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Hong Kong IPO Market Update

July 2014

Welcome to our 2014 first-half Hong Kong IPO Market Update. In April 2014, the Hong Kong IPO market showed signs of cooling down after a strong Q1. Thanks to the IPO pipeline that had built up prior to the new public disclosure requirements becoming effective on 1 April 2014, more entities were listed before the end of Q2, warming up the sluggish IPO market. In this issue, we review how the market has been performing since Q1 2014 and give an outlook for the rest of the year.

In April, the Chinese pork giant WH Group postponed its planned IPO due to weak investor demand. The withdrawal of this multibillion-dollar IPO, together with weak public reception of certain larger IPOs, lowered the chances of the Hong Kong IPO market hitting earlier full-year fundraising forecasts for 2014. However, we believe the full-year IPO proceeds for 2014 will exceed the HKD 169 billion recorded last year.

Second quarter of 2014: Signs of cooling down?

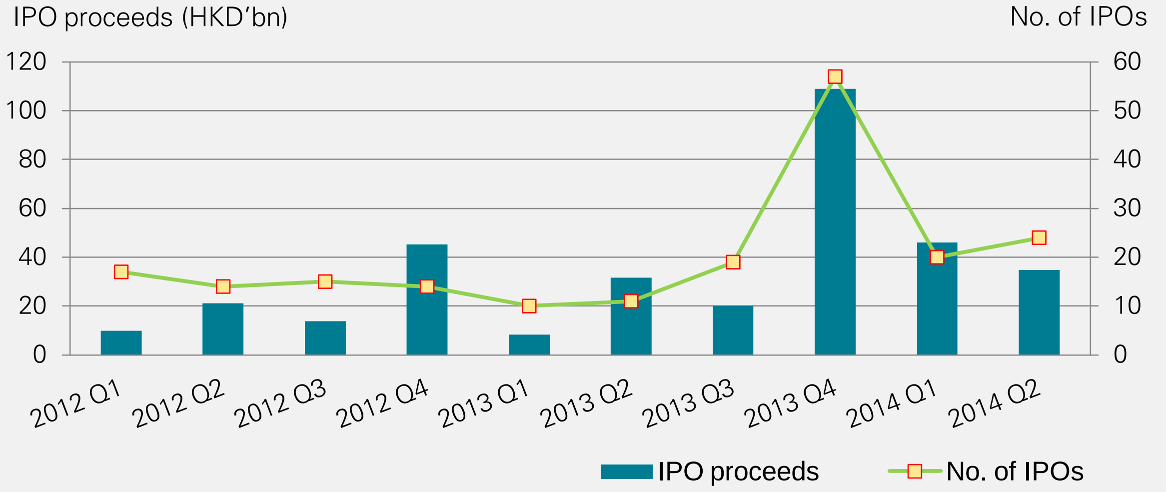
Q1 2014 sustained the momentum from Q4 2013 and IPO proceeds surged 461 percent year-on-year from HKD 8.2 billion to HKD 46 billion. This leap lifted the market mood and gave us a positive outlook for the rest of 2014 as the market generally anticipated that both IPO proceeds and the number of IPO cases would be higher than last year.

Stepping into Q2, Hong Kong's IPO market showed signs of cooling down. WH Group's withdrawal of its listing plan in April, plus the relatively low pricing of some mega IPOs in Q1 cast doubts on the market's appetite for mega IPOs. In April, only two companies listed, raising HKD 1.7 billion.

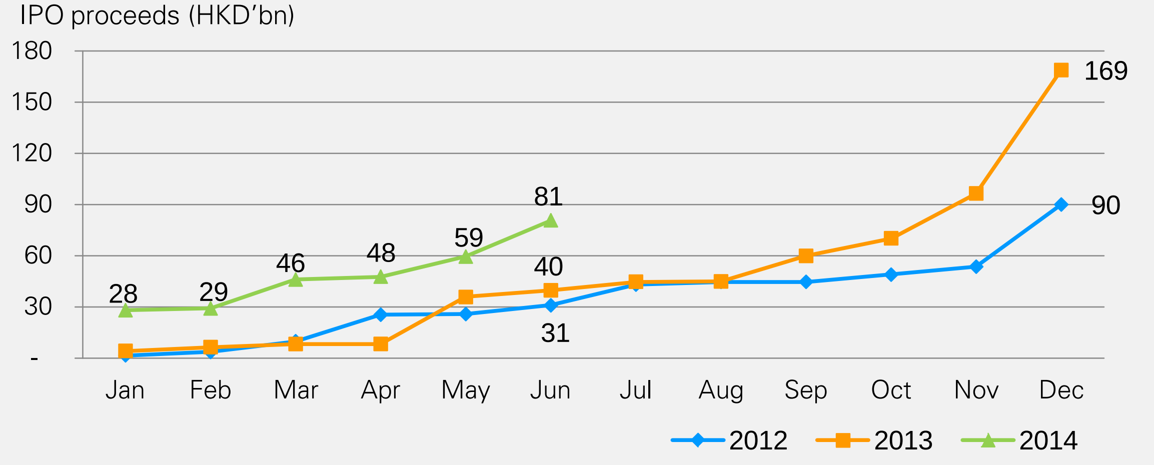
In May, China CNR (6199.HK) raised HKD 10.0 billion, making it the largest IPO in Q2 2014 and the second largest IPO year-to-date. Together with five other IPOs, the aggregate IPO proceeds reached HKD 11.8 billion in May.

The uptick became more apparent in June, when 16 companies listed on the Hong Kong Stock Exchange, raising HKD 21.3 billion in aggregate. This was partly attributable to the IPO pipeline built up by the 50 or so IPO applications in March 2014 before the public disclosure requirements under the new sponsor regime became effective. It is expected that the impact will still be felt in the second half of 2014, particularly in July, as over 20 companies are expected to list during the month.

Quarterly performance of the Hong Kong IPO market between 2012 and 2014



Year-to-date IPO proceeds of the Hong Kong IPO market between 2012 and 2014



The IPOs launched in Q2 2014 generated weaker public reception than those in Q1. Of the Main Board IPOs, 48% were priced in the lower range, compared with 33% in Q1 2014 and 42% in 2013.

	Q2 2014	H1 2014	H1 2013	FY 2013
Subscription – Main Board				
Number of deals over-subscribed on their retail portion	16	28	14	64
Average over-subscription rate [(a)]	77.4	367.1	227.2	122.2
% of Main Board IPOs priced at:				
Upper range	35	47	50	50
Lower range	48	42	43	42
Midpoint	17	11	7	8

Source: HKEx and KPMG analysis

(a) Average oversubscription rate is calculated by the average of the number of times shares are applied for, over the number of shares offered for companies with oversubscriptions.

The post-market performance of companies newly listed in Q2 2014 has been mixed, with 11 out of 24 seeing their closing share price on the first day of trade exceed the IPO subscription price.

Hong Kong IPOs with funds raised equal to or over HKD 1 billion during Q2 2014

			IPO subscription			The first trading day	
Stock code	Company	Funds raised (HKD'million)	Price range (HKD)	IPO price (HKD)	Date of listing	Closing price (HKD)	+/- (%)
6199	China CNR	10,028	5.00 - 6.20	5.17	22 May 2014	5.05	-2.32%
1619	Tianhe Chemicals	5,071	1.75 - 2.25	1.8	20 Jun 2014	1.79	-0.56%
6198	Qingdao Port	2,919	3.76	3.76	06 Jun 2014	3.71	-1.33%
3903	Hanhua Financial	1,863	1.55 - 2.05	1.62	19 Jun 2014	1.63	+0.62%
2100	BAIOO	1,518	2.00 - 2.60	2.15	10 Apr 2014	1.77	-17.67%
1375	CC Securities	1,501	2.51 - 3.14	2.51	25 Jun 2014	2.16	-13.94%
2298	Cosmo Lady	1,463	3.27 - 4.42	3.6	26 Jun 2014	3.55	-1.39%
3639	Yida China	1,421	2.30 - 2.90	2.45	27 Jun 2014	2.44	-0.41%
2014	Ozner Water	1,310	2.25 - 2.70	2.7	17 Jun 2014	2.99	+10.74%
1330	Dynagreen	1,035	3.00 - 3.70	3.45	19 Jun 2014	3.77	+9.28%

Source: HKEx and KPMG analysis

The number of deals and average deal size are illustrated in the tables below:

	Q2 2014		
	IPO proceeds[(a)] HKD'billion	Number of IPOs[(b)]	Average proceeds per deal HKD'billion
Main Board			
Above HKD 5 billion	15.1	2	7.5
HKD 1 to 5 billion	13.1	8	1.6
Below HKD1 billion	6.5	13	0.5
	34.7	23	1.5
GEM	0.1	1	0.1
Total	34.8	24	1.4

	H1 2014			H1 2013		
	IPO proceeds[(a)] HKD'billion	Number of IPOs[(b)]	Average proceeds per deal HKD'billion	IPO proceeds[(a)] HKD'billion	Number of IPOs[(b)]	Average proceeds per deal HKD'billion
Main Board						
Above HKD 5 billion	48.0	4	12.0	22.5	2	11.2
HKD 1 to 5 billion	22.4	13	1.7	11.9	5	2.4
Below HKD1 billion	9.8	21	0.5	4.4	8	0.6
	80.2	38	2.1	38.8	15	2.6
GEM	0.6	6	0.1	0.9	6	0.2
Total	80.8	44	1.8	39.7	21	1.9

	FY 2013		
	IPO proceeds[(a)] HKD'billion	Number of IPOs[(b)]	Average proceeds per deal HKD'billion
Main Board			
Above HKD 5 billion	91.5	6	15.2
HKD 1 to 5 billion	59.0	28	2.1
Below HKD1 billion	15.3	40	0.4
	165.8	74	2.2
GEM	3.2	23	0.1
Total	169	97	1.7

Source: HKEx and KPMG analysis

(a) Q2 2014 amounts include actual proceeds raised for IPOs up to 30 June 2014 and have not taken into account any overallotment subsequent to that date.
(b) 2013 and 2014 numbers exclude listings by introduction or transfers from the Growth Enterprise Market (GEM) to the Main Board.

Excluding listings by introduction or transfers from the GEM to the Main Board, there were 24 IPOs in Q2 2014, taking the number of IPOs in the first half of 2014 to 44. Both the IPO proceeds and the number of IPOs in the first half of 2014 doubled compared to the corresponding period in 2013.

Despite the increased number of IPOs in Q2 2014 from the previous quarter, the overall market sentiment was weak due to sluggish investor demand, evidenced by weak subscription rates and some IPOs' bottom-of-range pricing. In Q2, seven out of 23 Main Board IPOs were undersubscribed in the retail portion and, interestingly, all of these IPOs were seeking to raise above HKD 1 billion. Such weak market demand for relatively large IPOs may prompt potential applicants to take a wait-and-see attitude towards attempting IPOs in the remaining part of 2014.

The rest of 2014: Full of uncertainties

Having considered the strong performance in Q1 2014 and the prevailing uncertainties, we formed a mixed outlook for the Hong Kong IPO market in our last communication. As events have developed, the withdrawal of WH Group’s IPO plan as well as the weak investor demand for some IPOs have prompted us to form a blurry outlook for the rest of 2014.

Approximately 50 IPO applications were filed in March 2014, as applicants and market participants were generally trying to stay away from the new public disclosure requirements in their initial phase. We saw very few IPO applications submitted immediately after the new public disclosure requirements came into effect in April, but as expected, the impact was relatively short-term and market participants adapted to the change quickly. The pipeline that built up in March 2014 drastically drove up the number of IPOs in June 2014, with 16 out of 24 IPOs in Q2 2014 happening that month. We expect to see the remaining pipeline keep the market rolling in the second half of 2014, particularly in July, as over 20 companies are expected to list during the month.

The Hong Kong IPO market’s performance depends heavily on the realisation of mega IPOs – those expected to raise more than HKD 10 billion. Though WH Group pulled its IPO plan in April, it may try again this year. With a few other mega IPOs anticipated by the market, including BAIC Motor, China General Nuclear Power Group, Bank of Shanghai and China Guangfa Bank, we are not too pessimistic about the outlook for the rest of the year.

In April 2014, the China Securities Regulatory Commission and the Securities and Futures Commission approved, in principle, the development of Shanghai-Hong Kong Stock Connect for establishing mutual stock market access between mainland China and Hong Kong. The scheme is expected to boost the flow of funds between the two markets as well as market confidence.

It is believed that there will be more southbound capital flows than northbound ones under this scheme. Mainland investors can gain access to new types of stocks which they did not have access to before, such as Hong Kong’s blue-chip companies and Macau gaming stocks. On the contrary, Hong Kong investors already have a wide range of choices when it comes to investing in mainland businesses, as many sizeable PRC entities are already listed in Hong Kong. However, the scheme is clearly beneficial to both stock markets and is a huge step towards internationalising the mainland capital markets.

We maintain our earlier forecast that non-bank financial services, in particular micro and small loan companies, will be the upcoming focus of Hong Kong's IPO market. This is a highly fragmented industry and has numerous market players in the PRC. Though we do not expect the number of deals and IPO proceeds from this sector to outweigh the others in the short run, it has relatively high growth potential and is expected to attract more market attention than traditional entities. It is nevertheless important to consider the pace of PRC policy change, and the extent to which it affects the growth and development of the non-bank financial industry.

Factors such as interest rate movement, timing of quantitative easing (QE) tapering and PRC economic data will continue to be the key factors affecting the Hong Kong IPO market. When Shanghai-Hong Kong Stock Connect goes live later this year, it should add momentum and, at the same time, volatility to the stock market. Southbound investments under the scheme will likely add liquidity and expand the investor base in Hong Kong's stock market, hopefully stimulating the sluggish IPO market we observed in Q2 2014.

The overall performance in 2014 will depend heavily on Q4, the traditional peak season for Hong Kong's IPO market. The withdrawal of WH Group's IPO plan, the weak public reception of large IPOs, together with weak investor demand in Q2, adversely affected the chances of hitting earlier forecasts for full-year IPO proceeds. Despite the uncertainties that have emerged during Q2, the first half of 2014 recorded a strong year-on-year growth and there is still a good chance that the full-year IPO proceeds for 2014 will exceed last year's amount of HKD 169 billion.

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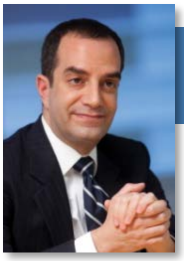

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