



Weiqliao Textile – Parent Company's Secret ATM

August 21, 2017

Weiqliao Textile Company Limited (2698.HK) has finally come "clean" with its 2016 full year results, and our analysis also shows that it has been its parent company's secret ATM (automatic teller machine) for years!

It is now clear that Weiqliao Textile, just like its sister company, China Hongqiao Group Limited (1378.HK), has been mismanaged by their common controlling shareholder Zhang Shiping. Emerson Analytics published a report February 28 strongly condemning China Hongqiao's fraudulent accounting practices.

Weiqliao Textile's 2016 results were audited by Shine Wing who replaced Ernst and Young at the eleventh hour. EY was also China Hongqiao's auditor but resigned after our report. The recently announced 2016 results not only raise serious governance issues but cast doubts on the existence of its allegedly huge pile of cash and bank balances, and by extension, the whole integrity of its financial statements.

Exhibit 1 – Weiqliao Textile's huge "cash-flows" with its holding company

	2016 RMB'000	2015 RMB'000 (restated)
INVESTING ACTIVITIES		
Purchase of property, plant and equipment	(3,790,199)	(373,708)
Advance to immediate holding company	(4,772,465)	–
Payment to acquire land use right	(104,030)	–
(Increase) decrease in pledged deposits	(32,040)	22,397
Government grant received	869	–
Dividends received from an associate	4,125	8,387
Bank interest income received	32,918	40,518
Gain on available-for-sale investments	–	49,726
Proceeds from disposal of property, plant and equipment	123,837	54,813
Proceed from disposal (acquisition) of available-for-sale investments	1,384,938	(1,298,000)
Repayment from immediate holding company	1,845,836	–
Fund inflow from immediate holding company	3,820,000	900,000
Fund outflow from immediate holding company	(3,820,000)	(900,000)

Source: Weiqliao Textile

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Exhibit 1 above shows part of Weiqiao Textile's statement of cash flows during 2016. We can see that the listco had huge "cash-flows" with its immediate holding company during the year and in 2015 (which were previously undisclosed). Why are these "cash-flows" part of investing activities? Further, to say "cash-flows" implies that the cash actually exists. This is a heroic assumption to make, given that the counterparty is the holding company.

We believe investors and regulators should focus on the following issues.

- The "fund inflow and fund outflow with the holding company" amounted to Rmb3.8bn in 2016. According to Weiqiao Textile, the parent company had to transfer Rmb3.8bn to the listco's accounts in order to comply with the "[Guidelines for Commercial Banks on the Management of Risks Associated with the Granting of Credit to Group Customers \(商業銀行集團客戶授信業務風險管理指引\)](#)". The "GOOD NEWS" is that the listco returned every single penny to the parent company within two business days;
- The company's "advance to immediate holding company" amounted to Rmb4.8bn during 2016, or as much as 42% of its self-proclaimed year-end cash and bank balances. Weiqiao Textile says the money came from its own bank facilities. Does this "indirect" source of cash plundering sound more compliant with Listing Rules, or more acceptable to investors? The "GOOD NEWS" is that the holding company repaid Rmb1.8bn during the year, while the remaining Rmb3.0bn outstanding at the end of the year was settled in April 2017; and
- Such huge "cash-flows" with the holding company had never been disclosed to, let alone approved by, independent shareholders beforehand. And the company dares put up such a ridiculous lie as "due to the deviation in the understanding of the Listing Rules of relevant management of the Company". The "GOOD NEWS" is that "the Company will convene meetings to seek approval for the past fund transactions".

Is there really any regulatory supervision over this company? The acid test of cash and bank balances below shows that Weiqiao Textile has been exaggerating its cash and bank balances for years. More likely, though, the controlling shareholder has been plundering Weiqiao Textile's huge cash at will all along.

Exhibit 2 – Weiqiao Textile's average deposit interest rates, 2010-16

Year end Dec 31 (Rmb m)	2009	10H1	2010	11H1	2011	12H1	2012	13H1	2013	14H1	2014	15H1	2015	16H1	2016
Interest income			59		34		21		30		33		41		82
Cash	4,987	6,049	4,174	2,523	2,615	4,251	7,714	4,820	10,353	9,703	10,795	11,246	12,091	8,772	11,383
Average Cash			5,070		3,104		4,860		7,629		10,284		11,377		10,749
Effective deposit interest rate			1.15%		1.08%		0.42%		0.39%		0.32%		0.36%		0.77%

Source: Emerson Analytics

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Given our analysis on China Hongqiao, it doesn't surprise us that Weiqiao Textile also turns out to be a fraud, and we call on the Securities and Futures Commission of Hong Kong to take all necessary regulatory actions against both companies.

In a little over three years since April 2014, Emerson Analytics has published a number of reports exposing serious financial frauds at seven listed companies. We are particularly disappointed with the following phenomena:

- The Stock Exchange of Hong Kong, as the direct regulator of listed companies, has ignored its duty in safeguarding the integrity of the Hong Kong financial markets. They are willing to accept any absurd excuse put up by these fraudsters. If HKEX's objective is simply to get trading resumed ASAP so that it can earn more transaction levies, fraudsters will come up with even more absurd excuses; and
- So far, none of the senior executives of the listcos or their related intermediates (particularly the auditors but also the bankers, valuers and lawyers) has been held accountable by the regulators. In Weiqiao Textile's case, how did EY do its audit such that it couldn't detect the huge cash plundering? Is Weiqiao Textile senior management fulfilling its duty toward the public shareholders, or are they deliberately lying? The fact that so far no senior executive has been held responsible is the key reason why some listcos are blatantly falsifying their accounts.

Disclaimer

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.

In exposing these crimes we challenge the listed companies to prove the integrity of their announcements and financial statements. The listed companies, of course, want everybody to believe that their announcements and financial statements are true. Their auditors, employees, independent directors, lawyers, shareholders and even the general public all hope that these announcements and financial statements are true.

We have made our best effort to ascertain that everything we say in this report is accurate. We have obtained our information from public sources that we believe to be accurate and reliable, or from sources whom we believe are not insiders or connected parties to the companies mentioned herein. However, we are certainly NOT in the business of making investment recommendations. This is not an investment report and should not be regarded as such. Read and use our reports at your own risk. Most important of all, DO YOUR OWN RESEARCH BEFORE YOU COMMIT OTHER PEOPLE'S MONEY.

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