

**The Latest Development of GEM
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Good afternoon, ladies and gentlemen:

I am very pleased to have this opportunity to share our experience of the Growth Enterprise Market, which we call GEM.

GEM is one way that the Stock Exchange is responding to the challenges faced by participants in the development of the *New Economy*.

In the past, new companies were expected to develop and grow organically. This was a process that could take and still takes years.

Today's companies developing in the new economy are more impatient – perhaps they've been genetically modified. They tend to be technology driven and you have to be quick to take advantage of a new technology before it is overtaken by an even newer one.

Companies from the old and new economies, though, have at least one thing in common. They both need capital. And availability of capital is as important as advanced technology or bright ideas in any business model; perhaps more so in the new economy.

GEM provides a new and alternative source of capital formation for enterprises with good growth prospects. More importantly, it lowers some of the traditional barriers to capital formation faced by new companies.

It recognises and accepts that companies in the new economy, as relatively new start-ups, may not have a sustained record of profitability, and a three year profitable track record is required for a listing on our more traditional main board. GEM therefore opens a new window to capital formation without which many companies pursuing e-business on an Internet platform might wither on the vine for want of capital.

GEM provides a market with a separate identity for innovative technology and growth companies. And it meets the bigger objective of widening Hong Kong's economic base and developing a technology and knowledge-based economy.

GEM also enhances the velocity of capital. It provides a ready exit for venture capital investments in start-up companies. Previously, lack of an exit has tended to deter venture capitalists from investing in start-ups in this region until they have matured; but they are now more ready to invest in them, and at an earlier stage.

The rules and requirements of GEM are designed to satisfy the needs and standards desired by professional and informed investors. Thus, a different regulatory philosophy is involved - GEM operates under a disclosure-based regime. While small retail investors can of course choose to invest in GEM stocks, they must take the time and effort to understand the companies concerned and accept the risks under the *caveat emptor* principle. At the end of the day, the market will decide the fate of the GEM-listed companies.

Although GEM listing applicants need not show a three-year record of profitability, they have to have been in business for at least one year under substantially the same management. They have to show pursuit of a single focused line of business.

Applicants must appoint a GEM-approved sponsor for the remaining period of the company's financial year, and for the two following years to act as advisor. The sponsor will be the principal channel of communication between the Exchange and the issuer.

A minimum public float of 20 per cent is required, subject to a minimum value of \$30 million, for companies with market capitalisation of less than \$1 billion. For market capitalisation of more than \$1 billion, a minimum public float of 15 per cent is required, with a minimum value of \$200 million.

Initial management and significant shareholders must collectively hold not less than 35 per cent of the issued share capital at listing; and are subject to a moratorium on disposal of their shares.

They may not dispose of any shares for the first six months, and their collective shareholding should not fall below 35 per cent during the second six months.

The Exchange allows some flexibility in the GEM rules which are not available in the listing rules for the Main Board. For example, GEM places no restriction on the offering mechanism; competing businesses of directors, controlling shareholders, and substantial shareholders are allowed, subject to full disclosure on a continuing basis. Underwriting is not compulsory provided that the minimum public float and minimum subscription amount as set out in the prospectus are met.

The lowering of barriers to listing has been well received in the market, and GEM has made a good and promising start. Since its introduction last November, it has received more than 60 listing applications. Among them, 25 have been approved and listed on GEM, 11 have been approved and pending listing, while another 40 are being processed.

It has raised more than \$10.5 billion in new capital and market capitalisation of the 25 listed GEM companies currently stands at around \$65 billion. Average daily trading turnover is around \$400 million.

The Exchange has received more than 50 applications from potential sponsors and has admitted 45 so far, including one from the accounting profession.

GEM is more than a local market as is shown by the origins of its listing applicants. Listing applications have been received from China, Macau, Taiwan and even the Silicon Valley. The business target of overseas applicants is almost certainly China and it is encouraging to see this reaffirmation of Hong Kong's role as the gateway to China.

Let me share with you some of the practical advice we give potential applicants.

We require companies to have strong corporate governance commitment in order to uphold GEMs' market integrity. The issuer must designate an

executive director as compliance officer, responsible for compliance with the GEM listing rules and internal control.

Issuers have to appoint at least two independent non-executive directors. A qualified accountant who is a member of the Hong Kong Society of Accountants or other body of professional accountants recognised by the Society must be appointed.

Although GEM does not require a profitable track record, issuers have to provide a full account of what was done in the period before listing. Both qualitative and quantitative information is required. Some examples of that are :-

- sales and marketing activities including turnover, customer base and geographical mix;
- employment of human resources including number, expertise and experience;
- licences held, including type, purpose, expiry dates, and exclusivity;
- details of joint ventures, collaborations or other business arrangements;

The issuer should compile its Business Objectives statement carefully as its actual business progress will be compared against it every six months for two years after listing.

Risk factors have to be disclosed in full. Prepare as comprehensive a list as possible. Risk factors differ from company to company and can usually be classified as company, industry or country related.

GEM operates a disclosure based regulatory regime and it is up to the market to decide on the merits of companies. Issuers must keep investors fully aware of the risk factors to help them in their investment decisions.

Mainland-based issuers should factor into their listing timetables the time needed to obtain all necessary approvals in China. They may need approval

from China Securities Regulatory Commission and must provide a Chinese legal opinion on the planned listing.

The Exchange requires all listing applicants operating in a jurisdiction outside Hong Kong to comply fully with the laws of that jurisdiction.

Finally, remember the six month limit. The financial period reported in a listing application must have ended no more than six months before the date of the document. Applications outstanding for more than six months will be considered to have lapsed.

The Exchange has issued a market consultation paper on proposed rule changes for GEM. The proposals are based on experience gained during the past six months and feedback from the market.

Please give the consultation document your careful and thoughtful attention, and let us have your views. I promise you that they will all receive our careful consideration.

It is clear that e-transformation has created huge business potential and that the Internet is here to stay and grow, despite the current stock market volatility.

GEM is our Exchange's response to the challenge and needs of the emerging new economy and its participants.

As a market operator and front-line regulator, we are committed to developing GEM into a market of choice in the Asian region. We are encouraged by the initial development of GEM, but we need your continued participation and support.

Thank you for being an attentive audience.