

To: Business Editors

HONG KONG SPAC POLICY SHOULD BALANCE THE INTEREST OF PROMOTERS, INVESTORS AND TARGET COMPANIES

US SPAC PROMOTER COMMENTS ON HKEX'S "SPAC" CONSULTATION PAPER

18 October 2021 -- The prime consideration for Hong Kong to introduce special purpose acquisition companies ("SPACs") listing is the balance of interests among SPAC Promoters, investors, and target companies. Some of the measures proposed in the Consultation Paper on "Special Purpose Acquisition Companies" published by Hong Kong Exchanges and Clearing Limited ("HKEX"), such as tying up redemption rights to opposition votes on de-SPAC transactions, limiting the dilution effect resulted from the issuance of warrants, and allowing the application for listing via a traditional IPO and negotiation with several SPAC Promoters to be conducted simultaneously, would potentially undermine the appeal to promoters and investors to participate in SPAC listing in Hong Kong, noted Mr. Jason Wong, who has successfully promoted the listing of four SPACs on Nasdaq in the US.

Mr. Jason Wong, founder and CEO of Norwich Investment Limited ("Norwich Investment"), referring to his own experience in SPAC listing in the US, expressed his opinion as a market stakeholder on the Consultation Paper on "Special Purpose Acquisition Companies" published by HKEX on 17 September 2021. He pointed out that the competitive edges of SPAC listing lie upon the high listing certainty, short approval period, and controllable costs, as well as its offering of a relatively convenient and efficient listing alternative to traditional IPOs.

The Negative Impact of Tying Up Redemption Rights to Opposition Votes on De-SPAC Transactions

Mr. Jason Wong pointed out that the SPAC Consultation Paper stipulates that a SPAC must not accept elections for redemption other than those SPAC Shares voted against the relevant resolutions at a general meeting, and the de-SPAC transaction must be approved by the SPAC shareholders at a general meeting. From the SPAC Promoter's perspective, the proposed rules that tie investors' redemption rights to the opposition votes and stipulate that the de-SPAC transaction must be approved by its shareholders at a general meeting will increase the uncertainty of the de-SPAC transaction and increase the risk of SPAC liquidation. The adverse impact of tying up redemption rights to opposition votes has been proven in the US SPAC market. From 2010 to 2014, 33% to 57% of SPACs in the US market were liquidated as a result of failed merger. In 2015, the US authorities adjusted the SPAC rules to allow investors to exercise their redemption right regardless of their voting decision on the proposed business combination. The risk of liquidation is thereby significantly reduced for SPAC Promoters, and it provided higher certainty of listing for de-SPAC targets, making this public listing method more appealing. In 2019, the SPAC liquidation rate in the US was only 1.7%.

Low Warrant Conversion Ratio could Reduce Initial Investor Returns

The Consultation Paper proposed the prohibition from issuing warrants that entitle the holder to purchase more than a third of a share upon their exercise, and from issuing warrants in aggregate (i.e., including SPAC Warrants plus Promoter Warrants) that, if exercised, would result in more than 30% of the number of shares in issue at the time such warrants are issued. There is no such requirement in the US, while the Singapore Exchange (“SGX”) sets 50% as the maximum percentage limit of dilution with respect to conversion of warrants. In other words, the return to investors offered by Hong Kong SPAC is lower than those offered by SPACs in the US and Singapore. In addition, the time frame for a de-SPAC transaction in Hong Kong is proposed to be 24 + 12 months (the de-SPAC transaction is usually completed within 24 months after the listing of a SPAC in the US). This means that the average time to complete a de-SPAC transaction in Hong Kong may be longer than that in the US while the number of warrants received by investors and the premium appreciation return through the exercise of warrants is lower in Hong Kong. These factors are likely to diminish Hong Kong SPAC’s appeal to investors. Mr. Jason Wong believes that a warrant conversion ratio closer to that of the US SPAC market should be applied and should allow the market to decide the warrant conversion ratio as long as it falls within a maximum warrant conversion ratio of one warrant to one ordinary share.

The Exercise of Warrants is not Without Consideration, and Should not Only Focus on its Dilution Impact

The de-SPAC target valuation is usually several times the amount of SPAC IPO proceeds. The dilution effect upon the exercise of warrants on a Successor Company (targeted company being merged by a SPAC) is not as significant as some imagine. For example, the valuation of a target company is 7 times the SPAC IPO proceeds and that one warrant is eligible to conversion into one ordinary share, the maximum dilution effect after exercising the warrants is only 12.5% (assuming that all the SPAC IPO shareholders’ shares opt for redemption, and not taking PIPE investment into account). More importantly, the conversion of warrants into shares is not without consideration. In fact, the warrant exercise price is higher than the subscription prices of a SPAC IPO and a PIPE investment (which is usually similar to the subscription price during a SPAC IPO). For example, the warrant exercise price in US is normally US\$11.50. With the warrant exercise price higher than the subscription prices of SPAC IPO and PIPE investment, the Successor Company would be able to secure further financing and increase the size of its public float, which in turn would allow it to enhance its shares’ liquidity and further optimise its shareholder base. Thus, Mr. Jason Wong believes the exercise of warrants should not be simply seen as a dilution in shareholding.

High Shareholding Ratio Requirements for PIPE Investment May Cause Pressure on Financing during De-SPAC Transactions

Mr. Jason Wong agreed with HKEX’s proposal to introduce independent PIPE investment to SPAC in Hong Kong. He believed the measure would serve to enhance the fairness in the valuation and transparency of the de-SPAC transaction. However, Mr. Jason Wong questioned the need for independent PIPE investment constituting at

least 15 to 25% of the expected market capitalisation of the Successor Company. According to the Consultation Paper, the de-SPAC transaction shall be approved by the SPAC shareholders at a general meeting, which means that more than 50% of the SPAC IPO proceeds will be retained in the end. If the PIPE investment constitutes 25% (or 15-25%) of the expected market capitalisation of the Successor Company, the proportion of public shareholders after the SPAC merger would be higher than that of companies seeking listing through traditional IPO, thereby posing significant financing pressure on the target company during the de-SPAC transaction. Owing to the fact that there are varying financing needs for projects of different nature, the financing needs of the enterprise should be determined in accordance with its operation scale and environment.

Dual-track Listing is Unfair to Promoters

The Consultation Paper states that issuers (listing applicants) are allowed to take a “dual-track” approach to go public, whereby they can simultaneously apply for listing via a traditional IPO and negotiate with several SPAC Promoters for listing via a SPAC. HKEX believed that the “dual-track” option could attract companies from Greater China to go public in Hong Kong. However, such arrangement may be unfair to SPAC Promoters, according to Mr. Jason Wong, as SPACs are subject to a merger deadline and would face liquidation if they fail to complete the merger within the given time frame. The “dual-track” approach would greatly increase the risk of failure in de-SPAC transaction or liquidation.

SPAC Investment Restricted to Institutional Investors during Initial IPO Likely to Increase Retail Investor Risk Exposure

The Consultation Paper proposes that only professional investors may subscribe to or trade SPAC shares prior to the completion of the de-SPAC transaction. It means that retail investors are not able to enjoy the “downside protection” during a SPAC IPO, while at the same time having to pay a premium for SPAC shares on a secondary market. The actual outcome may deviate from the Exchange’s original intended effect. Mr. Jason Wong suggests that the Exchange re-consider such requirement.

Extending the Lock-up Period Further Cements the Interests of Controlling Shareholders with Investors

Mr. Jason Wong suggested HKEX consider extending the lock-up period for the controlling shareholders of the Successor Company to 12 months after the merger, making it consistent with that of the promoters, to further strengthen the bond between the interests of the controlling shareholders and that of investors. For companies that are not profitable at the time of the merger, HKEX may consider applying the listing rules of STAR market of Mainland China, where the controlling shareholders, board of directors, and core technicians are prohibited to sell their shares before the company becoming profitable (HKEX may wish to consider introducing five or three years for the lock-up period).

Hong Kong has Great Potential to Become the Hub for Asian SPACs

Hong Kong's status as international financial centre puts it in an advantageous position in attracting global capital. With Mainland China as its hinterland, Hong Kong is able to access a reservoir of technology companies. According to the latest data published by the Chinese Ministry of Science and Technology, the number of high-tech firms in China exceeds 200,000, indicating an excess demand for financing via public listing. Furthermore, the recent regulatory issue of Didi and rising US-China tensions may mean tightened supervision on PRC enterprises listing in the US, hence making Hong Kong more appealing to mainland technology companies for listing via SPAC.

The main reason for SPACs gaining significant public attention is that they represent a new viable listing alternative which could be more convenient than traditional IPOs, as has been demonstrated in the US SPAC market. Mr. Jason Wong noted: "The core advantage of SPAC listing is maintaining proportionate attention to the interests of all parties and forming a balanced regulatory framework, thereby establishing a convenient, efficient and fair listing alternative. Excessive thresholds and restrictions may undermine the balanced regulatory framework of the SPAC listing method and reduce the appeal of SPACs in Hong Kong."

About Jason Wong

Jason Wong is the founder and CEO of Norwich Investment Limited, which is an investment company established in BVI and the sponsor of Tottenham Acquisition I Limited (Nasdaq : TOTA), a Nasdaq listed SPAC that had successfully completed its de-SPAC transaction in December 2020. As of today, Mr. Wong has successfully launched four SPACs listed on Nasdaq in the US, and is involved in two other SPAC listing applications. As a pioneer of Asian SPAC listing in the US with over 20 years of private equity investment experience in the Asia-Pacific region, Mr. Wong launched the first Asian SPAC after 2008 global financial crisis, and subsequently launched Asian SPACs including Tottenham Acquisition I Limited (NASDAQ: TOTA) and Ace Global Business Acquisition Limited (NASDAQ: ACBA). Mr. Wong leads the way in Asia in terms of the number of SPACs launched and is known in the industry as the "Asian Godfather of SPAC".

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