Proceedings of the 4th International Conference on Management Research and Economic Development
DOI: 10.54254/2754-1169/2026.33643

Analysis of IPO Valuation Logic for Companies with Low VC Funding Ratio – A Case Study of Cofoe Medical Technology Co., Ltd.

Yuyou Wang

College of Economics and Management, Nanjing University of Aeronautics and Astronautics, Nanjing, China
wangyuyou@nuaa.edu.cn

Abstract. With VC/PE generally regarded as a prerequisite for IPO, how companies with low VC financing can gain recognition from the capital market and obtain reasonable valuations has become an important issue. This paper takes Cofoe Medical Technology Co., Ltd.(hereinafter Cofoe Medical) as an example and uses a combination of case analysis, literature analysis and financial analysis to study its financing structure, financial fundamentals, core capabilities, and merger and acquisition expansion process. This paper finds that Cofoe Medical is a typical company where the founder holds control and external capital financing accounts for a small proportion. Its valuation does not rely on the certification effect of VC/PE, but is supported by its sound financial condition and growth potential, its continuously developing level of commercialization, and industry dividends. Capital backing is not the sole determinant of IPO valuation; both companies and investors should conduct a comprehensive assessment across multiple dimensions to gain a more holistic understanding of the underlying logic behind the valuation.

Keywords: IPO, Cofoe Medical, Valuation logic, VC/PE

1. Introduction

In recent years, the degree of marketization in China's IPO market has steadily increased. Meanwhile, against the backdrop of macroeconomic fluctuations and a slowdown in the pace of investment and financing within the primary market, the difficulty for enterprises in securing external equity financing has increased, and VC/PE firms have become more rigorous in their project selection. Currently, a widely held market view suggests that companies backed by top-tier VC and PE firms typically benefit from high valuations, strong endorsements, and superior resources. Consequently, VC and PE backing is increasingly regarded by the market as an essential prerequisite for companies embarking on the path to an IPO.

An extensive body of literature already exists that provides a theoretical basis for the relationship between VC/PE and corporate valuation. Traditional IPO pricing theory emphasizes that information asymmetry leads to deviations in stock pricing, and the quality of intermediaries also has an impact on this [1]. Megginson and Weiss proposed a "certification effect" in venture capital, arguing that

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venture capital firms can reduce information asymmetry through reputational endorsement and professional oversight, thereby influencing IPO pricing [2]. Brav and Gompers further pointed out that, in the long run, there are also differences between VC-backed and non-VC-backed companies after listing, indicating that VC can not only affect the valuation of companies at the IPO stage [3], but also extend the growth period of companies and have an impact on various major decisions throughout the company's life cycle [4]. Many subsequent studies have become more detailed, exploring how VC/PE influences corporate quality, governance, and sustainable performance. VC support can bring higher-quality management teams, thereby supporting higher IPO valuations [5]. If VCs continue to hold shares and supervise after the IPO, it may affect corporate mergers and acquisitions [6]. Companies are also more likely to maintain a good long-term development trend [7]. Somaya and You's research indicates that the availability of VC funding can influence company valuation and IPO timing [8]. However, under certain conditions, the expansion of VC/PE supply may lower the average quality of IPO companies [9] and also have a certain negative impact on the innovation capabilities of listed companies [10].

However, some real-world examples in the capital market can illustrate that highly valued companies do not necessarily need the support of VC/PE firms with a high proportion of financing. While capital backing is important, it is not an indispensable condition for a company to obtain a high valuation. Based on this, this paper takes Cofoe Medical as an example to analyze the IPO valuation formation logic of companies with low VC ratios, and attempts to explore what factors companies can rely on to improve market recognition in the absence of high external capital backing. This paper further supplements the IPO valuation logic beyond external capital through case studies, and can also provide some reference for companies planning to go public and investors in valuation judgment.

2. Case introduction

2.1. Company profile

Cofoe Medical Technology Co., Ltd. is a medical and health enterprise with home medical devices as its core business. Its business covers health monitoring, rehabilitation aids, respiratory support, medical care and traditional Chinese medicine physiotherapy. It has now formed an integrated business system of research and development, production, sales and service. The company has established an online presence on major e-commerce platforms in China, and an offline presence covering chain pharmacies, self-operated stores, and warehouses, and is gradually expanding into businesses such as hearing solutions. The company was listed on the ChiNext Market of the Shenzhen Stock Exchange in October 2021, with the stock code 301087.

2.2. Key milestones in the development process

The predecessor of Cofoe Medical was Hunan Cofoe Medical Technology Development Co., Ltd., which was established on November 19, 2009, with a registered capital of RMB 2 million. On December 25, 2019, with the unanimous consent of all shareholders at the shareholders' meeting, Cofoe Limited was converted into a joint-stock company, with 120 million shares converted based on the audited net assets of Cofoe Limited as of October 31, 2019.

The company's founder, Zhang Min, started working in the distribution and sales of medical devices in 2000. In 2009, the company's predecessor, Hunan Cofoe Medical Technology Development Co., Ltd., was established, and Cofoe was officially established as a brand. The

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business gradually shifted to a model that combined independent brand operation and agency. From 2010 to 2017, Cofoe established or acquired multiple companies and operated under brands such as Cofoe, Keyuan, and Hao Hushi, gradually forming a business structure that combined online retail, offline warehousing and sales, and sales to major customers. It subsequently underwent financing and asset restructuring and was listed on the ChiNext Market of the Shenzhen Stock Exchange in 2021.

2.3. Financing structure and VC/PE shareholding analysis

During the IPO reporting period, the company conducted four capital increases and two equity transfers. In September 2017, Zhang Min transferred RMB 12.08 million of his RMB 19.9 million investment in Cofoe Limited to Xiezihao Investment. The company's registered capital increased from RMB 20 million to RMB 78.2 million, with the increase mainly contributed by Nie Juan, Zhang Zhiming, Keyuan Tongchuang, and Xiezihao Investment. In October 2017, Cofoe Limited's registered capital increased to RMB 85 million, with the additional RMB 6.8 million subscribed by Ningbo Huaige. In January 2019, Cofoe Limited's registered capital increased to RMB 88.28 million, with the additional RMB 3.28 million of registered capital subscribed by Xiangtan Dingxin. In July 2019, Nie Juan transferred her RMB 700,000 equity stake in Cofoe Limited to Changsha Dingxin, increasing the company's registered capital to RMB 100.696 million. The additional RMB 12.416 million in registered capital was subscribed by Hu Hongxia, Guangzhou Danlu, Hunan Bofu, Hunan Cultural Tourism, Changsha Dingxin, and Yanjin Holdings. In December 2019, Cofoe Limited was restructured into a joint-stock company.

Overall, the financing goal of Cofoe Medical is clear, which is to supplement capital to achieve listing. Therefore, it mainly conducted multiple rounds of financing in the years before listing. In addition, the founders always maintain control of the company, which is a key characteristic of the company's financing. Xiezihao Medical Investment, with a shareholding ratio of over 50%, is wholly owned by Zhang Min and Nie Juan, and the external financing introduced does not significantly weaken the founders' control over the company. External financing mainly comes from equity investment funds and individual investors, and the financing structure is relatively simple.

Besides Zhang Min and Nie Juan, and their wholly-owned Xiezihao Medical Investment, other shareholders holding more than 5% of Cofoe Medical's shares include Keyuan Tongchuang, Zhang Zhiming, Ningbo Huaige, Xiangtan Dingxin, and Changsha Dingxin. Keyuan Tongchuang was established with full funding from Zhang Min, Nie Juan and Zhang Zhiming, and its funding is unrelated to VC/PE.

Ningbo Huaige holds 8.10 million shares of Cofoe Medical, representing 6.75% of the company's total share capital before the issuance. Ningbo Huaige Health Investment Management Partnership (Limited Partnership) serves as the executive partner and fund manager of Ningbo Huaige. It has completed the registration procedures as a private fund manager and holds a 1.07% capital contribution interest in Ningbo Huaige.

Xiangtan Dingxin and Changsha Dingxin together held 5.25% of the Company's total share capital before the IPO, of which Xiangtan Dingxin held 3.91 million shares, accounting for 3.26% of the Company's total pre-IPO share capital, and Changsha Dingxin held 2.39 million shares, accounting for 1.99% of the Company's total pre-IPO share capital. The executive partner and fund manager of both Xiangtan Dingxin and Changsha Dingxin is Hunan Dingxin Taihe Equity Investment Management Co., Ltd., which has completed the registration procedures as a private fund manager and holds 3.68% of the capital contribution interests in Xiangtan Dingxin and 3.48% of the capital contribution interests in Changsha Dingxin, respectively.

Therefore, it can be seen that the proportion of VC/PE financing in Cofoe Medical's financing is not high, making it a typical company with a low proportion of VC/PE financing.

3. IPO valuation logic analysis of companies with low VC funding ratio

3.1. Financial fundamentals analysis

Cofoe Medical was officially listed in October 2021, with an offering price of RMB 93.09 per share, a price-to-earnings (P/E) ratio of 37.15, and a price-to-book (P/B) ratio of 3.29. The company's listing announcement states that 2018-2020 is the reporting period, and the following financial analysis is based on data from these three years.

During the reporting period, the company's revenue growth was extremely impressive. Operating revenue in 2018, 2019, and 2020 was approximately RMB 1.087 billion, RMB 1.462 billion, and RMB 2.375 billion, respectively. The 2020 revenue showed a significant increase, with a year-on-year growth of approximately 62.45%, demonstrating the company's strong growth potential before its IPO. This is even more evident in the net profit growth rate. Net profit for the three years was approximately RMB 66 million, RMB 124 million, and RMB 425 million, respectively, reflecting strong profit elasticity and a high level of profitability. Meanwhile, the company's cash flow growth was also considerable, with net cash flow from operating activities increasing from about RMB 6.18 million in 2018 to about RMB 496 million in 2020. This demonstrates that Cofoe Medical's cash flow and profits are well-matched, indicating that the company possesses both strong profitability and cash collection capabilities, resulting in high-quality earnings. This is crucial for enhancing its IPO valuation.

However, it should be noted that the significant increase in operating revenue and profit in 2020 was highly correlated with the impact of the COVID-19 pandemic. The increased demand for epidemic prevention materials such as thermometers, masks, and disinfection products was the main driver of the company's accelerated performance growth. The high revenue and profits during this period can support the company's IPO valuation, but since they are mainly affected by short-term factors, they are highly accidental and should not be regarded as a normal phenomenon.

3.2. Core competencies

Cofoe Medical has strategically planned and implemented an integrated online and offline sales channel. On the offline side, the company cooperates with well-known national chain pharmacies such as Yifeng, Sinopharm Group and China Nepstar, while also establishing self-operated stores such as the "Jian'er" hearing aid fitting centers. This not only meets the diverse needs of different customers but also further expands Cofoe's brand awareness. On the online side, the company has opened official flagship stores on well-known Chinese e-commerce platforms such as Tmall and JD.com, making full use of the convenience of online shopping channels to drive market expansion.

The continuous increase in online sales makes a significant contribution to the company's revenue. From 2018 to 2020, online sales accounted for 64.95%, 71.62%, and 77.82% of the company's main business revenue, with the proportion increasing year by year, which clearly shows the importance of online sales to the company. Apart from the accidental factor of the pandemic, the expansion of the online market is a significant reason for the company's revenue growth, providing substantial profits and cash flow, which largely support the company's valuation.

In terms of research and development, Cofoe Medical is not a typical R&D-driven medical device company, and most of the medical device products produced by it do not have high

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technological barriers. During the three-year reporting periods, the company's R&D expenses were RMB 11.93 million, RMB 16.01 million, and RMB 44.26 million, accounting for 1.10%, 1.10%, and 1.86% of the operating revenue, respectively. It can be seen that although the company continues to increase its R&D investment, the overall R&D intensity is not high. This shows that Cofoe Medical is not a company that achieves high valuation by creating high technological barriers through high R&D investment, but relies more on brand effect and the expansion of sales channels to achieve more profits. In other words, compared to R&D capabilities, the level of commercialization plays a greater role in the company's development.

3.3. Mergers and acquisitions expansion

As of the signing date of the prospectus, Cofoe Medical has 27 wholly-owned subsidiaries, 2 holding subsidiaries, 1 equity-invested company, and 92 branches.

In 2017, Cofoe Medical launched a large-scale asset restructuring. This is also the only major asset integration action carried out by the company since its establishment to the signing stage of the prospectus document. From 2010 to 2017, the founders, Zhang Min and Nie Juan, established or acquired a number of companies including Hangzhou Meiwen, Hunan Yajian, Guangzhou Senhe, Wuhan Kecheng, Shandong Yiyuan, Cofoe Supplies, Changsha Beida, and Guizhou Meiwen. After the asset restructuring work, all of the above companies were incorporated into Cofoe Limited. This asset restructuring has made the company's internal structure clearer, while effectively reducing competition from peers and further enhancing the overall competitiveness of Cofoe Medical.

In 2018, Hefei Haijixing was acquired. This company's main business is selling medical device products to chain pharmacies, which can provide new support for Cofoe Medical's offline sales business. In 2020, Zhuhai Acorn was acquired. This company's main business is the production and sales of oxygen concentrators, and this acquisition will enhance Cofoe Medical's competitiveness in this product market.

It is clear that Cofoe Medical carried out targeted mergers and acquisitions based on its own market positioning and actual business needs. Such expansion plans lay a solid foundation for the company's long-term development and also provide important support for its IPO valuation.

3.4. Valuation performance and market acceptance

Cofoe Medical has a total share capital of 160 million shares at the time of its IPO, with an issue price of RMB 93.09 per share. Based on this, its total market value is around RMB 14.894 billion, with an issue price-to-earnings ratio of 37.15. At that time, the average static price-to-earnings ratio of the company's industry, C35 Special Equipment Manufacturing, was 41.63. This shows that although Cofoe Medical got a high issue price in its IPO, the issue price-to-earnings ratio was slightly lower than the industry average.

Cofoe Medical received close attention during the subscription stage, with over 14 million valid online subscriptions. The winning rate was only 0.017%, and the effective subscription multiple was 5978 times, fully demonstrating the market's strong recognition of this company.

This phenomenon is closely related to the company's steady development over the years. Before going public, Cofoe Medical experienced rapid growth and expanded its business scale. It sold a wide range of medical devices through both online and offline channels, instead of relying on a single product or sales method. This business model further ensured the company's operational stability and gave investors greater confidence in its future development. Furthermore, the medical device industry gained widespread market attention during the COVID-19 pandemic. Thus, Cofoe

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Medical's valuation in the IPO market was strongly supported with the help of this positive industry sentiment.

4. Conclusion

This paper finds that although Cofoe Medical introduced some VC/PE funds before its listing, the proportion of VC/PE in the company's financing was not high in general, and the company was still controlled and dominated by the founders rather than by external capital. Therefore, the valuation logic cannot be mainly attributed to the capital backing of VC/PE. Based on an analysis of Cofoe Medical's financial fundamentals, core competencies, and characteristics of mergers and acquisitions, the company's valuation is mainly influenced by three factors. First, the company's revenue and profits are both showing a rapid upward trend, indicating strong growth potential and an optimistic future development trend. Second, the company's product range, sales channels, and market size continue to expand and form a certain brand effect, and the level of commercialization continues to develop. Third, the accidental factor of the COVID-19 pandemic boosted demand in the medical device market, providing a unique opportunity for the company's development. The case of Cofoe Medical illustrates that a company's IPO valuation is influenced by many factors besides the certification effect of VC/PE. Even with a relatively low proportion of VC/PE funding, a company can still obtain a reasonable valuation based on its clear business model.

Overall, this paper believes that companies should focus more on their own operational quality than on increasing external investment. A sound financial condition and a reliable business development path are more likely to gain the trust of investors, thus supporting the company's long-term valuation. This paper also has some limitations. For example, when discussing the impact of the medical device industry on the company's development, it only considers the short-term factor of the COVID-19 pandemic and does not take into account the driving force of factors such as population aging and further improvement of medical insurance in recent years. In the future, more potential influencing factors can be included in the research scope to more comprehensively reveal the differences in IPO valuation formation mechanisms in China's capital market.

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