PROPERTY

HEADING HOME

Experts are divided over whether Dalian Wanda's move to de-list its commercial property arm in Hong Kong will spark similar actions among other companies envious of the higher valuations on the Chinese mainland

By **Danny Leung and Ray Chan**

Plans by one leading Chinese conglomerate to de-list its shares in Hong Kong have sparked speculation over a potential new going-private trend for Chinese companies listed in the territory.

Dalian Wanda Group, the property-to-entertainment conglomerate controlled by China's richest man Wang Jianlin, announced last month that it intends to privatise its flagship listed entity Dalian Wanda Commercial Properties in a deal worth at least $3.9 billion.

Hong Kong's loss could be Shanghai's or Shenzhen's gain if the entity is then relisted on a domestic stock exchange to achieve a higher equity valuation. Wang is targeting a mainland listing for the unit by August 2018.

Wanda Group's proposal to take its commercial properties unit private could be a rational decision.

Shenzhen-traded shares in Wanda Cinema Line have risen by more than 300% in price since they were listed in January 2015. In contrast, Dalian Wanda Commercial Properties's share price has largely disappointed since its initial public offering in December 2014. Having risen by an initial 60% above its HK$48 IPO price during China's stock market frenzy last spring, it largely traded below water for much of the ensuing period. In late April the shares were trading at just over HK$51.

Of course, there could be much more to it than meets the eye; China's growing hunger for leisure and entertainment needs to be juxtaposed against the vagaries of Chinese real estate market and slowing economy. One sector can be flavour of the month with investors; the other isn't.

Wang, even so, believes the commercial property business could triple in value once it completes a mainland listing.

VALUATION ARBITRAGE

The strategy of de-listing and relisting is not unusual; it has been widely adopted in recent years by Chinese companies listed on US markets. But de-listing from Hong Kong and relisting on the mainland would be something new.

There have been more than 40 take-private transactions of US-listed Chinese companies since 2013 and at least 10 of them are ongoing, Stephanie Tang, a partner with US law firm Shearman & Sterling in Hong Kong, told *FinanceAsia*.

That has come about as the Chinese stock market has exploded in recent years as both a recipient of capital and as a source of it for fast-growing capital-starved firms, creating a valuation premium for companies listed there compared with elsewhere.

The valuation gap is particularly salient in the technology,

media, and telecommunications sectors. Outdoor advertising company Focus Media, for example, delisted from the US market at a valuation of $2.7 billion in 2013 and returned to the Shenzhen exchange last year through a backdoor listing that valued the company at $7.4 billion. It was literally able to more than double its valuation within two years despite volatile global market conditions.

"Many of these companies feel their business is undervalued in the US markets," said Tang, who specialises in mergers and acquisitions and has advised a number of firms on their take-private proposals, including Bona Film Group, Jumei International, E-Commerce China Dangdang, and Momo Inc.

"It is a logical move for them to return to their home market from a long-term business development perspective, particularly when the Chinese market could fetch a higher valuation for their business," she said.

David Ludwick, a US capital markets partner with Freshfields Bruckhaus Deringer, said Chinese company owners may feel the upside for their share prices is limited in New York because American investors are not that familiar with the underlying businesses.

Indeed, most US-listed Chinese companies do not have businesses outside of China and only chose to list in the US because the Chinese capital markets were not well developed when they went public (most floated their shares before 2010).

Alibaba is, of course, one major exception to the rule. But Alibaba aside, one general perception among US investors is that bad accounting is common among Chinese companies, according to a senior banker at a bulge-bracket investment bank.

So in order to reflect the potential downside from sub-standard corporate governance, many US investors have factored in a valuation discount for Chinese companies.

Dalian Wanda's Wang Jianlin reaches for a higher vlauation on the mainland

HONG KONG TO FOLLOW?

Now with Dalian Wanda looking to go down the take-private route too, but this time in Hong Kong, there is speculation that a new trend could emerge that sees Chinese companies abandoning what for much of this decade has been the world's leading IPO hub, in favour of a mainland Chinese listing.

Shearman & Sterling's Tang believes that if Dalian Wanda makes a success of it, then others will follow. "I don't see why not," she said. "There has been a surge of [US take-private] activities after Focus Media returned to the A-share market last year. If Dalian Wanda makes it back to the Chinese market, other companies [in Hong Kong] would certainly consider that proposal."

Tang believes TMT firms listed in Hong Kong could be ripe for take-private operations because the Chinese government has implemented measures to encourage local listings of businesses in these fast-growing sectors. They include streamlining the approval process for listing applications and lowering the profitability threshold for going public.

Another favourable condition for take-private activities is the abundant cheap financing currently available in China for buyouts, Tang told *FinanceAsia*.

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Number of successful cases of relisting in China

Very often company owners and their financial supporters need a large sum of money to de-list a company and take it into private hands. The buyers also have to back the company up with additional cash, since it means losing some access to capital markets.

But the cost of short-term onshore financing has declined in recent years as domestic interest rates have tumbled and Chinese banks have emerged as financial backers.

The start of a Chinese corporate caravanserai from Hong Kong to mainland China migration is by no means a given, though, even if Dalian Wanda is successful in its de-listing/relisting quest.

Freshfields's Ludwick is among the industry experts to have doubts, not least because the migration from New York to Shanghai or Shenzhen has been far from straightforward; while more than 40 companies have so delisted, only a few have so far executed the second half of the operation by relisting in China.

"If you look closely, there have been only one successful case of relisting in China so far (Focus Media) although a number of them have delisted from the US market," Ludwick said. "There are still a lot of hurdles before they can be relisted."

One of the hurdles is the relatively long queue of listing applications currently outstanding in both the Shanghai and Shenzhen markets. According to official data, there were around 800 companies waiting for approval for a mainland listing as of the end of last year.

Philip Li, a Chinese M&A partner with Freshfields Bruckhaus Deringer, said many companies seek to list through a backdoor listing in order to bypass the long queue. However, the prices of the so-called shell companies, which are required for a backdoor listing, have surged in recent years, putting up another hurdle for them.

Chinese companies that have international private equity funds invested and pushing for a take-private have an additional headache.

"By Chinese law, international investors are forbidden to participate in Chinese IPOs in certain industries," Li said. "To successfully relist domestically, they will have to find a buyer for the stake held by foreign shareholders. But it will depend on a lot of factors including pricing and market conditions and could drag on for a long time."

Chinese law also prohibits the listing of red chip companies – Chinese companies that are incorporated outside of China. A number of relisting hopefuls in Hong Kong, including Guangzhou R&F and Red Star Macalline, are red chip companies.

In order to remove their red chip status, these companies would have to reorganize, a process that would take several months at least depending on the nature and the complexity of their business, Li said.

And if US trends are any guide, companies could face revolts from minority shareholders if they don't offer a sufficiently large buyout offer.

So Dalian Wanda's next move is worth tracking and could encourage others to follow suit, if successful. But it's way too early to judge whether it's the start of a trend that sees companies sacrifice the higher global visibility and corporate standards of Hong Kong for the perceived riches beyond the Northern Territories and further north by the East China Sea, or just a one-hit Wanda. **FA**

Red Star Macalline may follow Dalian Wanda's lead back to the mainland

"IF DALIAN WANDA MAKES A SUCCESS OF IT, THE OTHERS WILL FOLLOW"

–Stephanie Tang, Shearman & Sterling