

Statement on China Hongqiao: Just One Simple Truth, Right There in Plain View

November 22, 2017

China Hongqiao announced that on November 3 it had applied to High Court of Hong Kong for an interim injunction against our reports on the company.

So far we have published three reports on China Hongqiao. Anyone who has read them carefully will see that our logic is clear and our evidence is convincing. For example, we used three independent methods to estimate China Hongqiao's cost of electricity, and they arrive at very similar results. These three methods include calculations based on such data as the market price of coal, coal consumption and other costs; talking to its former employees; and relying on data from an industry consultancy.

Are we justified in concluding that China Hongqiao has committed significant financial fraud? You can easily reach an answer if you consider the following:

- The article cited by China Hongqiao to justify its low standard coal consumption actually refers to generating units whose ratio of heat-to-electricity is more than 50%, while the company's overall steam output was only 13.8% of electricity output for 2015. They are totally different ballgames.
- What kind of technological improvement could have enabled China Hongqiao's 135 MW generators to reduce their power supply standard coal consumption by 18% a year during 2010?
- Is it possible for China Hongqiao's small generating units (less than 330MW) to achieve power supply standard coal consumption 21% better than the average achieved by leading Chinese independent power producers (IPPs), which tend to use large generators (600MW or more)?
- China Hongqiao's core subsidiary, Weiqiao A&P, had disclosed its power supply **standard** coal consumption as around the 350 g/kWh level. China Hongqiao clarified that it was actually power supply **raw** coal consumption. Was Weiqiao A&P really so ignorant as to mix up these two benchmarks?
- Does it exist in this world any 330MW generator (the biggest that China Hongqiao uses) that achieves about 250 g/kWh power supply standard coal consumption?
- Can China Hongqiao's small generating units achieve production cost of electricity (even including the cost of steam) 30% less than the average of the leading IPPs?

There can be only one truth to the above questions, and it is right there in full plain view. Go ask the technicians of the IPPs. Go ask the power generating unit manufacturers. Go ask anyone familiar with the basics of the power generation industry. According to data that have come to our attention, the power supply standard coal consumption of China Hongqiao's 330MW generators was about 324 g/kWh for 2015, as much as 30% higher than that claimed by the company.

There's nothing in these three reports that we need to amend, because their logic, evidence and conclusions are complete and consistent, and are based on facts. The raw data, which we obtained from the company's former staff, detail China Hongqiao's power plant operations and corroborate our reports.

The November 5 announcement also put us on notice to appear in the High Court of Hong Kong on November 27 to defend ourselves against the interim injunction application.

Curiously, it made a reference to our report on China Hongqiao's sister company, Weiqiao Textile Company Limited (2698.HK). Weiqiao Textile has admitted in its 2016 annual report that it had made a huge advance of cash to its immediate holding company without approval by minority shareholders. This constitutes a theft of property by the controlling shareholder, an obvious criminal offense in any jurisdiction.

We all know that questioning listed companies in China often invited government persecution, with the more prominent cases being Kun Huang against Silvercorp Metals Inc. (SVM.TO)¹ and Wang Weihua against Guanghai Energy Co., Ltd. (600256.SH)².

After the publication of our first China Hongqiao report, the company said it had hired an investigative agency to trace us. This has obliged us to take additional security measures. Our court appearance would endanger the personal safety of our investigators and the former China Hongqiao employees who provided us with much information about the company.

In the hope of enlisting government help, China Hongqiao has inflated a simple question regarding the integrity of its financial statement into an attack by "American elements" relating to Alcoa Corporation (AA.N) and Rio Tinto PLC (RIO.N) on China's aluminum industry³. It is easy to envisage a more brutal government persecution than the two cases mentioned above.

To protect our staff and the former employees of China Hongqiao, we are not appearing in court November 27. For the same reason, we are not making public the raw data supplied by the former employees for now. However, if any one associated with our reports is under threat, we will publicize these data.

About Emerson Analytics

We are a group of seasoned equities analysts with many years of experience in the research of economic and political trends as well as individual stocks around the world. With background in various international investment banks, we have followed the development of the Chinese equities market right from day one.

We are determined to expose as much of the fraud in the Chinese stock market as we can. The most widespread and serious fraud is probably that undertaken by listed companies, in fabricating non-existent businesses and stealing shareholders money, among other tricks.

¹ <http://nationalpost.com/news/canada/jailed-in-a-chinese-hellhole-a-b-c-short-seller-strikes-back-with-lawsuit-against-mining-company>

² <https://www.marketwatch.com/story/chinas-chilling-effect-on-investor-research-2013-10-29>

³ <http://money.163.com/17/0401/15/CGURSQCC002580S6.html>