* companies is overall positive and will encourage investments in R&D, innovation and tech

- Pathways for WVR/ dual-class share structure and early stage/ pre-revenue companies to list in Hong Kong are much needed
- Servicing the capital needs of new economy companies (many are set up with dual-class share structure) at different stages of their development can lead to great business and capital flow for SEHK. Global investor interests in new economy companies are well highlighted in the New Board Concept Paper
- IPO is an important route of capital formation for R&D intensive pre-revenue companies to meet their funding needs
- It will be crucial to success for Hong Kong government's current push to promote investments in R&D and goal to diversify Hong Kong's economy to innovation and tech
- Three main topics were raised in the New Board Concept Paper:

  1. WVR/ dual-class share structure
  2. Early stage/ pre-revenue company listing
  3. Private company market platform

  Along with the separate GEM Consultation Paper there are four topics which can potentially be addressed separately independent from each other or together in an holistic manner
- If the three topics raised in the New Board Concept Paper need to be addressed concurrently and taking into account historical debate of the topics, then a New Board maybe the "simplest" (though not easiest) solution
- However, the proposed New Board framework under the current New Board Concept Paper poses a few challenges for early stage/ pre-revenue companies to effectively use the new pathway

Note: It is assumed that the term "pre-profit company" used throughout the New Board Concept Paper is meant to be interchangeable with the term "pre-revenue company" – a company can be "pre-profit" and still meet the existing Main Board listing criteria using Market Cap rules; as such will not need to consider the New Board. A "pre-revenue" company is by definition "pre-profit"; hence a broader definition. There is no existing pathway for "pre-revenue" company to list on SEHK, which is the genesis of the need for the New Board discussion

Comments on the New Board

- The priority of SEHK (and SFC) should be the **integrity** of the market – listing standards **need not** and **should not** be lowered to accommodate dual-class share structure and early stage/ pre-revenue companies

- Arguably dual-class share structure is a philosophical debate on corporate governance as dual-class share **physically** poses no specific problem in the context of trading platform. Global markets have shown that a company with dual-class share structure **physically trades** the same as those without (e.g. Facebook vs. General Electric, both followed all SEC and exchange rules and are extremely liquid.)

- In the purest sense, SEHK's function is to provide a platform for trading and to maintain the integrity of such market. It is investors who should decide if they want to invest in a dual-class structure company based on their own philosophical view on corporate governance. If investors do not believe in the corporate governance structure of a company then they will not invest, as such there will be no demand for the company's shares and the company's IPO will not be successful

  - Wuxi Biologics recently listed on SEHK with an imbedded dual-class share structure was one of the most successful IPOs in 2017 with over 35x retail subscription

- It is arguable whether **Hong Kong** as a listing location (with SFC and SEHK as proxies) needs to take a stand for this specific philosophical debate of one-share-one-vote and not the other perceived "investor protection" debates such as mandatory minimum 30% female Board of Directors ratio or a stricter Environmental, Social and Governance rules and compliance. Thus far no major global investors nor issuers have proclaimed that they will move more funds to Hong Kong or list in Hong Kong because Hong Kong stands for one-share-one-vote? Similarly NYSE, NASDAQ and SEC are not taking a stand on the issue

- Whether any company's share will be eligible for index inclusion is the decision of the index providers, which are all commercial organizations; index criteria also changes based on the time and investor demand. SEHK's decision for dual-class listing should be independent from the action of the index providers that have no formal relationship with SEHK or SFC

  - S&P and FTSE Russell both recently announced decisions to partially or fully exclude companies with dual-class share structures from their indices – S&P will apply the criteria to new companies only. While market constituents of all FTSE Russell indices must have greater than 5% of the company's voting rights held by unrestricted shareholders. Existing constituents will need to comply by September 2022. These changes highlight the growing roles of investors and index providers in shaping governance standards – but the changes were at the behest of INVESTORS not action from regulators nor exchange operators

- Not permitting dual-class share structure is inconsistent with other major global exchanges and unnecessarily hindered SEHK's ability to attract good global issuers. Most importantly, inclusion of dual-class shares should not impact the overall functioning of the Hong Kong market. Investors should indeed have their own rights to decide whether to invest in a dual-class share

Comments on the New Board (cont'd)

- Listing standards, however, will directly impact the overall functioning of the market. If standards are not upheld then the market and Hong Kong's strength as a well-functioned capital market will be negatively affected; e.g. GEM board as it is right now

- The New Board PRO's proposed ""lighter touch" approach to initial listing requirements" and low minimum listing market cap lowered the listing standards and positioned the New Board PRO to below GEM – given the broad market view that GEM listed companies are second tier, and even those companies will require a full listing process

  - The implied assumption is that early stage/ pre-revenue companies are sub par and unable to meet the rigor of an IPO process

- There are many "unicorn" – private companies with valuation above US$1 billion, especially in new economy sectors of technology and healthcare. The unicorn companies will be able to meet all the **regulatory** aspect of SEHK Main Board listing requirements most often than not, the only listing rule they are unable to meet is the profit and financial standards requirement of rule 8.05

Comments on the New Board (cont'd)

- There are in essence **two** groups of early stage/ pre-revenue companies that the proposed New Board is trying to address. It is imperative to separate the two groups given their distinct capital needs and **market readiness**

Group I

- The more established R&D based companies, e.g. companies that are developing new fuel cells for power generators or drug for cancer treatment
- Generally have been around longer – as it often takes over ten years to develop a drug and in-depth subject knowledge to invent new technologies
- Usually led by industry veterans and experienced institutional VC/ PE investors
- The "early stage/ pre-revenue nature" to this group means the **PRODUCT** development is still in process and the main associated risks are R&D risks. They are pre-revenue as R&D intensive companies are cash-burn companies
- Higher capital needs for product research and development efforts
- Previous institutional VC/ PE rounds set valuation benchmark
- Can be companies located anywhere – e.g. a large number based in China or led by Chinese executives and investors

Group II

- The younger start-up companies
- Generally have been around for only a few years
- Usually led by less experienced team with no institutional VC/ PE support
- The "early stage/ pre-revenue nature" to this group means the **COMPANY AND PRODUCT** development are still in early stage and the associated risks are more than R&D risks
- Given young nature of the company, generally lower capital needs
- Usually raised small amount from friends and families
- Many local Hong Kong based start-ups – under the Hong Kong government's active encouragement for Hong Kong population to venture into (new economy) business. However, start-up culture is still relatively new in Hong Kong

Comments on the New Board (cont'd)

- Group I companies are market ready and often unicorn companies. If the New Board is meant to be a marquee listing venue for global new economy companies, then Group I should be the targeted issuers of the New Board. The companies will be able to meet all the **regulatory** aspect of the Main Board listing requirements most often than not, the only listing rule they are unable to meet is the profit and financial standards requirement of rule 8.05
  - Many R&D based companies have extensive regulatory filing experience working with IP offices, CFDA, U.S. FDA, and EMA etc.
- Founders and owners of Group I companies will want to have a proper IPO process to raise global institutional capital and attract good investors. Preparing a proper prospectus is a given as that is a mean to explain their technologies. The companies will want to have retail tranche for increased liquidity
  - No reputable global institutional fund managers will invest in a stock without prospectus and proper exchange vetting
- Group II companies are smaller in scale and will benefit from the lowered listing standards. They will appreciate the lowered listing expenses by not requiring a prospectus, sponsor, and public tranche. However, if a company finds the IPO process and the preparation of a prospectus onerous, then it is unlikely it will be able to handle the scrutiny of public institutional and professional investors. The company is simply **not** ready to go public in the proper sense
- By trying to accommodate the needs of both groups, the New Board has inadvertently lowered the listing standards to the lowest denominator, which in the long run may affect the overall integrity of the Hong Kong market
- Most of the Group I companies qualify to list on NYSE and NASDAQ. They will unlikely choose to list on the New Board if it is perceived as having a lower standard and for subpar companies. Only a New Board with equivalent reputation as the Main Board will attract **the best** global new economy issuers and investors
  - The lowered listing standards then lead to need to limit the investments to professional investors only which further reduces attractiveness of the New Board to proper potential issuers
- The New Board as it is proposed now may run the risks in long run to only attract the smaller companies that are not qualified for listing anywhere else – akin to Taiwan's now defunct early stage company board, TSX Venture Exchange and Singapore Catalist Board where there are in fact no institutional investors
  - Worst case scenario is that given a pathway, inexperienced management maybe persuaded by dishonest market participants that the company can go public when it is in fact not ready. Going public when not ready can also destroy a company, just as lack of capital

Proposed New Board set up

- The New Board (without tier) should be positioned as the same level as the Main Board and have the same listing requirements and governance rules as the Main Board, including the newly proposed increased market cap and float but with the addition of:

  1. Allowance for WVR/ dual-class share structure

  2. Additional qualification method for listing (e.g. a new Listing Rule 8.05(4)) that allows new economy company to list if it can achieve listing market cap of **HK$585 million/ US$75 million** – same as NYSE Business Development Companies rule and Nasdaq Global Market

     - Along with that there will need to be an expanded 8.05B to apply to new economy companies qualified under new 8.05(4) – The Exchange may accept a shorter trading record period and/or may vary or waive the profit or other financial standards requirement in rule 8.05 (add new 8.05B(4))

- Given the same Main Board rigor for IPO and governance are applied to the New Board, it should then be open to retail investors and have no separate PREMIUM and PRO tiers; i.e. just one New Board that is parallel in positioning as with the Main Board

  - View it from another angle, the proposed New Board can be a ”new tier”/ extension of the Main Board; or expanding the proposed New Board PREMIUM to include new economy early stage/ pre-revenue companies

- A New Board with equivalent listing rigor and reputation as the Main Board will attract the best issuers globally and increase the overall visibility and capital flow of SEHK

- To safeguard the application of this “new economy company listing rule”, the Listing Committee can work with an independent industry advisory board to determine if the applicant falls under the scope of “new economy.” The industry advisory board can also provide views on whether the applicant’s business pass the ”smell test” – especially for companies that are R&D and technology intensive

  - To note is verifying the validity of the applicant (i.e. the company’s business falls in the defined scope of ”new economy”) should not be interpreted as guaranteed success of the company’s technology or drug. Not all technologies and drug development will come to fruition and the success can be influenced by multitude of factors in addition to availability of capital. A mature company operating a theme park can face competition from nearby new theme park and experience business loss; while the new theme park operator can grossly misjudge consumer’s taste and failed to attract tourists to its park. Business success or failure is not unique to new economy companies

  - There should be different independent advisory board for technology and healthcare given specific knowledge of the sectors

Proposed New Board set up (cont’d)

- It is not SEHK’s responsibility to guarantee success of the New Board companies, neither does it guarantee success of the Main Board companies. However, applying Main Board level rigor of IPO review and governance on the New Board are precisely the value-added services that SEHK can provide to investors (and issuers) given the higher risks of early stage/ pre-revenue investing

- The proposed set up above will also have the benefit of simpler execution from SEHK perspective – a new board based on the existing Main Board rules but allowing VWR and adding a fourth qualification rule for new economy companies will be a much simpler task than designing a brand-new board from scratch for the case of New Board PRO

- Requiring sponsors and a proper IPO process will also ensure participation from established global investment banks, law firms and auditors. They can serve as additional check points and safeguard for quality listings. Most importantly, they are the key to bringing in reputable global investors to invest in the New Board companies

- In the U.S. market, which has the longest history for early stage/ pre-revenue company listings, good research analysts and portfolio managers in healthcare and tech sectors serve as thought leaders for investors in a more meaningful way than in less technical sectors such as consumer due to the high knowledge intensity of the sectors. They are often relied upon for their views on seemingly negative or positive news; providing thought leadership on the company and its technology’s viability – hence indirectly **share price stability**

- To ensure the long-term success of the New Board and ultimately the integrity of the market, SEHK should set up the New Board in a way that allows the creation of a proper ecosystem of marquee issuers, investors, banks, law firms and auditors. GEM board companies highlight the peril of not having top tier professional involved – extreme volatility, mostly retail investors, to the extent there are “institutional” investors, they are not the marquee global names

Thoughts on addressing Group II companies funding needs

- A vibrant private capital raising ecosystem will better serve the needs of younger Group II companies that are not ready for public market. There can be a more comprehensive approach to the Private Market than currently proposed in the Concept Paper. An effective private capital raising mechanism can alleviate the need to lower the New Board's standard and maintain the integrity of the market while protecting investors from certain risks

- However, since young start-ups are inherently riskier due to less structure and governance of the companies, it is arguable if the Private Market's potential negative headline risks to SEHK is proportional to the potential revenue gain – headline risks likely similar whether as registration platform or actual capital raising services are provided

  - Unscrupulous companies can misrepresent the "registration platform" as "listed on SEHK" to less knowing investors. If SEHK provide capital raising facilitation services hence gatekeeping and governance on the platform, that may in fact help prevent such situations

  - Any negative events from company registered on the platform can be misinterpreted as part of the overall quality of the companies listed on SEHK. As such an open-to-all registration platform may impact the perceived integrity of the market

  - Setting up a full fledge Private Market with safeguard and services will certainly take time and require additional management bandwidth that SEHK might not be able to fill immediately

- To address the social aspect of Hong Kong start-up community needs, one potential approach is to work more closely with industry associations such as HKVCA or other Hong Kong government entities such as Hong Kong Science and Technology Parks and Hong Kong Cyberport that are part of the Hong Kong government's effort to promote entrepreneurship

  - SEHK to publish a set of best practice guidelines on private capital raising on information requirements (e.g. management info memo format), documentation (e.g. shareholders' agreement key points) and settlement procedures (e.g. timeline) etc. to help facilitate private capital raising process between less experienced management team and investors. SEHK can also provide continuous reporting best practice guidelines such as requirements for semi-annual audited financials or management accounts

  - The set of guidelines and "private capital raising facilitation site" can be hosted by industry association such as HKVCA. HKVCA has a broad private investor network and has the right resources to host a private investment platform. As an investment industry organization independent from SEHK, it is understood that the platform is to facilitate private investments and NOT the implicit endorsement of SEHK. Companies and investors can have the CHOICE to follow SEHK best practice guidelines. The site can also be hosted by other Hong Kong government entities such as HKSTP/ HKC/ ITB

  - SEHK can build on the existing Road-to-IPO program and expand to guideline setting and ultimately capital raising facilitation services

Proposed New Board and Private Market positioning

- A New Board with equivalent listing rigor and reputation as the Main Board in order to attract the best new economy issuers and investors
- A vibrant private capital raising ecosystem will better serve the needs of younger companies that are not ready for public market

Open to all investors

Main Board

- Existing Main Board listing rules
- Increased minimum listing market cap of HK$500 million
- Increased minimum float at listing of HK$125 million
- Post-IPO lock-up period on controlling shareholders to remain six months

New Board

- Same Main Board listing and governance rules, including increased market cap and float but with the addition of:

1. Allowance for WVR/ dual-class share structure
2. Additional qualification method – new Listing Rule 8.05(4) that allows new economy company to list if it can achieve listing market cap of HK$585 million/ US$75 million
   - Expand 8.05B to apply to new economy companies qualified under new 8.05(4) – The Exchange may accept a shorter trading record period and/or may vary or waive the profit or other financial standards requirement in rule 8.05 (add new 8.05B(4))
   - Listing Committee + independent industry advisory board to determine qualification under new 8.05(4)

GEM Board

- New rules as proposed under GEM Consultation Paper
- Open to all small and mid cap issuers including new economy companies that can meet the listing criteria
- Post-IPO lock-up period on controlling shareholders to remain six months

Professional investors only

Private Market

- An effective private capital raising mechanism can alleviate the need to lower the New Board's standard
- In partnership with industry associations