

Webb-site responds to the HKEX proposal which further raises the barriers to entry for smaller companies on its monopoly stockmarket and reduces investor choice. Help us out and add your voice!

## The Main Board profit requirement - for whom? 14 January 2021

To: The Stock Exchange of Hong Kong Limited (**SEHK**)

This is my response to your [consultation paper](#) titled "Main Board Profit Requirement" [announced](#) on 27-Nov-2020. I'll keep this brief because, having ignored many of my previous submissions, you don't deserve much of my remaining time. I also ask any member of the investing public or market professional who agrees with this submission or has any other views, to write to you at [response@hkex.com.hk](mailto:response@hkex.com.hk) with the subject line "Profit Requirement CP", by 1-Feb-2021.

1. SEHK, as a wholly-owned by Hong Kong Exchanges and Clearing Ltd (**HKEX**, 0388), is a for-profit regulator and also has a statutory monopoly on the operation of a stock market in HK. Nobody else can set up a stock market here. You are also [exempted](#) from abusing your monopoly under the Competition Ordinance.
2. Companies, particularly smaller companies, wishing to raise public equity in HK have no other choice, short of being driven into exile on an overseas exchange. As a monopoly, you have a moral Universal Service Obligation (**USO**) to list any company that meets disclosure and governance requirements and is willing to bear the costs of being listed, including appropriate listing fees.
3. A minimum market cap has nothing to do with corporate governance. It's an artificial limit on your USO. On 15-Feb-2018 you raised the minimum market cap for new listings from HK\$200m to \$500m. At the end of 2020 [there were 779](#) Main Board stocks with market caps below HK\$500m, or 36% of all stocks.
4. Now you complain that having raised the minimum market cap, some companies are listing on P/Es of 25x the minimum profit of HK\$20m, so you want to raise that too. One misconceived regulation begets another. We have certainly seen cases of companies squeaking into the market at HK\$500m valuation and the share price promptly collapsing. Promises or indemnities may have been issued to people to take the IPO stock at the required valuation. This is a problem of your own making.
5. A minimum profit requirement has nothing to do with corporate governance and little to do with investment risk. Companies which make profits before listing can make losses afterwards. There are hundreds of Main Board companies that make a loss in any given year, some of which have made losses for several years running. You don't relegate them to GEM. They are presumably all suitable to remain Main Board listed as long as they comply with disclosure and governance requirements, and investors are free to invest in them. That's what makes a free market.
6. Both the market cap requirement and the profit requirement (or on GEM, the cashflow requirement) are simply targets for fraud or accounting manipulation.
7. You now list "[pre-revenue](#)", cashflow-negative, loss-making biotech companies on the Main Board. It has always been possible for infrastructure and mineral exploration companies to list without a profit. Why impose a cashflow or profit requirement on everyone else?
8. If public equity investors wish to invest in a small, loss-making company that may one day be a big, profitable company or may simply go bust, who are you to stop them? It's not like you don't list riskier [derivatives](#) that expire worthless on a regular basis.
9. So, scrap the market cap and profit requirements. Without that, there is little difference between the GEM and the Main Board. So merge the two, but impose the best features of both on the unified board (as we advocated in a [submission](#) on 7-Aug-2017), namely:
  - Quarterly financial reporting (as required on GEM): more disclosure for the former Main Board companies (only a few of which, including HKEX and all companies with a mainland listing, report quarterly)
  - A 3-year clean audit report before listing (up from 2 years on GEM).
  - Substantially the same management during the 3-year track record period (up from 2 years on GEM).
  - No requirement to conduct a public offering rather than just a placement. Participating in IPOs is not a human right. The Main Board requirement doesn't prevent stocks being manipulated after listing, as is shown by numerous cases. Don't confuse corporate regulation with securities market regulation.

- Leave companies without a 3-year track record to the private equity or venture capital markets.

10. One would be forgiven for thinking that the title of your paper, "The Main Board Profit Requirement", is actually a requirement that you should stop making losses on listing and regulating small companies. Vetting their prospectuses must take an inordinate amount of resources for a fee of only HK\$250k. HKEX loves to boast about the amount of money mega-IPOs have raised, and you have bent over backwards to facilitate this by allowing listings of second-class shares in tech giants, undermining corporate governance standards in a race to the bottom, with the support of the HK Government and against the original objections in 2015 of the SFC. You seem much less keen to facilitate fund-raising by small and medium enterprises that will contribute little to your bottom line. The message seems to be "go away until you are profitable, for us". If you don't want to be in the conflicted "business of regulation", then pass it over to the SFC, where it rightfully belongs.

Yours sincerely

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