

Think Ahead

ACCA

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17 Nov 2017

**ICPAK 22<sup>nd</sup> Annual  
Executive Seminar  
“From  
Private Equity  
to  
Public Market”**

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# About the Speaker

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Ernest Wong

- Current posts :
  - President and Group CFO – KVB Kunlun Holdings Ltd
  - Director of several listed companies in HK and overseas
- BBA (HKU), MSc Investment (HKUST), MSc Electronic Engineering (CUHK)
- FCPA, FCCA, CFA, MHKSI
- Successfully listed companies in London and HK stock exchange
- Invested in a PE deal with 10X return in 3 years
- Experience in start up, venture deal, billion dollar restructuring transaction, pre-IPO fund raising, IPO, M&A and corporate finance transactions
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# Sources of Funding for Private Company

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- Personal
  - ♦ Family and friends
  - ♦ Business angels
- Business
  - ♦ Potential Partners
  - ♦ Joint venture support from other company
- Public Funding
  - ♦ Government Grants
  - ♦ Support from Universities
- Financing Institutions
  - ♦ Venture Capital Firm
  - ♦ Incubation Centre
  - ♦ Bank



# Local and Foreign VC /PE Firms



# Stages of Investment

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- Angel round (seed stage)
  - Initial idea and R&D
  - Financing from entrepreneur's own resource or angel fund
- Start Up
  - Product development and initial market effort
  - Investment in facilities and operation equipment
  - Business still has no track record, high failure rate
- First round (series A)
  - Commercial production
  - Initial sales, trying to build up track record
  - Not yet profitable

# Stages of Investment

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- Expansion (series B or C)
  - Seeking additional capital to expand a firm, production and marketing capacity
  - The firm is turning profitable
  - Banking facilities may be available but need personal guarantees and collateral
  - May have several rounds of fund raising
- Pre-IPO stage (mezzanine)
  - Last round of VC funding as expecting to go public
  - May intend less to raise capital than to bring in to bring in strategic shareholders as a part of preparation for IPO
  - May have certain aspects for window dressing and cleaning up the balance sheet

# Angels vs VCs

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## Angels

- Usually high net worth individuals, with investment and / or management experience, investing their own money
- At seed round
- Smaller amount invested
- Usually take common stock and not taking control stake
- Can invest with VCs

## VCs

- Intuitional investor, investing LPs money
- At Series A or later stage
- Investing in bigger tranche
- Invest through preferred share or convertible bond with attendant preferences (board seat, liquidation preferences, participation...)



# Investment Process

- *Management Skill*
- *Investment Profession*
- *Technical Knowledge*
- *Capital Funding*
- *Networking*

Venture Capital /  
Private Equity



Deal Sourcing &  
Initial Screening



Detailed Due  
Diligence

- *Capable Management*
- *Viable Business Plan*
- *Proprietary Technology*
- *Accounting Integrity*

- *Major Terms*
- *Deal Structure*
- *Valuation*

Negotiation &  
Terms Sheet



Divestment  
/ Exit



Project Funded &  
Monitoring



Documentation &  
Completion

- *IPO*
- *Sale Back*
- *Trade Sale*
- *Put Option*

- *Board Seat*
- *Financial Monitoring*
- *Adding value*

- *Legal Structure*
- *S&P Agreement*
- *Employment Agreement*

# Preparation for Approaching a VC / PE

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- **A good business plan**
  - But VC / PE may not read it
  - Write it for your edification, recruiting, banking, government grants, licensing, etc
- **Prepare an excellent “One Pager”**
  - VC / PE probably read it before getting interest in the full plan, mini business plan
- **Have an outstanding evaluator pitch**
- **Prepare an investor presentation at the first meeting**
- **Good to have a Private Placement Memorandum**
  - as a supporting document
- **Well prepare for the due diligence**
- **Term Sheet**
  - Agreed all the major terms
- **Legal documentation**
  - Prepare to flight with the lawyer

# What's the VC / PE looking for?

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- **Management, management, management**
- **A “good” company**
  - Market, technology, product, competition, competitive advantage, sustainable
- **Attractive financial returns**
  - Financial performance
  - Valuation
  - Exit Strategy
- **Track record and reputation of the firm**
- **Reputation of co-investors, if any**
- **Fit with other portfolio companies**
- **Right industry focus**
- **Right investment stage**
- **Right geographic restriction from the VC / PE mandate, if any**

# What should the Company Consider?

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- **Right investor?**
  - Chemistry (treat it like a marriage, do DD, track record, reputation)
  - Active or Passive? Lead or Follow? Specialist or Generalist?
  - Interest aligned?
- **Good valuation and enough funding**
- **Dilution on shareholding – Major shareholder? Minority stake?**
- **Management control, board seat**
- **Employment contract, retention of key staff, share option scheme**
- **Assistance – strategy, industrial knowledge, network, team building/recruiting**
- **Assistance with follow-on rounds of financing, long term financing strategy**
- **Conflict resolution among investors and between investors and founder**

# Venture Funding vs Going Public

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## Venture Funding

- VC / PE requires board seats and certain decision-making authority
- Lower valuation
- Lower profile
- Smaller number of shareholders
- Information disclosed to limited number of shareholders only
- Lower cost in the fund raising
- No need to spend high professional fee annually
- Less time to spend on taking care of investors

## Going Public

- Management remain control
- Higher valuation
- Higher profile
- Larger shareholders basis
- Higher transparency on the company information to public
- Very costly to go public
- Higher professional fee to maintain the listing status
- More time to do the Investor relationship

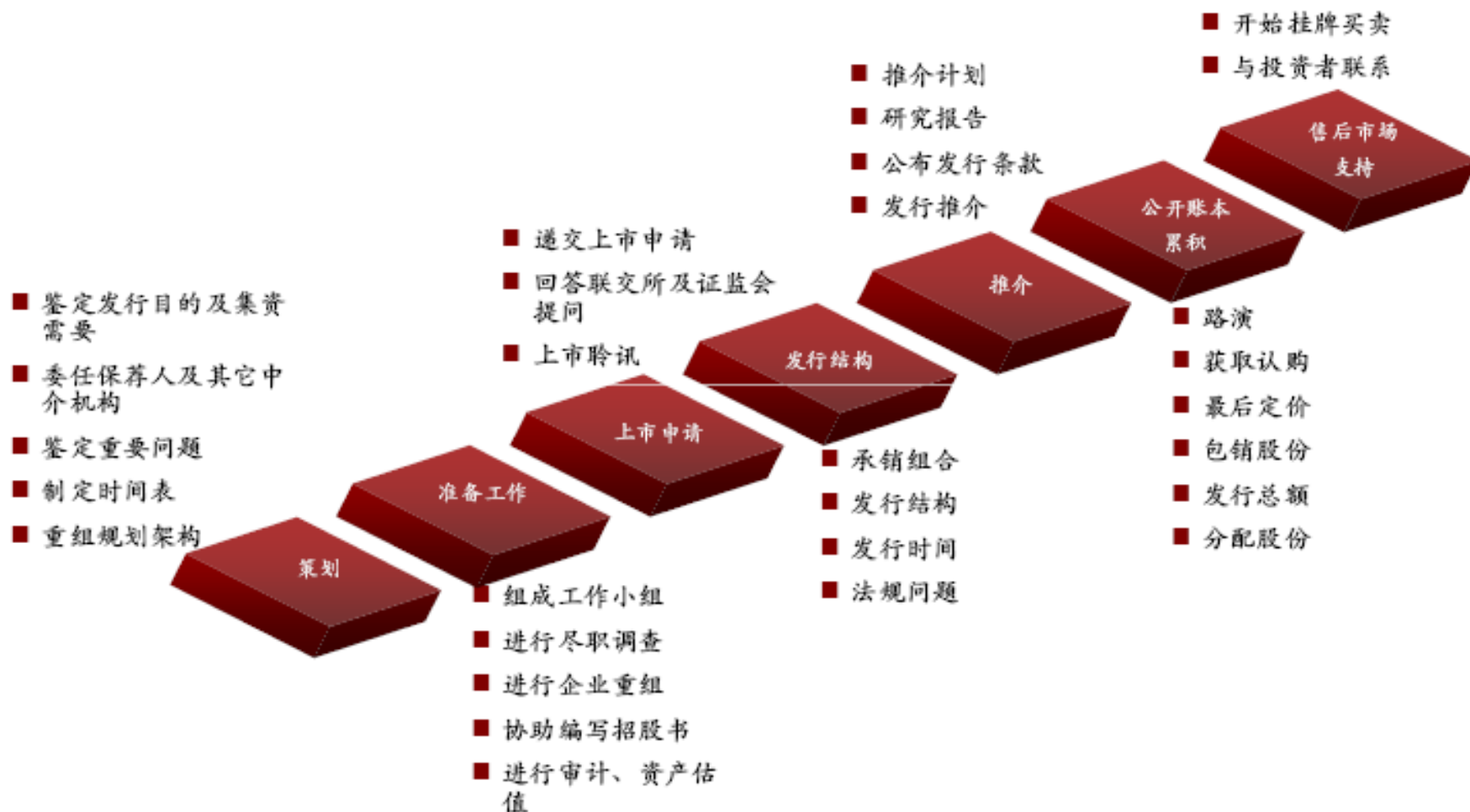
# Benefit of Listing

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- Access to capital for growth
- Broader shareholder base
- Employee incentive and commitment
- Higher profile and visibility
- Increased corporate transparency
- Greater efficiency



# Listing Process



# Comparison of Listing Requirements in different Stock Exchanges

	Main Board - HK	GEM - HK	LSE AIM	LSE Main Market (Premium)
<b>Financial requirements</b>	<p>Either one:</p> <ul style="list-style-type: none"> <li>● Profit ≥ HK\$20M (US\$2.6M) in last yr;</li> <li>● Profit ≥ HK\$30M (US\$3.8M) in 2 preceding yrs; &amp;</li> <li>● Market cap ≥ HK\$200M (US\$26M). <b>OR</b></li> <li>● Market cap ≥ HK\$4,000M (US\$513M); &amp; Revenue ≥ HK\$500M (US\$64M) in last yr. <b>OR</b></li> <li>● Market cap ≥ HK\$2,000M (US\$256M); &amp; Revenue ≥ HK\$500M (US\$64M) in last yr; &amp;</li> <li>● Positive operating cash flow ≥ HK\$100M (US\$13M) in last 3 yrs.</li> </ul>	<ul style="list-style-type: none"> <li>● Market cap ≥ HK\$100M (US\$13M); &amp;</li> <li>● Operating cash flow ≥ HK\$20M (US\$2.6M) in last 2 yrs.</li> </ul>	N/A	Market cap ≥ £700,000
<b>Free float requirements</b>	≥ 25% and a min. of HK\$50M (US\$6.4M) at all times	≥ 25% and a min. of HK\$30M (US\$3.8M) at all times	No min. free float required, but Market expects ≥ 10% on IPO	25% at all times
<b>Operating history*</b>	≥ 3 yrs trading record	≥ 2 yrs trading record	No trading record required	≥ 3 yrs trading record covering a least 75% of business

# Comparison of Listing Requirements in different Stock Exchanges

	Main Board – HK	GEM - HK	LSE AIM	LSE Main Market (Premium)
<b>Operating management and ownership *</b>	≥ 3 yrs management continuity; & ≥ 1 yr ownership continuity.	≥ 2 yrs management continuity; & ≥ 1 yr ownership continuity.	N/A	Demonstrate control over the majority of business assets for the 3 yr period
<b>Management presence</b>	≥ 2 EDs are ordinarily resident in HK (in case of primary listing).	N/A	N/A	≥N/A
<b>Corporate governance practices</b>	The Code on Corporate Governance <ul style="list-style-type: none"> <li>• Code provisions; and</li> <li>• Recommended Best Practices</li> </ul>		<ul style="list-style-type: none"> <li>▪ No mandated rules;</li> <li>▪ General expectation of applying the procedures appropriate to the company's size e.g QCA</li> </ul>	Adhere to the Combine Code of Corporate Governance or explain why
<b>Minimum no. of INED</b>	<ul style="list-style-type: none"> <li>▪ ≥ 3 INEDs; and</li> <li>▪ ≥1 INED having appropriate professional qualifications</li> </ul>		Not mandatory, but market practice expects at least 1, normally 2, sometimes 3.	<ul style="list-style-type: none"> <li>▪ ≥ half the Board (excl. Chairman) are INEDs;</li> <li>▪ ≥ 2 INED for companies below FTSE SmallCap</li> <li>▪ 1 INED as Senior Independent Director</li> </ul>
<b>Audit committee</b>			Not mandatory, but market practice expects it to be compliant with the Combined Code for smaller companies	<ul style="list-style-type: none"> <li>▪ Required;</li> <li>▪ ≥ 3 INEDs (2 for FTSE SmallCap);</li> <li>▪ ≥ 1 member has recent and relevant financial experience</li> </ul>

# Comparison of Listing Requirements in different Stock Exchanges

	Main Board – HK	GEM - HK	LSE AIM	LSE Main Market (Premium)
<b>Accounting Standards</b>	<ul style="list-style-type: none"> <li>▪ HKFRS / IFRS; or</li> <li>▪ USGAAP / other accounting standards acceptable under certain circumstances.</li> </ul>		<p><i>European Economic Area incorporated companies</i></p> <ul style="list-style-type: none"> <li>▪ IFRS.</li> </ul> <p><i>Non-EEA incorporated companies</i></p> <ul style="list-style-type: none"> <li>▪ IFRS;</li> <li>▪ USGAAP;</li> <li>▪ Canadian GAAP;</li> <li>▪ Australian IFRS; or</li> <li>▪ Japanese GAAP.</li> </ul>	<ul style="list-style-type: none"> <li>▪ IFRS; or</li> <li>▪ Equivalent standards for non-UK issuers</li> </ul>
<b>Reporting deadline – Annual audited accounts</b>	▪ ≤ 3 months	▪ ≤ 3 months.	≤ 6 months.	≤ 4 months.
<b>Reporting deadline – Interim unaudited accounts</b>	<ul style="list-style-type: none"> <li>▪ Half-yearly basis;</li> <li>▪ ≤ 2 months</li> </ul>	<ul style="list-style-type: none"> <li>▪ Quarterly basis;</li> <li>▪ ≤ 45 days.</li> </ul>	<ul style="list-style-type: none"> <li>▪ Half-yearly basis ;</li> <li>▪ ≤ 3 months.</li> </ul>	<ul style="list-style-type: none"> <li>▪ Half-yearly basis ;</li> <li>▪ ≤ 2 months;</li> <li>▪ Quarterly summary (≤ 45 days)</li> </ul>

# Fund Raising Products for Going Public

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- **Pre-IPO Investment – 28/180 days**
- **IPO**
  - Public subscription, placement, by introduction
  - Ordinary shares
  - Preferred shareholders - no voting rights, receive fixed dividends, claim on corporate assets, ranks ahead of ordinary shareholders in the event of liquidation
- **Post – Listing**
  - Bank Loan
  - Debt / Bond
  - Warrants
  - Issuing new shares : Right issue vs Open offer
  - Convertible Bond
  - Selling of shell

# Points to Consider for Going Public

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- Disclosure requirement on the financials & executive compensation which could be useful to competitors
- Costly in listing and higher cost spending on the accounting, auditing, legal, compliance and director fee
- Company value is more on the stock price instead of the performance
- Loss of overall ownership and control of the business
- More stringent on director's responsibilities
- Higher requirements on the board composition and committees
- Continuing obligations – inside information, price sensitive information (PSI), announcement, circular, board meeting, shareholder meeting, disclosure of share interest, insider dealing, suspension and resumption of trading, maintenance of public float, noticeable and connected transactions (five tests)



# Thank you!!!

## Q & A ?