Hong Kong Listing – raising your equity capital

Listing, sometimes known as "going public" or "Initial Public Offering (IPO)" is to list a company's shares on a recognized stock exchange such as the Stock Exchange of Hong Kong Limited. In this article, we are going to talk about the advantage and disadvantages of going public, the requirements and process of obtaining a listing, corporate governance, etc.

Entrepreneurs who have worked so hard in building their business empire may at some point in time consider listing their company. In that case, they should consider the various factors before attempting to obtain a listing.

Advantages

a) Capital Funding

Going public provides the company with additional capital for expanding your business opportunities. This is a better alternative to funding your business from banks or other financial institutions because the capital does not have to be repaid and does not involve an interest charge. Beside this immediate infusion of capital provided by IPO, the company can obtain capital for future needs through new share offerings or public debt offerings.

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b) Business expansion

Going public allows the company to negotiate and pay for any acquisition of business by issuing its own shares in exchange for the target company instead of paying cash or loan/debt financing. In addition, no interest is payable on the shares issued, although dividends are expected by the shareholders.

c) Status

Going public will increase the status of the company and raise public awareness of the company which may lead to new opportunities and new customers. This status may have enhanced the company's credibility with its suppliers, customers, and lenders, which may lead to improved credit terms.

d) Valuation of shares

Going public provides a public valuation of your business which will become easier for the company to enter into any merger and acquisitions, because it can offer shares rather than cash. Secondly, companies listed on a stock exchange are typically worth more than similar companies that are privately held.

e) Marketability and Liquidity

The shares of public listed companies are usually more liquid than private companies in most cases because investors can easily buy and sell their shares in the market. Hence, going public will make the company's shares more marketable and investors are willing to pay a premium for liquidity which varies over time and economic conditions.

f) Share options

Going public involves the ability to use share options in creative incentive packages for management and employees. Offering share options as part of compensation may enable a business to attract better and capable management talent, and to provide them with an incentive to perform well.

Disadvantages

a) Public Scrutiny

Going public will become the focus of investors and capture the attention of the media. Most of its activities will be monitored by the public and exposed to critical comments both in the press and elsewhere.

b) Directors' declaration and undertakings

The directors will have to provide declaration, under oath, and an undertaking at the time of listing. The declaration covers such matters relating to conviction of any offences involving fraud, dishonesty or corruption, or guilty of insider dealing, or disqualification from acting as a director. The declaration will commit the directors to comply with the relevant Listing Rules and to co-operate with the Listing Division in any investigation launched by it.

c) Directors' new responsibilities and pressures

A public listed company will have to observe the relevant Listing Rules and other requirements of the Exchange covering the publication of its interim and annual reports, issuing notices to shareholders and the public regarding significant acquisition, etc.

d) Increased disclosures

Going public will mean moving from private ownership to public, hence vastly increase the number of people who will have access to the company's financial records. This will not only cover the company's financial results but the disclosure of management salaries and perks that not applicable for a private company.

e) Costs of IPOs

Going public is not cheap because it involves various professional charges and investment bankers' commission. Other ancillary cost, such as public relations, printing, corporate advertising and others can add to the IPOs costs.

f) Time

Preparing for the IPOs will mean a considerable amount of executive time will be taken up in communicating with the various professionals, the Exchange and shareholders both during and after the listing process.

Listing requirement

The basic conditions for going public are track record and market capitalization requirements, and they are as follows:

- The company will need to have trading record of not less than three financial years;
- Management continuity for at least the three preceding years and ownership continuity and control for at least the most recent audited financial year;
- Three tests:
  1) **Profit test**
     - Profits of HK$20 million for most recent year and of aggregate of HK$30 million for the first two years
     - Market capitalization of at least HK$200 million at the time of listing
  2) **Market capitalization/revenue/cash flow test**
     - Revenue of at least HK$500 million for the most recent audited financial year
     - Positive cash flow from operating activities of at least HK$100 million in aggregate for the three preceding financial years
     - Market capitalization of at least HK$2 billion at the time of listing
  3) **Market capitalization/revenue test**
     - Revenue of at least HK$500 million for the most recent audited financial year
     - Market capitalization of at least HK$4 billion at the time of listing
     - Track record of less than three years may be accepted if:
       - Directors and management have sufficient and satisfactory experience of at least three years in the line of the listing business and industry
       - Management continuity for the most recent audited financial year
- Exemptions may be granted for mineral companies and newly formed project companies, such as major infrastructure projects, which can have shorter trading records
- A focused line of business not specifically required, but its core business should meet the minimum financial requirement
- The company must have control over the business

Minimum Public Floatation

The Listing Rules require:

- Market capitalization of at least HK$50 million held by the public at the time of listing
- Minimum 25% of the issuers' total issued share capital at the time of listing
- The exchange may, at its discretion accept a percentage of public float between 15% and 25% if the market capitalization of the issuer exceeds HK$10 billion

Future Prospects

There is no specific requirement relating to the company's future prospects but the applicant is required to include a general statement of future plans and prospects. Inclusion of any profit forecast will be optional for the company.

Acceptable Jurisdictions

For the purpose of listing, only companies incorporated in Hong Kong, Bermuda, the Cayman Islands and the People's Republic of China are acceptable. Other jurisdictions for secondary listing may be considered.

Restriction on Initial Shareholders

The Listing Rules stipulate:

- A controlling shareholder at the time of listing must undertake:
  - Not to dispose of his interest in the issuer from the prospectus issue date to the first six months after listing
  - Not to dispose of his interest in the issuer in the next six months such that he would cease to be a controlling shareholder: at least 30% interest in the issuer
- Other consideration
  - Competing business of controlling shareholders or directors are allowed but full disclosure is required
  - May not list by way of placing only
  - New issue must be fully underwritten
  - Listed issuer is not allowed to issue new securities in the first six months after listing

Corporate Governance

A public listed company requires:

- Three independent non-executive directors;
- Qualified accountant;
- To appoint a compliance adviser for the period commencing on initial listing and ending on publication of financial results for the first full financial year after listing.

How can we help?

Alpha Partners Certified Public Accountants will assist you:

- To liaise with sponsors, reporting accountant, legal adviser, valuer, underwriter, share registrar, receiving bank, printer, translator and public relations firm.
- To restructure the group of business, tax planning opportunities and re-organising other business aspects for the purpose listing.
- To assist you in preparing profits forecasts, if necessary.

- To assist you in developing and implementing internal control systems to meet the requirements.
- To act as your independent non-executive directors, audit committee, etc.

Please feel free to contact us, at no obligation, to discuss how we can assist you in bringing your business going public and assisting in creating value for your business as a whole. Our Mr. Gilbert Loke will be delighted to meet you to find out your needs and expectations. Please send your email to info@apcpa.hk or call us at +852-2512 0588.

Note paper

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