



In November 2018, Chinese President Xi Jinping ordered the launch of the STAR Market, his pet project that is the Asian take of the NASDAQ exchange. The aim is to focus on sustaining economic growth in China by directing capital to technological innovation as opposed to the usual method of massive infrastructure spending. The exchange was successfully launched in mid-2019, with its first debut of 25 IPOs on July 22, 2019 (Exhibit 1), and we are delighted to share this in greater detail below.

Exhibit 1: First trading day of the STAR Market for its first 25 IPOs
July 22, 2019

科创板上市首日行情							2019-07-22							
股票代码	股票名称	发行价	开盘价	最新价	涨跌幅	成交量	换手率	股票代码	股票名称	发行价	开盘价	最新价	涨跌幅	成交量
688018	乐鑫科技	62.00	152.45	152.45	+143.63%	77.89 万股		688018	乐鑫科技	62.00	152.45	152.45	+143.63%	77.89 万股
688019	安森科技	39.19	152.00	152.00	+287.65%	60.22 万股		688019	安森科技	39.19	152.00	152.00	+287.65%	60.22 万股
688020	方邦股份	53.88	106.00	106.00	+96.73%	51.83 万股		688020	方邦股份	53.88	106.00	106.00	+96.73%	51.83 万股
688022	瀚川智能	26.70	67.00	67.00	+162.14%	63.62 万股		688022	瀚川智能	26.70	67.00	67.00	+162.14%	63.62 万股
688028	沃尔康金刚石	26.68	53.88	53.88	+101.99%	74.74 万股		688028	沃尔康金刚石	26.68	53.88	53.88	+101.99%	74.74 万股
688029	南微医学科技	52.45	113.02	113.02	+115.46%	91.44 万股		688029	南微医学科技	52.45	113.02	113.02	+115.46%	91.44 万股
688033	天宜上佳	20.37	35.00	35.00	+71.65%	182.29 万股		688033	天宜上佳	20.37	35.00	35.00	+71.65%	182.29 万股
688066	北京航天宏图	17.25	43.00	43.00	+148.28%	162.89 万股		688066	北京航天宏图	17.25	43.00	43.00	+148.28%	162.89 万股
688088	虹软科技	28.88	66.00	66.00	+199.52%	178.07 万股		688088	虹软科技	28.88	66.00	66.00	+199.52%	178.07 万股
688122	西脉医疗	16.00	41.00	41.00	+173.33%	164.35 万股		688122	西脉医疗	16.00	41.00	41.00	+173.33%	164.35 万股
688333	西安铂力特	33.00	61.00	61.00	+84.85%	70.87 万股		688333	西安铂力特	33.00	61.00	61.00	+84.85%	70.87 万股
688388	高元科技	28.26	66.00	66.00	+133.55%	186.08 万股		688388	高元科技	28.26	66.00	66.00	+133.55%	186.08 万股

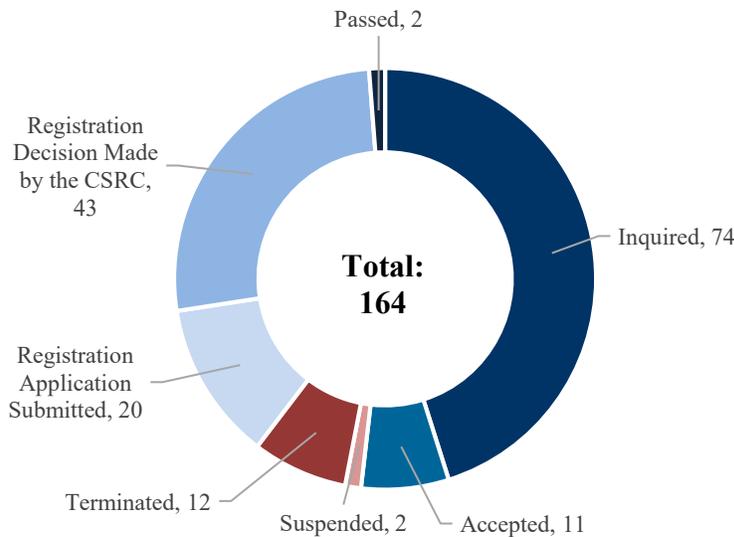
Source: Google Images

The first of its kind, the STAR Market allows unprofitable technology companies, including pre-revenue biotechnology start-ups, to go public on the Shanghai Stock Exchange (“SSE”). However, China does not intend to compromise on the quality of listings on the STAR Market, with Chinese regulators adopting a new registration-based IPO mechanism for STAR Market. The new system requires full disclosure of earnings and operational information by listing applicants, and the SSE will assess these documents before approving their IPOs. Regulators are also adopting a market-based approach to determine the valuation of the companies through preliminary pricing inquiry to decide a price range, followed by book-building through bids submitted by offline investors.

The China Securities Regulatory Commission also reviews IPO documents to ensure companies’ ability to sustain their earnings growth post-IPO, and has a final say on the pricing of shares. Several IPO applications on the new exchange have since been turned down due to failure to comply with regulations or information disclosure requirements. We believe this is a huge step in the right direction to building a more sustainable and competitive listing avenue.

Exhibit 2: Progress of registrations on the STAR Market

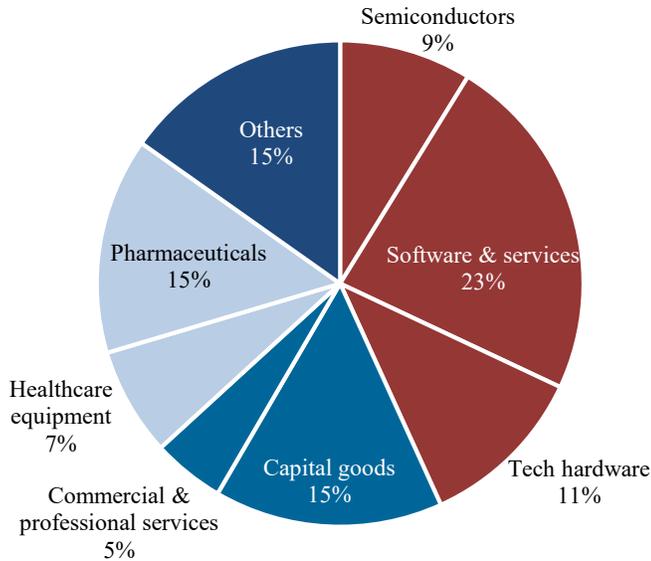
No. of applications



Source: SSE, data downloaded on Oct 14, 2019

Companies from the first batch of 125 applications were predominantly from tech, healthcare and industrials, representing 43%, 22% and 20% in terms of application count (Exhibit 3).

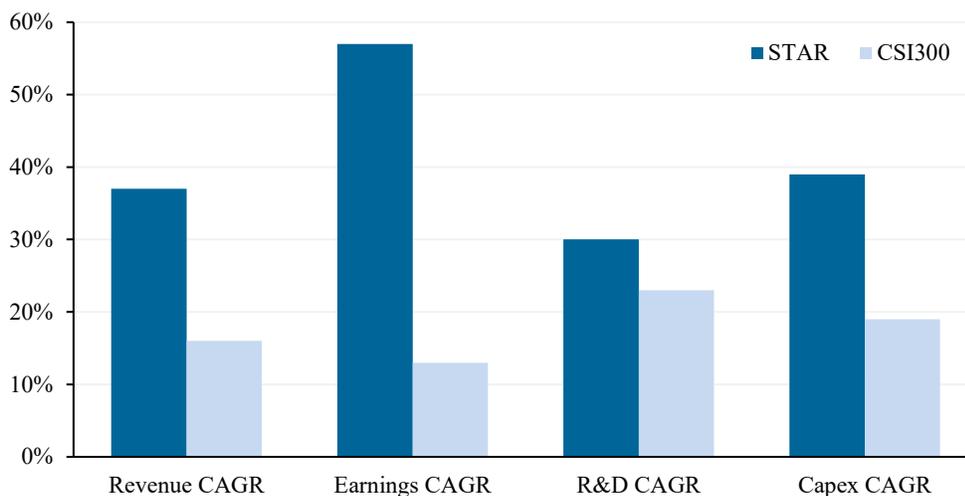
Exhibit 3: Initial 125 STAR Market applicants are concentrated in tech and healthcare
By application count (GICS industry classification by colour)



Source: SSE

The applicants tend to be faster growing in terms of revenue and earnings and had a higher R&D and capital expenditure CAGR than companies on the CSI300, an index which tracks the performance of the top 300 stocks in Shanghai and Shenzhen (Exhibit 4).

Exhibit 4: 2016-2018 fundamentals median CAGR of STAR Market applicants vs. CSI300
Percent

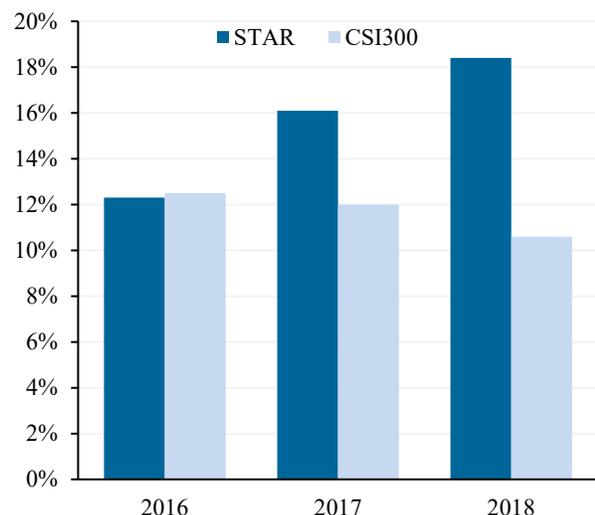


Source: FactSet, SSE

While companies in the pre-revenue and pre-earnings stage are eligible to go public on the STAR Market, most (98%) of the initial 125 applicants were already profit-making in their latest fiscal year and have been faring relatively well in terms of profit margins and ROEs (Exhibit 5 and 6) over the last 3 years. This outperformance of benchmarks in both respects by a decent 2% to 7% margin helps to alleviate investor concerns on investing in emerging companies, especially those which boast outstanding growth but lack in terms of profitability and monetization track record.

Exhibit 5: Profit margins (2016-2018)

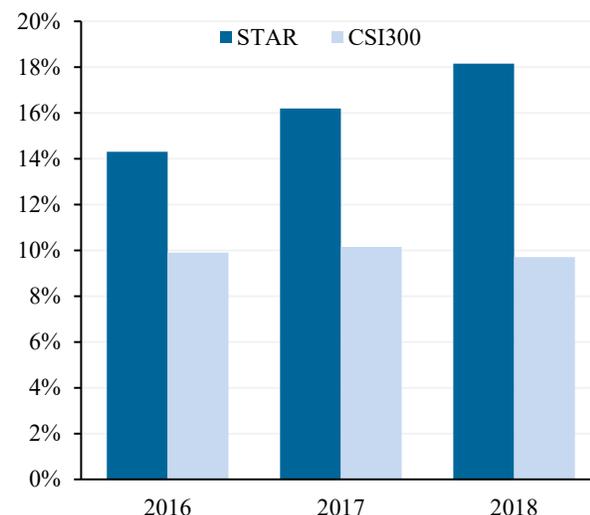
Percent



Source: FactSet, SSE

Exhibit 6: Return on equity (2016-2018)

Percent



Source: FactSet, SSE

The first 25 companies that were listed on the first day of trading have performed phenomenally (Exhibit 7). For instance, Micro-Tech Nanjing, a newly listed medical equipment manufacturer and distributor, has gained c.154% in share price since its IPO as of September 30, 2019. Returns on IPO price from the first 25 listings ranged from the worst performing at 38% (Ningbo Ronbay New Energy) to the best performing at 250% (Beijing Worldia Diamond).

As of this writing, a total of 34 companies have been listed on the STAR Market and growing, making up a total market capitalization of RMB586B. Goldman Sachs estimates that the aggregate market capitalization of the STAR Market could reach US\$2T in its mature stage and expects a steady pipeline of listing applications on the exchange.¹

In May 2019, US President Donald Trump signed an executive order targeted at China’s Huawei Technologies to ban the use of telecommunications equipment from the company, the world’s largest manufacturer of 5G equipment.² The STAR market provides a welcome alternative funding

¹ “Science-Technology Innovation Board (Part 2): What are China’s STARS?”, *Goldman Sachs*

² “US Commerce Department places China’s Huawei and 70 affiliates on trade blacklist”, *South China Morning Post*

platform for Chinese start-ups amid the US-China trade war. It is also an attempt by China to reintroduce liquidity into the tech and healthcare sector to dissuade its valuable homegrown technology companies from listing overseas. This could also have an impact on Hong Kong-based listings of Chinese companies, as they look locally for capital instead.

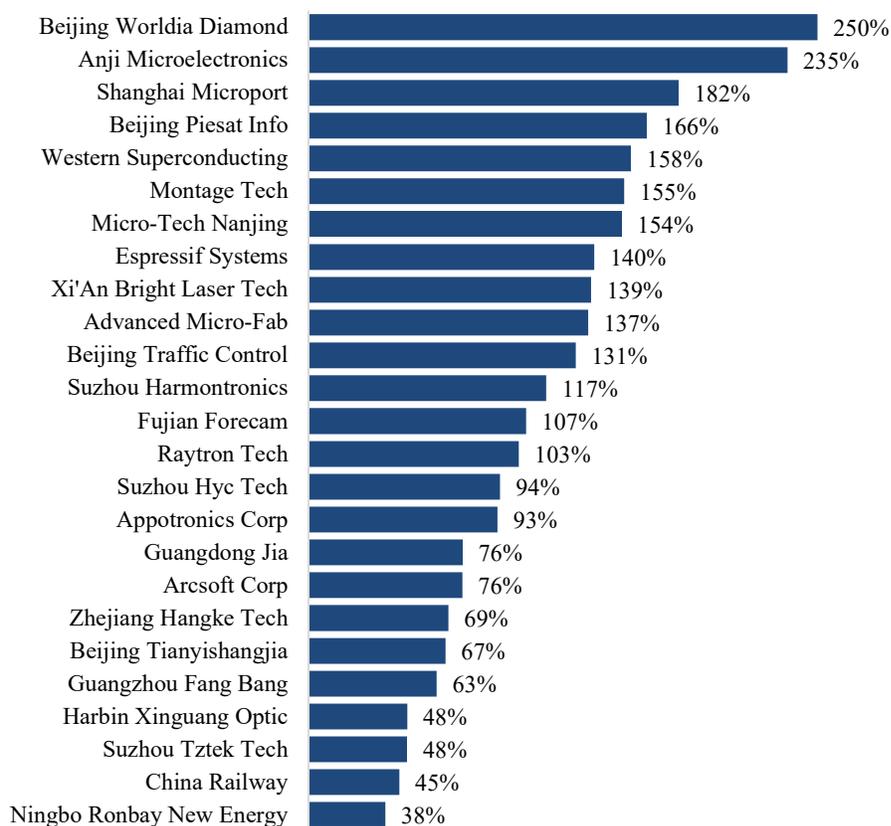
Over the last decade, the increasing openness of Asia's financial systems and the increased access that business owners have to liquidity, has enabled the region to become a more significant source of exits. This can be exemplified by China's recent decision to remove the foreign investment cap and quotas for global funds to invest in Chinese equities and bonds.

Despite this, inability to exit investments remains a key concern that many investors face when contemplating investing in Asia. A report by Bain in early-2019 highlighted that due to the high multiples which private equity investors had paid to invest in Chinese tech companies that have earned poor returns, Bain had predicted an extremely difficult exit environment for those investments.³ However, these worries have eased in the subsequent months as China's liquidity markets continued to adapt and evolve.

Overall, we expect capital markets for private equity exits in Asia to remain strong, with the financial markets constantly adapting to channel liquidity to companies with promising growth.

³ "Asia-Pacific Private Equity Report 2019", *Bain & Company*

Exhibit 7: Cumulative return of the first 25 stocks listed on the STAR market since IPO
Share price returns as at Sep 30, 2019



Source: Bloomberg

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