

## Realord Group – Real Lord of the Lies

August 21, 2019

The Basics	
Ticker:	1196.HK
Recent Price:	HK\$4.25
Market Cap:	HK\$6.1bn

Emerson Analytics Forecast
<b><i>Bankruptcy</i></b>

Controlling shareholder and chairman Lin Xiaohui had struggled to keep Realord Group above water after taking it over in late 2014. His scheme involved two properties in Shenzhen carried on the books of his privately held company at 6.0x the actual invested amount. Such properties were then further inflated by 1.7x in an acquisition valuation that ballooned to 16.4x the original cost. This allowed him to pull a HK\$7.9bn trick in April 2018 by stuffing minority shareholders with his rubbish, thus saving his own skin but pushing the listco to the brink of bankruptcy.

The Guanlan and Guangming Properties located in the outskirts of Shenzhen consist mainly of retail, commercial and office space as well as some carparks. The office space at the Guangming Property was valued at a low yield of 0.7%. This implies that the investment could be recouped in 135 years, three times the remaining life of the leasehold site itself.

The commercial carparks at the Guangming Property and the residential carparks at the Guanlan Property are both incapable of being sold. The carparks at the Guanlan Property are said to worth more than the residential apartments at Realord Villas, where the Guanlan Property is located.

But the more important thing is that Lin has stuffed the company with worthless assets: the commercial and office buildings remain vacant two years after completion, the retail arcade has only one shop in operation, and only 10% of the carparks at the Guanlan Property are leased out when the residential

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blocks there are probably 20% occupied. It is difficult for the company to achieve positive cashflow from them.

Likewise, other operations such as scrap metal recycling business in mainland China had inflated revenue by almost 150% and profit by five times in 2018. Our site visit to Realord Group factory in Wuzhou Park showed that it had ceased operation on tighter environmental laws in China. The real revenue of vehicle parts segment from mainland China was only 4% of reported during the 2015-18 period.

The property acquisition was mostly financed by bank borrowings, which enabled Lin to pocket \$5.8bn of cash so far but left the company with net debts of \$6.8bn or 231% of equity at the end of 2018. The company's cash can only afford bank interest this year and next.

Realord Group also exhibits a number of telltale signs of a company doctoring its books:

- frequent change of auditors (BDO audited the 2011-14 accounts and resigned in July 2015, but the successor EY lasted only two years and was replaced by Deloitte in mid-2017);
- two CFOs have left, one in July 2016 and the other September 2017 (when the outrageously high property valuation was being done);
- poor governance structure with only three executive directors who are all connected: wife and brother of chairman; and
- chairman obtained control in listco via backdoor listing.

We calculate that properties acquired in April 2018 are worth only \$1.6bn. This means Realord Group's net asset value was really a negative \$3.2bn. BANKRUPTCY is the only way forward.

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## 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.**

**We and/or our associates/partners may have long or short positions in the equities and/or their derivatives at the time of publication of our reports, and we and/or our associates/partners may maintain or change our positions at any time.**

# Realord Group – Real Lord of the Lies

## Part 1 Realord Group Checks the Box of Financial Fraud

Realord Group Holdings Limited (Realord Group) was renamed from the original Cheong Ming Investments Limited in September 2014, about two to three months after Lin Xiaohui acquired control and took over as chairman of the board.

### 1.1 Investment Properties are 80% of Total Assets

Exhibit 1 below presents Realord Group's revenue breakdown by business segments during 2016-18. Of the six, commercial printing, hangtag and property investment are the original businesses prior to Lin's takeover. Motor vehicle parts (MVP), financial services and environmental protection (EP) are new businesses started by Lin. In terms of revenue, EP contributed as much as 70% of the total in 2018.

<b>Year end Dec 31 (HK\$ m)</b>	<b>2016</b>	<b>2017</b>	<b>2018</b>	<b>2018 Mix</b>
Commercial printing	73	70	82	<b>10%</b>
Hangtag	8	3	1	<b>0%</b>
MVP	101	87	127	<b>16%</b>
Financial services	11	11	10	<b>1%</b>
Property investment	17	20	20	<b>2%</b>
EP	-	572	571	<b>70%</b>
<b>Total</b>	<b>210</b>	<b>763</b>	<b>811</b>	<b>100%</b>

Source: Realord Group

Geographically, the commercial printing, hangtag and financial services segments derived all of their revenue from Hong Kong in 2018. The MVP segment derived 67% of its revenue from mainland China and the rest from Hong Kong, whereas the property investment and EP segments were essentially mainland-based businesses.

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**Exhibit 2 – Revenue segment – geographical breakdown 2018**

Year end Dec 31 (HK\$ m)	Mainland China	Hong Kong	Other countries	Total
Commercial printing	-	82	-	82
Hangtag	-	1	-	1
MVP	85	42	-	127
Financial services	-	10	-	10
Property investment	19	1	-	20
EP	569	-	2	571
<b>Total</b>	<b>673</b>	<b>136</b>	<b>2</b>	<b>811</b>

Source: Realord Group

Realord Group reported total assets of HK\$11.4bn as at the end of 2018, with investment properties accounting for \$9.1bn or 80% of the total. Among all the properties held, the Guanlan and Guangming Properties, acquired in April 2018, accounted for 68% of total assets.

**Exhibit 3 – Investment properties breakdown (HK\$ m) 2018**

Property	Location	Book value	As % of total assets
Guanlan Property	Realord Villas, Guanlan Town, Longhua District, Shenzhen	4,469	39%
Guangming Property	Northwestern of Dongming Avenue, Guangming District, Shenzhen	3,292	29%
Industrial complex at Qiankeng Industrial Zone	Fumin Community, Guanlan Town, Longhua District, Shenzhen	585	5%
House No. 25, Villa Bel-Air	Bel-Air on the Peak, Island South, Hong Kong	353	3%
Industrial complex at Zhangkengjing Community	No. 5 Fuye Road, Guanlan Town, Longhua District, Shenzhen	192	2%
Unit 3306-3310, Excellence Time Square	Junction of Yi Tian Road and Fu Hua Road, Futian District, Shenzhen	92	1%
Others		98	1%
<b>Total</b>		<b>9,082</b>	<b>80%</b>

Source: Realord Group

## 1.2 Backdoor Listing in Hong Kong

The emergence and growth of Realord Group over the last few years exhibit most of the common features of financial fraud. We can see that it checks all the boxes in Exhibit 4 below, and we will examine them in great details one by one.

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## Exhibit 4 – Realord Group checks the boxes of financial fraud

- ☑ Backdoor listing in Hong Kong
- ☑ Auditors resigned consecutively
- ☑ CFO and company secretary resigned consecutively
- ☑ Poor earnings quality: earnings with no cash flow
- ☑ Massive and increasing debt load

Source: Emerson Analytics

Realord Group was backdoor listed in Hong Kong, and its core businesses were mostly acquired, mainly from connected parties. These acquisitions include:

- Realord Manureen Securities Limited, which undertakes stockbroking business in Hong Kong, from Su Jiaohua, an executive director of Realord Group and wife of Lin, for \$19m in 2014;
- A luxurious house located at 25 Villa Bel-Air in Hong Kong for \$225m in 2015;
- Two industrial complexes at Zhangkengjing Community and Qiankeng Industrial Zone in Shenzhen for \$93m in 2015 and \$282m in 2016, respectively, in order to participate in the rehabilitation of Shenzhen's industrial zones;
- A 60% stake in the EP business for \$49m in 2017; and
- The Guanlan and Guangming Properties for Rmb\$6,220m from Lin and his wife in 2018.

### 1.3 EY Resigned as Auditors in July 2017

Realord Group was audited by BDO from 2011 through 2014. On July 7, 2015, BDO resigned as auditor and Ernst and Young was appointed as the new auditor. The company claimed that "a rotation of auditor will help enhance the independence of the auditor"<sup>1</sup>. On July 10, 2017, only two years later, EY resigned as auditor because "EY could not reach a consensus on the audit fee"<sup>2</sup>.

We all know that auditors rarely resign as a result of fee disputes. There is sufficient competition among the Big Four and second tier audit firms to ensure they don't nickel and dime clients. "Fee disputes" are almost exclusively used as a means for auditors to resign without being forced to alert regulators of possible financial irregularities.

<sup>1</sup> <http://www3.hkexnews.hk/listedco/listconews/SEHK/2015/0707/LTN201507071253.pdf>

<sup>2</sup> <http://www3.hkexnews.hk/listedco/listconews/SEHK/2017/0710/LTN20170710706.pdf>

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In fact, a paper released in 2015 by the Hong Kong Institute of Certified Public Accountants states the following:

*In many cases, fee disputes are stated to be the reason for the change. Concern has been expressed that certain auditors have been relying on purported fee disputes to disguise the real reasons for the change. As a result, potentially significant and fundamental matters about the listed issuer may not be disclosed to investors and creditors and the market is not therefore being kept fully informed.<sup>3</sup>*

Auditor resignation is an obvious red flag of Realord Group's financial irregularities. Deloitte Touche Tohmatsu is currently the auditor.

## 1.4 Poor Governance Structure and Serial Resignations of CFO

Realord Group currently has three executive directors. Other than Lin and his wife Su, the other executive director is Lin Xiaodong, brother of the chairman. This is clearly a very bad corporate governance structure.

In addition to these three executive directors and three independent non-executive directors, the only member of the senior management team mentioned by the company is the chief financial officer (CFO). Since 2014, however, two CFOs have resigned:

- On July 11, 2016, Tsang Chin Pang tendered his resignation as CFO, company secretary and authorized representative of the company. He was replaced by Chan Ying Kay;
- Barely one year later, on September 12, 2017, Chan Ying Kay tendered his resignation as CFO, company secretary and authorized representative of the company.

Just like the resignation of external auditors, consecutive departures of the CFO are a clear sign of major financial problems at a company.

## 1.5 Bogus Earnings and Massive Debt Load

Realord Group has fabricated a massive 10.8x increase in net profit over the 2015-18 period, from \$33m to \$384m. However, it has suffered from negative operating cash flow (opCF) every single year during the period in question. Despite a cumulative pretax profit of \$979m during those four years, the company's opCF was negative \$379m. This is mainly because most of the profit came from non-cash items such as fair value gains on investment properties.

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<sup>3</sup> [http://app1.hkicpa.org.hk/ebook/HKSA\\_Members\\_Handbook\\_Master/volumeI/COErevised.pdf](http://app1.hkicpa.org.hk/ebook/HKSA_Members_Handbook_Master/volumeI/COErevised.pdf), p.157

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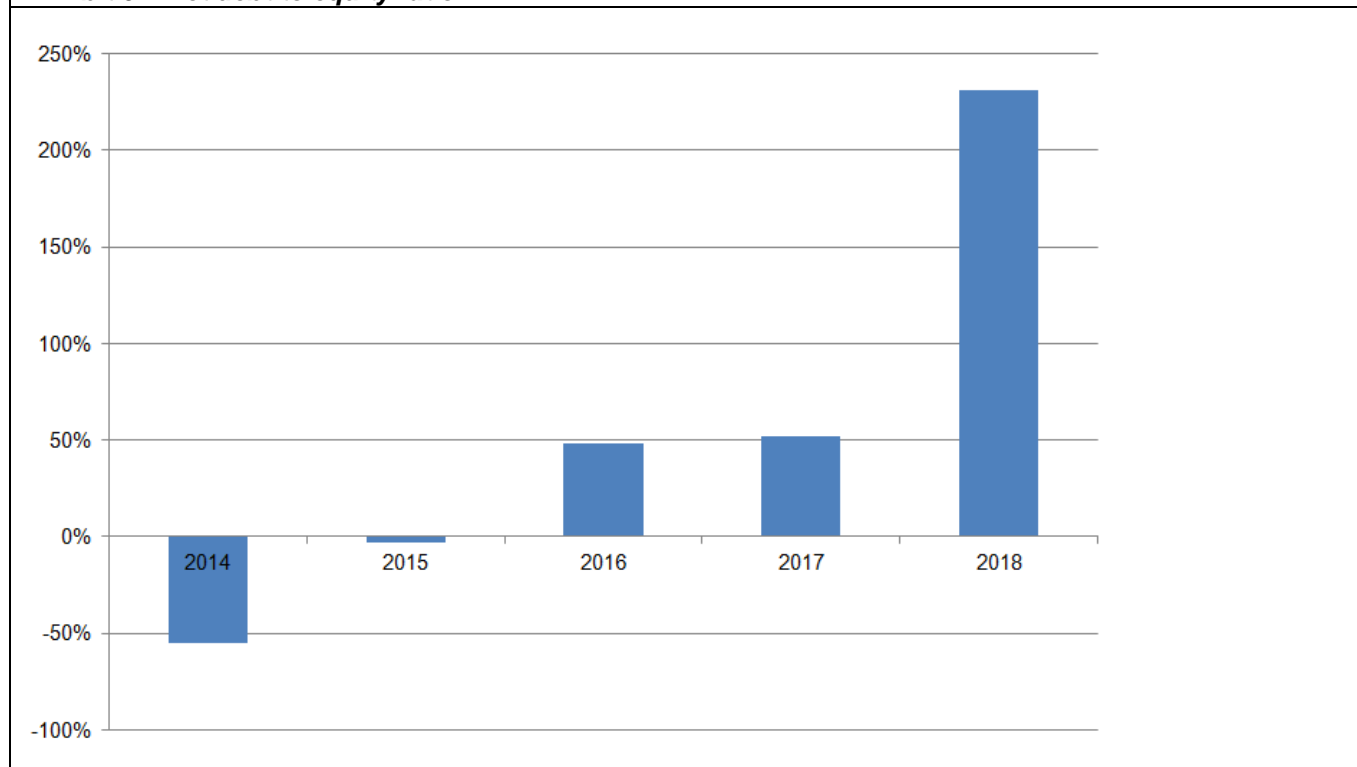
**Exhibit 5 – Reported pretax profit, actual pretax profit and opCF, 2015-18**

Year end Dec 31 (HK\$ m)	2015	2016	2017	2018	Total
Pretax profit – reported	48	208	166	556	<b>979</b>
- Fair value gains on investment properties	-90	-270	-156	-671	<b>-1,188</b>
- Exchange gains	0	-10	3	-265	<b>-272</b>
<b>= Pretax profit – actual</b>	<b>-42</b>	<b>-72</b>	<b>14</b>	<b>-380</b>	<b>-481</b>
opCF	-203	-97	-36	-43	<b>-379</b>

Source: Realord Group

At the end of 2018, Realord Group reported interest-bearing debts of \$7,675m, including \$821m from its ultimate holding company. The shareholder's loan was partly replaced by bank loans in early 2019.<sup>4</sup> Since 2014, Realord Group has seen its net debt to equity ratio rising steadily, to an astonishing 231% at the end of 2018.

**Exhibit 6 – Net debt to equity ratio**



Source: Realord Group

<sup>4</sup> <https://www1.hkexnews.hk/listedco/listconews/sehk/2019/0426/ln201904262653.pdf>, p.204

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## Part 2 Guanlan and Guangming Properties: Absurd Valuation

On March 22, 2018, Realord Group announced the acquisition of two Shenzhen property complexes, the so-called Guanlan and Guangming Properties for Rmb6,220m from chairman Lin and his wife, implying an outrageous 15.4x valuation surplus.

A few simple ratios tell us that Lin has perpetrated a serious financial crime: (i) The office buildings of the Guangming Property are valued at an absurdly low yield of 0.74%; and (ii) Carparks at the Guanlan Property are more expensive than the residential units upstairs, with a shockingly low effective yield of 0.07%.

### 2.1 Overview of Guanlan and Guangming Properties

The general conditions of the two properties are shown below in Exhibit 7.

The Guanlan Property is part of Realord Villas. Realord Villas has a total gross floor area (GFA) of 230,501 square meters (sm), of which only 51,039sm belong to the Guanlan Property. The assets being sold to the listco consist of a shopping arcade for retail use, as well as a commercial/office building with the basement to 6/F for commercial use and 7-26/F for office use. The rest of Realord Villas has been transferred to the local government. Details of the Realord Villas can be found in [Appendix I Realord Villas Overall Plan](#).

The Guangming Property takes up 8,000sm of a site, with the remaining 12,599.44sm being vacant at present. It consists of two blocks of office buildings, one 26 storeys high and the other four.

<b>Exhibit 7 – Overview of Guanlan and Guangming Properties</b>		
	<b>Guanlan Property</b>	<b>Guangming Property</b>
Land use	Residential use	Industrial use
Site area (sm)	32,987.14	20,599.44
Land lease terms	70 years October 10, 2012-October 9, 2082	50 years March 17, 2009-March 16, 2059
Total GFA (sm)	51,039	53,973
Completion	June 2017	End of 2017
Main structures	One shopping arcade One commercial/office building 1,012 carparks	Two office buildings 315 carparks
Furbishing	Rough cast	Rough cast
Occupancy	Vacant	Vacant

Source: Realord Group

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The acquisition announcement contains many typo and translation errors, some of which are in fact serious mistakes. For example, the actual site area of Realord Villas is 32,987.14sm, but is put at 329,870.14sm<sup>5</sup> in the announcement, 10x the real value.

The total consideration of the acquisition was arrived at with reference to the Rmb6,220m valuation of these two properties as of September 30, 2017. According to the Valuation Report in the acquisition announcement, the appraised value as of December 31, 2017 was Rmb6,400m, as shown in Exhibit 8 below.

	Guanlan Property	Guangming Property	Total / Average
<b>sm/lot</b>			
Retail use	9,671 <sup>*</sup>	-	<b>9,671</b>
Commercial use	16,716	-	<b>16,716</b>
Office use	24,652 <sup>#</sup>	53,973	<b>78,625</b>
Carparks	1,012	315	<b>1,327</b>
<b>Rmb/sm (Rmb/lot)</b>			
Retail use	93,000	-	<b>93,000</b>
Commercial use	52,000	-	<b>52,000</b>
Office use	53,000	51,700	<b>52,108</b>
Carparks	400,000	400,000	<b>400,000</b>
<b>Valuation (Rmb m)</b>	<b>3,480</b>	<b>2,916</b>	<b>6,396</b>
Retail use	899	-	<b>899</b>
Commercial use	869	-	<b>869</b>
Office use	1,307	2,790	<b>4,097</b>
Carparks	405	126	<b>531</b>

Sources: Realord Group, Emerson Analytics

# Total GFA of office space from Appendix I Realord Villas Overall Plan

\* With total GFA of 51,039sm, the amount of retail space, X sm, can be calculated with the formula  $X * 93,000 + (51,039 - 24,652 - X) * 52,000 + 24,652 * 53,000 + 1,012 * 400,000 = 3,480,000,000$ . Accordingly, the retail space is 9,671sm.

## 2.2 Acquisition Valuation a Staggering 16.4x Actual Invested Amount

(1) Book value 6.0x the actual invested amount while appraised value 16.4x

The book value of the Guanlan and Guangming Properties was \$2,735m or Rmb2,278m as at December 31, 2017<sup>6</sup>, as audited by Deloitte. Our investigations reveal that the actual costs of the two properties were only Rmb284m and Rmb96m, respectively, for a total of Rmb380m. We present in Exhibit 9 below the actual invested amount, the book value and the appraised value of the two properties.

<sup>5</sup> <https://www1.hkexnews.hk/listedco/listconews/sehk/2018/0322/tn201803221147.pdf>, VI-6

<sup>6</sup> <https://www1.hkexnews.hk/listedco/listconews/sehk/2018/0322/tn201803221147.pdf>, IV-6

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**Exhibit 9 – Appraised value 16.4x actual costs**

	Actual investment (Rmb m)	Book value (Rmb m)	Book value / actual investment (x)	Appraised value (Rmb m)	Appraised value / actual investment (x)
Guanlan Property	284	-	-	3,300	11.6
Guangming Property	96	-	-	2,920	30.4
<b>Total</b>	<b>380</b>	<b>2,278</b>	<b>6.0</b>	<b>6,220</b>	<b>16.4</b>

Sources: Realord Group, Emerson Analytics

As can be seen from Exhibit 9, the book value was 6.0x the actual investment and the appraised value 16.4x. Was the book value exaggerated in advance so that the appraised value would show a more palatable 1.7x appreciation? Our experience in investigating financial fraud suggests that Lin probably had aimed to stuff minority shareholders with the two properties at about 6.0x original cost, hence the fabricated book value. Subsequently, he probably realized, most likely with the help of the banks and other "professional advisers", that he could fetch more. As a result, the appraised value further inflated the fraudulent book value by 1.7x.

## How could Deloitte sign off Rmb2,278m of book value against the Rmb380m actual cost?

(2) Guanlan Property actual invested amount only Rmb284m or 8.6% of valuation

According to the [建設項目環境影響報告書簡本](#) (Abridged Construction Project Environmental Impact Report), the actual invested amount of Realord Villas was Rmb1,080m.

**Exhibit 10 – Actual invested amount of Realord Villas Rmb1,080m**

建设项目环境影响报告书简本	
<p>至观益路，东临澜清二路，项目四至情况详见图 2-1，项目具体位置详见图 2-2。建设工程总用地面积为 32987.14m<sup>2</sup>，总建筑面积约为 229889m<sup>2</sup>，<b>项目总投资 10.8 亿元人民币</b>，<b>Total invested amount was Rmb1,080m</b> 0.3%。预计施工期为 2012 年 10 月至 2014 年 12 月，共 26 个月。</p> <p>建设内容包括：（1）商业、商务办公楼：A、B、C、D、E、F、G 栋 1 层、部分-1 层共同形成商业区，A 栋-1-4 层均为商业，5-26 层为商务办公区。（2）配套服务设施：公交首末站、幼儿园、物业管理用房、社区服务站、社区健康服务中心、社区居委会、社区警务室、公共厕所、垃圾收集站、邮政所、社区体育活动中心。（3）地下车库：地下一层至地下二层。（4）人才安居居住楼：</p>	

Source: <https://max.book118.com/html/2018/0428/163509669.shtml>

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According to the acquisition announcement, the residential buildings of Realord Villas (hereinafter referred to as Residential Buildings) had been transferred to the local government in September 2017 at cost, or Rmb796m<sup>7</sup>.

It follows that the actual invested amount of the Guanlan Property was merely Rmb284m (= 1,080 – 796). This represents just 8.6% of the appraised amount.

(3) *Guangming Property actual invested amount only Rmb96m or 3.3% of valuation*

According to the [偉祿科技園環境保護驗收監測表](#) (Monitoring Tables of the Environmental Protection Inspection of Realord Science Park (i.e. the Guangming Property)), the actual invested amount of the Guangming Property was only Rmb96m, merely 3.3% of the Rmb2,920m appraised value.

The actual invested amount of Rmb96m for 53,973sm of total GFA (which turned out to be 4.8% more than the designed total GFA) implies a unit cost of Rmb1,779/sm, which matches the cost of similar buildings in Shenzhen.

**Exhibit 11 – Guangming Property actual invested amount only Rmb96m**

建设项目名称	伟祿科技园报建项目		
建设单位名称	深圳市伟祿科技股份有限公司		
建设单位地址	深圳市福田区上梅林梅华路 105 号国际电子商务产业园科技大厦 2 楼		
建设项目主管部门	——		
建设项目性质	新建		
主要产品名称	总用地面积 20599.44m <sup>2</sup> , 总建筑面积 51499 m <sup>2</sup>		
设计生产能力	1 栋研发办公楼 14 层 (建有地下室)、2 栋厂房 6 层		
实际生产能力	1 栋研发办公楼 14 层 (建有地下室)		
环评时间	2011 年 7 月 25 日	开工日期	2011 年 10 月
投入试生产时间	——	现场监测时间	2017 年 12 月 25~26 日
环评报告表审批部门	深圳市宝安区环境保护和水务局	环评报告表编制单位	深圳市宗兴环保科技有限公司
环保设施设计单位	——	环保设施施工单位	——
		环保投资总概算	91 万元 比例 0.95%
		实际环保投资	91 万元 比例 0.95%
	(一) 验收监测依据		

Source: <http://apps.szgm.gov.cn/szgm/132100/152326/152474/152502/1135405/index.html>, third attachment

Note: This table mistakenly states the project as consisting of one 14-storey office building and two 6-storey factory buildings

## 2.3 The Absurd "Capable of Being Sold" and "Direct Comparison Method"

The valuation report in the acquisition announcement says that "We assume that the property is capable of being sold in the open market... We have valued the property using direct comparison method". Applied to the carparks, the assumption and comparison method are totally absurd.

<sup>7</sup> <https://www1.hkexnews.hk/listedco/listconews/sehk/2018/0322/tn201803221147.pdf>, p.17

# Realord Group – Real Lord of the Lies

Carparks may generally be categorized into commercial carparks and residential carparks. According to the acquisition announcement, commercial carparks, such as those at the Guangming Property, are normally not for sale as they are one of the facilities complement to the commercial buildings. What about residential carparks in Shenzhen?

Shenzhen property agents told Emerson Analytics that there has been virtually no sale of carparks in residential estates for many years. They also told us that residents usually spend no more than Rmb250 a month<sup>8</sup> to park their cars at the residential estate where they live. Our investigators asked around the residential estates near the Guanlan Property, and confirmed the property agents' descriptions.

In Shenzhen there are two types of residential carparks – most of them are ancillary carparks that are required under the project approval, with very few supplementary carparks that are rarely granted. Ancillary carparks are owned by all residential owners collectively and are not transferable<sup>9</sup>. Realord Group staff told Emerson Analytics investigators that carparks at the Guanlan Property are not for sale either.

Clearly, the assumption that "the property is capable of being sold" is utter rubbish for both commercial carparks and residential carparks.

The acquisition announcement says that "for the carparks comparables, they are extracted from a website that specialised in carpark transactions in Shenzhen i.e. <http://sz.chewei.cn/>". From Exhibit 12 below, there are only two carpark sales advertisements in Shenzhen since mid-2018. With so few samples, what's the point of this "direct comparison method"?

**Exhibit 12 – Only 2 carpark sales advertisements since mid-2018**

标题	所在小区	总价	时间
南山蛇口南海玫瑰花园1期车位 联系人: 17722678717	南海玫瑰花园1期	53 万元	10小时前
惠州市富力南昆山二期洋房车位急售!低于市场价。 联系人: 何先生	惠州市富力南昆山二期	15 万元	07-05
深圳市南山区大冲城市花园车位一个出售 联系人: 刘生	城市花园	30 万元	06-01
惠州市惠阳区天麓花园地下车位 联系人: 陈先生	天麓花园	11 万元	01-30
惠州市龙门县碧桂园南昆大观车位出售 联系人: 何先生	碧桂园南昆大观	16 万元	01-30
世贸广场车位出售 联系人: 舒先生	世贸广场	27 万元	06-20

车位出租、车位出售、车位求租、车位求购就在车位网!

[免费发布信息](#)

焦点信息

联系我们

☎ 电话:13959292993

✉ 邮箱:kefu@chewei.cn

📱 微信:chewei.cn (车位网)

👤 QQ:149305903|454022543

Source: <http://sz.chewei.cn/>

<sup>8</sup> [http://fgw.sz.gov.cn/xxgk/zdly/fwjg/201712/t20171229\\_10633514.htm](http://fgw.sz.gov.cn/xxgk/zdly/fwjg/201712/t20171229_10633514.htm), second attachment

<sup>9</sup> [http://www.sz.gov.cn/cn/xxgk/zfxxgj/tzgg/201412/t20141202\\_2720846.htm](http://www.sz.gov.cn/cn/xxgk/zfxxgj/tzgg/201412/t20141202_2720846.htm)

# Realord Group – Real Lord of the Lies

## 2.4 Guangming Office Buildings Valued at Yield of 0.74%

During the first half of 2019, investigators of Emerson Analytics went on a site visit to the two properties acquired by Realord Group from its controlling shareholder. Exhibit 13 below shows the dilapidated front entrance of the Guangming Property said to worth Rmb2,920m.

**Exhibit 13 – Shabby entrance of Guangming Property**



Source: Emerson Analytics

Next door to the Guangming Property are Ocean's King Technology Building (海洋王科技樓) developed by Ocean's King Lighting Science & Technology Co., Ltd. (Ocean's King Lighting, 002724.SZ, 海洋王照明科技股份有限公司) and EVOC Intelligent Valley (研祥智谷) developed by EVOC Intelligent Technology Company Limited (2308.HK, 研祥智能科技股份有限公司). All three projects next to each other have been built on land for industrial use. Exhibit 14 below shows the basic information of the three projects.

**Exhibit 14 – Overview of Guangming Property and nearby projects**

Project name	Lot no.	Land use	Site area (sm)	Total GFA (sm)
EVOC Intelligent Valley	A508-0030	Industrial use	80,074	245,305
Guangming Property	A508-0031	Industrial use	8,000	53,973
Ocean's King Technology Building	A508-0032	Industrial use	13,308	40,840

Source: Emerson Analytics

# Realord Group – Real Lord of the Lies

The red boxes in the photograph in Exhibit 15 below shows the leasing billboards of Ocean's King Technology Building and EVOC Intelligent Valley. EVOC Intelligent Valley is mainly leasing small furnished offices while Ocean's King Technology Building is offering an entire stand-alone rough cast building of 9,000sm for leasing.

**Exhibit 15 – Guangming Property and nearby office buildings**



Source: Emerson Analytics

The sales staff of Ocean's King Technology told Emerson Analytics that the building was priced at Rmb40/sm/month but negotiable. Exhibit 16 below is the translated transcript of the conversation.

**Exhibit 16 – Ocean's King Technology Building priced at Rmb40/sm/month**

Emerson investigator:	Have you got some office space for lease?
Leasing staff:	Yes.
Emerson investigator:	What is the size, generally speaking?
Leasing staff:	We are leasing out the whole building.
Emerson investigator:	Leasing out the whole building?
Leasing staff:	Yes. We don't lease by floor or by units. We lease the whole building out, it's quite big, more than 9,000 square meters.
Emerson investigator:	What's the approximate price for leasing the whole building?
Leasing staff:	Rmb40 per square meter a month.
Emerson investigator:	Rmb40 per square meter a month?
Leasing staff:	Correct.

Source: Emerson Analytics

## Realord Group – Real Lord of the Lies

A staff member at Realord Group told us that the company was also planning to lease out the entire building, and the lessee is free to use it or sub-lease it to others. We believe the Guangming Property will be priced at less than Ocean's King Technology Building.

- Rmb40/sm/month is merely the asking price of Ocean's King Technology Building, and the actual transacted price is going to be lower;
- Total GFA of the Guangming Property is almost six times that of the space for lease at Ocean's King Technology Building, which will further depress the lease rate.

It is reasonable to assume that the Guangming Property needs to offer a 20% discount to the Ocean's King asking price. Based on a rent of Rmb32/sm/month, the property has been valued at a yield of 0.74% ( $= 32 \times 12 / 51,700$ ).

The Guangming Property site has a lease term of 50 years, from March 17, 2009 to March 16, 2059. The remaining life of the site is less than 40 years. The valuation of the property can be recouped in 135 years ( $= 51,700 / (32 \times 12)$ ) at the unchanged rental rate, more than three-times the remaining life of the site. How can this be possible?

### 2.5 Guanlan Carpark Worth More than Apartment at Yield of 0.07%

The Residential Buildings are public leased housing, which are discussed in great details in section 3.2. There are a total of 2,016 units at the Residential Buildings with a total GFA of 127,040sm, for an average 63sm per unit. According to public disclosures by the Futian District government in Shenzhen, the Residential Buildings are priced at an average of Rmb5,494/sm<sup>10</sup>, implying an average value of Rmb346k ( $= 5,494 \times 63 / 1,000$ ) per unit.

According to the valuer, a carpark is worth Rmb400k, more expensive than a residential unit upstairs. Can anything be more absurd than this? The people who live at the Residential Buildings are lessees. Why would they be willing to spend Rmb400k to buy a carpark?

Exhibit 17 below shows a billboard that publicizes car parking fees at Realord Villas, where one can rent a carpark at Rmb230 a month. This means the acquisition was priced at yield of 0.69%.

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<sup>10</sup> [http://www.szft.gov.cn/ftxx/xwdt/ftdt/201308/t20130826\\_9501288.htm](http://www.szft.gov.cn/ftxx/xwdt/ftdt/201308/t20130826_9501288.htm)

# Realord Group – Real Lord of the Lies

Exhibit 17 – Realord Villas carparks are leased at Rmb230/month



Source: Emerson Analytics

There are a total of 1,012 carparks at the Guanlan Property. Some property management personnel told our investigators that normally there are about 900 vacant carparks. That means only about 100 carparks are regularly used, for an actual occupancy of roughly 10%.

Taking this low occupancy into account, the real yield for all carparks as a whole is a non-existent 0.07%. This is complete madness.

# Realord Group – Real Lord of the Lies

## Part 3 Guanlan and Guangming Properties: Not Generating Cashflow

We have shown in Part 2 that the Guanlan and Guangming Properties have been sold to the listco by the controlling shareholders at a huge 15.4x premium over the actual investment amount. We have also calculated that the acquisition valued the Guangming Property office buildings at a yield of 0.74%, and that it valued a Guanlan Property carpark at more than an apartment there.

Even though the two properties are located in the Tier 1 Chinese city of Shenzhen, they can hardly generate any meaningful cash flow. For a real estate investor, the most important consideration is naturally the location of the property. From this point of view, the Guanlan and Guangming Properties are situated at less-than-desirable locations.

Exhibit 18 below is a map of Shenzhen with the Guanlan and Guangming Properties marked. The main commercial districts in Shenzhen are the Luohu, Futian and Nanshan districts. Using the Luohu border crossing point (to Hong Kong) as reference, the Guanlan Property is 31 kilometers (km) away while the Guangming Property is 43km away.

**Exhibit 18 – Locations of Guanlan and Guangming Properties**



Source: Emerson Analytics

# Realord Group – Real Lord of the Lies

## 3.1 Leasing Constantly Delayed

The Guanlan and Guangming Properties were completed in June 2017 and the end of 2017, respectively. Let's review the lease progress so far:

- According to the acquisition announcement dated March 22, 2018, leasing of the two properties is expected to commence in the second quarter of 2018;
- According to the 2018 interim report, the two properties are expected to generate rental income in the second half of 2018;
- According to the 2018 annual report, the renovation of the two properties is scheduled to complete in late 2019 and mid-2020, respectively; and
- The 2018 annual report also says that the two properties are likely to commence business in early 2020 and late 2020, respectively, after the renovation.

The renovation first appeared in the 2018 annual report. We believe the so-called renovation is simply an excuse to cover up the difficulties in leasing the two properties out and there is no renovation at all. During our on-site investigations in 1H19, we found no trace whatsoever of any renovation work at the two properties.

If the properties are easy to lease out and if the renovation is a requisite for leasing, then why isn't there any renovation work? Why would a property be left vacant for more than two years if it were easy to be leased out?

## 3.2 No Demand for Commercial Space at Low Occupancy Public Leased Housing

The Guanlan Property is located at Realord Villas, where the Residential Buildings are used for public leased housing and have very low occupancy.

According to the [深圳市保障性住房條例](#) (Shenzhen Public Assured Housing Regulations), public assured housing can take the form of low-rental housing, public leased housing and affordable housing. In May 2016, low-rental housing and public leased housing are combined into one<sup>11</sup>. The Residential Buildings are the public leased housing provided by the Futian District government<sup>12</sup>, even though they are located at Longhua District.

According to the [福田區企業人才住房配售管理辦法](#) (Administrative Rules for the Placement of Futian District Enterprise Staff Housing), the government has sold the Residential Buildings to qualified

<sup>11</sup> [http://zjj.sz.gov.cn/csml/zcfg/xxgk/zcfg\\_1/zcfg/bzzf/201606/t20160624\\_3723086.htm](http://zjj.sz.gov.cn/csml/zcfg/xxgk/zcfg_1/zcfg/bzzf/201606/t20160624_3723086.htm)

<sup>12</sup> [http://www.sz.gov.cn/szst2010/zdlyzl/zf/jsxx/201604/t20160414\\_3577320.htm](http://www.sz.gov.cn/szst2010/zdlyzl/zf/jsxx/201604/t20160414_3577320.htm)

## Realord Group – Real Lord of the Lies

enterprises, which in turn lease to their staff at fixed rentals. The enterprises have limited ownership over such housing in the sense that they cannot transfer ownership to any entity other than the government.

But actual occupancy rate at Realord Villas is less than 20%. This is confirmed by our on-site investigations in the first half of 2019. Exhibit 19 below, taken at about 8:30pm, shows that Building 3 was probably occupied as to 20% or so. The other buildings had even lower occupancy rates.

**Exhibit 19 – Realord Villas residential building 3 (left) and 4/5/6 (right) at about 8:30pm**



Source: Emerson Analytics

The low occupancy at the Residential Buildings makes it difficult to lease out the retail and commercial space. In any case, the poor location of the Guanlan Property cannot attract non-residents. Realord Group is putting retail and commercial space on the market (Exhibit 20). Our on-site investigations in 1H19 showed that there was only one retail shop in business (Exhibit 21).

# Realord Group – Real Lord of the Lies

**Exhibit 20 – Retail and commercial space of Guanlan Property put on market**



Source: Emerson Analytics

**Exhibit 21 – The only shop in business two years after completion**



Source: Emerson Analytics

# Realord Group – Real Lord of the Lies

## 3.3 The Office Space with No Cashflow

Broadly speaking, there are two ways to lease the office buildings: (i) wholesale lease of the entire building to a third party who may use it and/or sublease it; and (ii) lease out various units in the office buildings on a piecemeal basis to end users.

The office buildings at the Guanlan and Guangming Properties are ready to be leased out in their entirety, and the lessees will refurbish the buildings as they see fit. Realord Group prefers this approach because of its very little risk. Unfortunately, there has been no taker for more than two years, and no one knows when a lessee will show up.

Will Realord Group take the second approach? This involves additional investment in refurbishing the office buildings before putting them on the market for lease. The rental income of these two properties will not be sufficient to recoup the refurbishing costs and operating costs for years. Therefore, it may be sensible for Lin to be sitting on his hands for the past two years, but it also suggests that it is difficult for the office buildings to generate positive cash flow.

The office buildings at the Guanlan and Guangming Properties were completed in mid- and late-2017, but have remained empty for the last two years. The reason is simple: the location is not right, so there are few takers. The neighboring buildings, completed around the same time, are also struggling to fill up their excess office space, as the landlords are unable to fully utilize their own buildings.

Compared with the large amount of cash that Lin has harvested (please see section 3.4 below), possible rental income in the next couple of years is just peanuts. He is therefore not so desperate to lease the office space out. During our site visit in 1H19, there was absolutely no visible sign for the leasing of office space at the Guanlan and Guangming Properties while the neighboring office buildings seemed to be working hard to lease their offices. Leasing staff at nearby office buildings had no idea there was an office block inside Realord Villas. They asked our investigators, "Is there office for leasing inside Realord Villas?"

## 3.4 Lin has pocketed \$5,776m of Cash

The controlling shareholders Lin and his wife sold the company that controlled the Guanlan and Guangming Properties to the listco at a price of \$7,910m. They generously offered the listco a discount of \$587m or 7.4%, and settled for \$7,323m as total consideration for stuffing the minority shareholders with their rubbish properties.

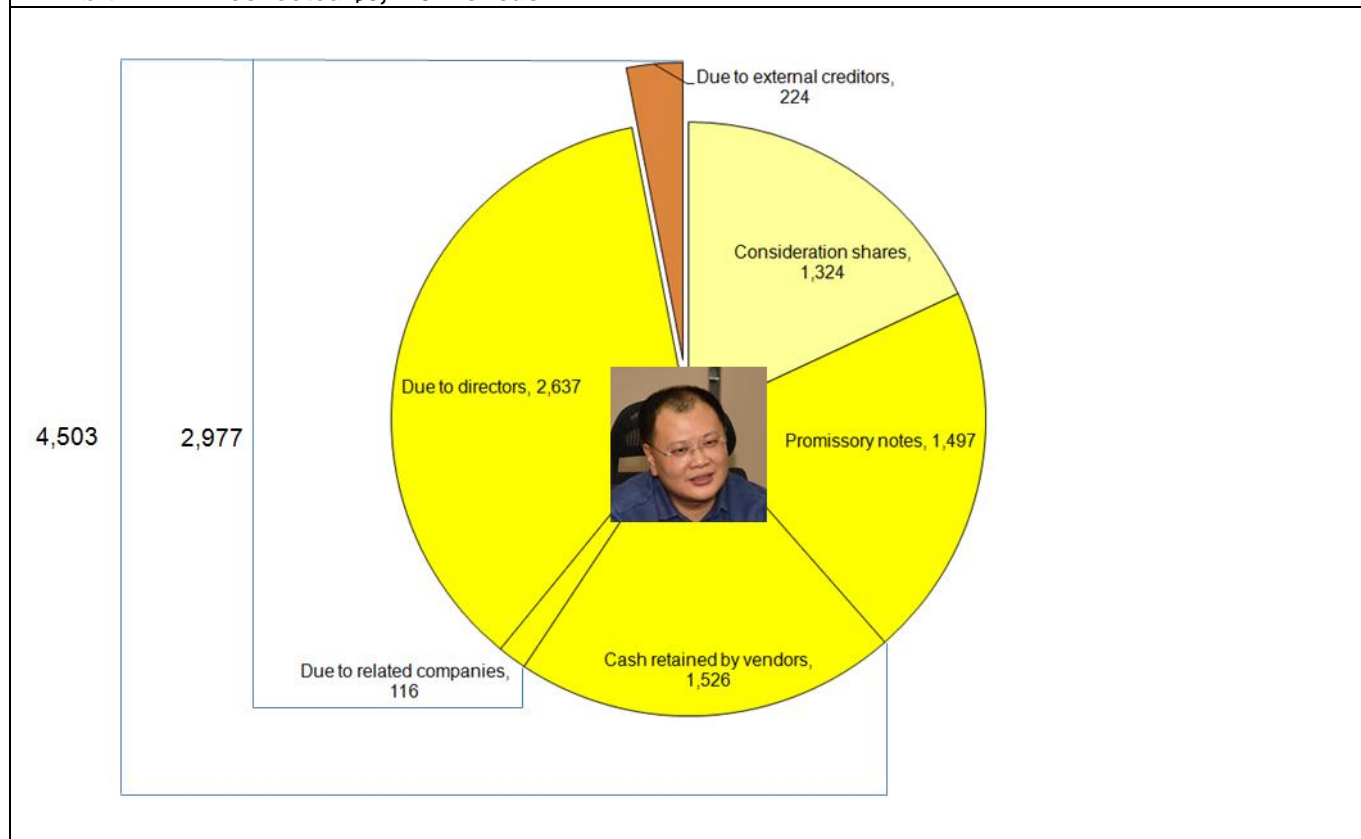
Payment consisted of three parts: cash of \$4,503m, shares at market price on completion date of \$1,324m and promissory notes of \$1,497m. As shown in the following pie chart, Lin is required to use the cash to settle all the \$2,977m debts – \$2,637m due to directors (i.e. themselves), \$116m due to related companies (again, themselves), and \$224m due to third parties.

Ignoring the share consideration worth \$1,324m, we can see that upon completion, Lin received as much as \$4,279m ( = 4,503 – 224 ). About one year later, the full amount of the promissory notes was repaid

## Realord Group – Real Lord of the Lies

through unsecured banking facilities obtained by Realord Group. Together, the husband and wife team ripped \$5,776m (= 4,279 + 1,497 ) of cash off minority shareholders.

**Exhibit 22 – Lin collected \$5,776m of cash**



Source: Emerson Analytics

But of course the listco had no money to buy the properties (at the end of 2017, it had only \$61m of cash and \$634m of debts). So, the banks came to Lin's rescue, first lending some \$5,361m to Realord Group in 2018 (\$4,864m of long-term loans and \$497m of short-term loans at the end of the year) and in March 2019 a further Rmb2,400m to replace the \$1,492m promissory notes and certain loans from the ultimate holding company.

According to the 2018 annual report, the company established relationship with Guangzhou Rural Commercial Bank Co., Ltd. (GRCB, 1551.HK) during that year. In April 2018, around the time of the acquisition completion, Realord Group pledged its shares in the companies that directly held the Guanlan and Guangming Properties to GRCB. About one year later, Lin bought 221m GRCB shares at \$5.12 each, which gives him a 12.2% stake in the "H" shares or 2.3% in the entire equity capital of the bank. We suspect most of Realord Group's debts are provided by GRCB.

**Why would any bank lend billions of dollars to Realord Group against such lousy assets? The truth may be very complicated and intriguing.**

# Realord Group – Real Lord of the Lies

## Part 4 Revenue of Core Operations Way Below Claims

We will now look at Realord Group from the revenue point of view. The environmental protection (EP) and motor vehicle parts (MVP) segments are said to be the main contributors of Realord Group's revenue, chalking up \$571m and \$127m, respectively, in 2018, or 70% and 16%, respectively, of the total.

These two segments actually generated much less revenue than that reported by Realord Group. The real revenue of EP Group was only 40% of that reported in 2018. The aggregated MVP real revenue from mainland China was only 4% of reported during 2015-18.

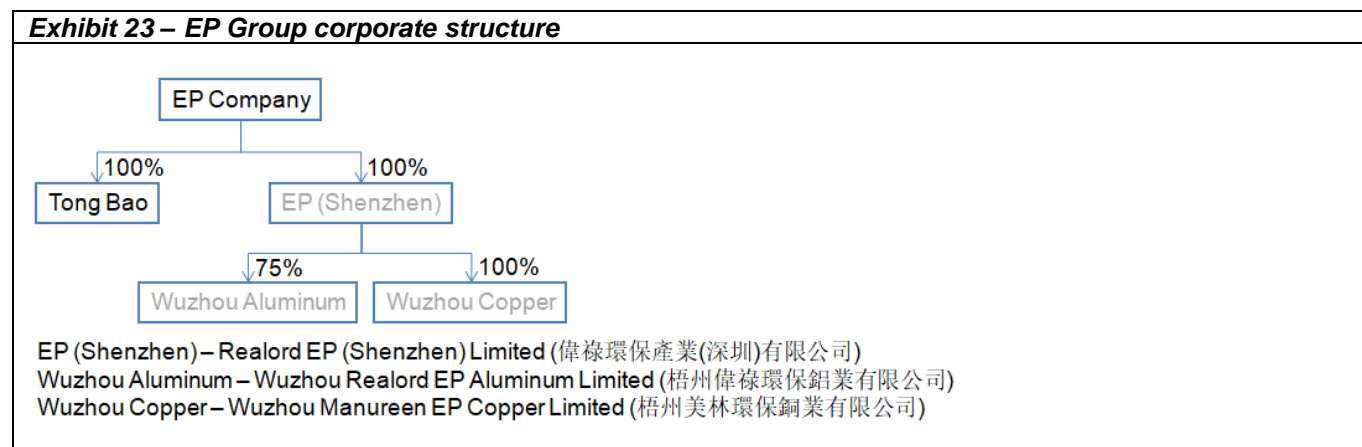
### 4.1 Two Irregularities of the EP Segment

Realord Group entered the EP business in 2017 by acquiring a 60% stake in Realord EP Industrial Company Limited (EP Company) and its subsidiary Guangxi Wuzhou City Tong Bao Renewable Materials Limited (Tong Bao, 廣西梧州市通寶再生物資有限公司, collectively with EP Company referred to as EP Group).

The principal business of EP Group is the dismantling of scrap metals in mainland China. The raw materials processed are imported, and include scrap electrical machineries (HS code: 7404000010) for recycling copper, scrap electrical cables (HS code: 7602000010) for recycling aluminum and scrap electrical equipment (HS code: 7204490020) for recycling iron and steel (hereinafter referred to as Scrap Metals).

In 2018, three subsidiaries (EP (Shenzhen), Wuzhou Aluminum and Wuzhou Copper) were created though they had no real operations: (i) each of them had zero paid-up capital; (ii) none of the three had any revenue in 2018; and (iii) none of them was included in the list of principal subsidiaries in 2018 annual report. The only information we have managed to find about these three entities is that Wuzhou Aluminum bought certain assets from Wuzhou City Hai Gang Metals Limited (Hai Gang, 梧州市海港金屬有限公司) in March 2019<sup>13</sup>. Tong Bao and Hai Gang are both located at Wuzhou Import Renewable Resources Processing Park (Wuzhou Park).

**Exhibit 23 – EP Group corporate structure**



Source: Emerson Analytics

<sup>13</sup> <http://gxwzxhyq.com/index.php?route=common/article&id=203>

# Realord Group – Real Lord of the Lies

**Irregularity 1:** Since the 2017 acquisition, Realord Group has never mentioned any other entities beyond the EP Group engaging in the EP business. Thus, the EP segment revenue should be the same as EP Group's revenue. However, in 2018, revenue of the EP segment exceeded that of the EP Group<sup>14</sup> by \$88m.

<b>Year end Dec 31 (HK\$ m)</b>	<b>2017</b>	<b>2018</b>	<b>Chg (%)</b>
EP segment	572	571	0%
EP Group	572	483	-16%
Gap	0	88	

Source: Realord Group

**Irregularity 2:** Since the EP Group acquisition, the only investment plan announced is a processing plant for the recycling and production of aluminum and copper ingots in Wuzhou Park. In its 2018 annual report, Realord Group says the construction of the plant has been delayed to the second half of 2019. Strangely, net cash used in EP Group's investing activities amounted to as much as \$209m in 2018<sup>15</sup>. Even more strange is that there is no corresponding item in Realord Group's consolidated statement of cash flows.

## 4.2 Scrap Metal Imports Tumbled 82% but EP Group Revenue Down Only 16%

As seen from Exhibit 2 above, the revenue of the EP segment is almost entirely within mainland China. EP Group's revenue is therefore derived from mainland China. EP Company mainly acts as an agent by sourcing scrap materials from overseas and reselling to Tong Bao. Tong Bao's revenue should be identical to that of EP Group, because EP Company's revenue will be eliminated upon consolidation.

The Chinese government has worked hard on environmental protection in recent years, and has tightened the imports of solid wastes. In 2018, authorized imports of Scrap Metals amounted to a total of 1,671k tons, down a massive 74% from the 6,363k tons in 2017. Imports of Scrap Metals have been banned from December 31, 2018<sup>16</sup>.

We have obtained the amount of authorized scrap metal imports of Tong Bao and Hai Gang from China Solid Waste and Chemicals Management Center, a unit of the Ministry of Ecology and Environment of China. Usually, the amount of actual imports is about 80% of authorized imports. From Exhibit 25 below, we can see that both companies suffered significant decrease in their respective authorized imports last year. How could EP Group's revenue merely contract 16% when the scrap metal imports tumbled by 82%?

<sup>14</sup> <https://www1.hkexnews.hk/listedco/listconews/sehk/2019/0426/1tn201904262653.pdf>, p.202

<sup>15</sup> <https://www1.hkexnews.hk/listedco/listconews/sehk/2019/0426/1tn201904262653.pdf>, p.203

<sup>16</sup> [http://www.mee.gov.cn/xxgk/xxgk01/201804/t20180419\\_629582.html](http://www.mee.gov.cn/xxgk/xxgk01/201804/t20180419_629582.html)

# Realord Group – Real Lord of the Lies

**Exhibit 25 – Authorized imports (tons) of Tong Bao and Hai Gang**

	2017	2018	Chg (%)
Mainland China	6,362,757	1,670,585	-74%
Tong Bao	40,000	7,108	-82%
Hai Gang	23,500	8,449	-64%

Source: China Solid Waste and Chemicals Management Center

During the first half of 2019, Emerson Analytics conducted a week-long on-site investigation at Wuzhou Park. Nearly all the scrap metals processing plants there had suspended their operations at that time – the whole park was deathly quiet all the time, and Tong Bao was no different. Exhibit 26 below shows the main entrance of Tong Bao. During that week, we talked to many companies at Wuzhou Park, and they all confirmed to us that all the factories there, including Tong Bao and Hai Gang, have failed to operate normally since mid-2018 due to changes in government policies.

**Exhibit 26 – Main entrance of Tong Bao**



Source: Emerson Analytics

## 4.3 EP Group 2018 Real Revenue Only 40% of Claim, Net Income Merely 17%

Exhibit 27 below compares Tong Bao's revenue as reported to ECIS with that claimed by EP Group. For 2018, Tong Bao reported revenue of Rmb164m or \$194m to ECIS, which was about 40% of that claimed by EP Group. For 2017, the ECIS revenue of Tong Bao was for the whole year, whereas EP Group reported revenue from February 28, 2017 (the date of acquisition) to December 31, 2017. On a pro forma basis, Tong Bao's actual revenue would amount to 49% of EP Group's reported revenue.

## Realord Group – Real Lord of the Lies

**Exhibit 27 – Revenue of EP Group comparison – actual vs. reported**

Year end Dec 31 (HK\$ m)	2017	2018	Chg (%)
Tong Bao (Rmb m)	293	164	-44%
Pro forma Tong Bao (Rmb m)	244	164	
/ Exchange rate (Rmb/HK\$)	0.8669	0.8436	
= Tong Bao – actual	282	194	
EP Group – reported	572	483	-16%
<b>Percentage</b>	<b>49%</b>	<b>40%</b>	

Sources: Realord Group, ECIS and Emerson Analytics

At the net profit level, the exaggeration was even more serious. For 2017 and 2018, Tong Bao reported profit of \$0 and \$8m, respectively. EP Company reported net profit that was about 11% and 13% of Tong Bao in 2014 and 2015<sup>17</sup>. Adding net income of EP Company would yield an aggregate net profit of \$0 and \$9m for EP Group in 2017 and 2018, respectively. This implies only 0% and 17% of disclosed amounts.

**Exhibit 28 – Net income of EP Group comparison – actual vs. reported**

Year end Dec 31 (HK\$ m)	2017	2018
Tong Bao (Rmb m)	0	7
/ Exchange rate (Rmb/HK\$)	0.8669	0.8436
= Tong Bao	0	8
+ EP Company (12% of Tong Bao)	0	1
= EP Group – actual	0	9
EP Group – reported	45	51
<b>Percentage</b>	<b>0%</b>	<b>17%</b>

Sources: Realord Group, ECIS and Emerson Analytics

<sup>17</sup> <https://www1.hkexnews.hk/listedco/listconews/sehk/2016/0905/ltm201609051623.pdf>, p.11&12

# Realord Group – Real Lord of the Lies

## 4.4 MVP Real Revenue from Mainland China Only 4% of Reported

Realord Group did not report regional revenues from the MVP segment for 2015-17. However, such regional revenues can be calculated, as shown in Exhibit 29. Realord Group reported revenue of \$127m for the MVP segment in 2018. Of this amount, revenue from mainland China was said to be \$85m and that from Hong Kong \$42m. The Hong Kong MVP business ceased operation in November 2018 due to high rental expense.

Guangdong Realord Vehicle Parts Limited (Guangdong MVP, 廣東偉祿汽車零件有限公司) is the only Realord Group subsidiary that distributes vehicle parts in mainland China. Its revenue, obtained from ECIS, is also presented in Exhibit 29.

<b>Year end Dec 31 (HK\$ m)</b>	<b>2015</b>	<b>2016</b>	<b>2017</b>	<b>2018</b>	<b>Total</b>
Hong Kong	115	132	117	136	<b>500</b>
- Hong Kong other segments*	85	92	83	94	<b>355</b>
<b>= Hong Kong MVP</b>	<b>30</b>	<b>40</b>	<b>34</b>	<b>42</b>	<b>146</b>
MVP	95	101	87	127	<b>410</b>
- Hong Kong MVP	30	40	34	42	<b>146</b>
<b>= Mainland China MVP</b>	<b>66</b>	<b>60</b>	<b>53</b>	<b>85</b>	<b>264</b>
Guangdong MVP (Rmb m)	0	2	9	0	<b>10</b>
/ Exchange rate (Rmb/HK\$)	0.8033	0.8555	0.8669	0.8436	
<b>= Guangdong MVP</b>	<b>0</b>	<b>2</b>	<b>10</b>	<b>0</b>	<b>12</b>
Percentage	0%	3%	18%	0%	<b>4%</b>

Sources: Realord Group, ECIS and Emerson Analytics

\* Realord Group did not disclose its very low property investment revenue from Hong Kong for 2015-17. For 2018, Realord Group reported \$0.7m of property investment revenue from Hong Kong.

For 2015 and 2018, Guangdong MVP reported zero revenue to ECIS, but it should have revenue of \$66m and \$85m, respectively. For 2017, revenue reported to ECIS only amounted to 18% of that implied by Realord Group's disclosures. In aggregate, the 2015-18 revenue according to ECIS was only 4% of Realord Group's claim.

# Realord Group – Real Lord of the Lies

Realord Group had professed its intention to boost the vehicle parts business through its B2B platform [www.1196.com](http://www.1196.com). In May 2015, it took full control of Realord Vehicle Parts Limited and its shareholder's loan for \$12.7m to expand the e-commerce business. Just one and a half years later, the website ceased updating. Exhibit 30 below shows the last updated page of the website, in which MVP is one of the more inconspicuous channels. Currently, visitors to this website will be automatically directed to Realord Group's website <http://www.realord.com.hk/>. Is there any reason to believe Realord Group's various brags?

Exhibit 30 – The last update of [www.1196.com](http://www.1196.com) October 2016

The screenshot shows the Realord website homepage. At the top, there is a navigation bar with the Realord logo and the tagline '伟禄全球购'. Below the logo is a search bar with the placeholder text '请输入关键词' and a '搜索' button. To the right of the search bar is a '我的购物车' button. The main content area features a large promotional banner for '万圣大跳' (Halloween Party) with the text '发哆糖不捣蛋' and '满99就发糖 预热爆款满200减100'. The banner includes images of Halloween pumpkins, candy, and a witch. To the left of the banner is a sidebar menu with categories like '母婴用品', '食品保健', '美妆洗护', '家居日用', '服装配饰', and '汽车配件' (Motor Vehicle Parts). To the right of the banner is a '加盟入驻' (Join Us) section with a list of '最新动态' (Latest News) and images of Land Rover and Mercedes-Benz logos. At the bottom of the page, there is a horizontal navigation bar with icons for '选购商品', '提交订单', '在线支付', '物流配送', and '服务评价'.

Source: <https://web.archive.org/web/20161002041611/http://www.1196.com/>

# Realord Group – Real Lord of the Lies

## Part 5 Financials and Valuation

Having presented our detailed analysis of and investigations into the various businesses of Realord Group, we can now discuss the true revenue, asset value and valuation of the company. For 2018, its actual revenue was only about 43% of the amount claimed. This year, we expect a serious withering with a massive 87% decline from the 2018 reported level.

In February 2019, a Hong Kong listed company took out a long term lease on some commercial properties very similar to Guanlan Property's commercial space. To comply with the HKFRS16 requirement for "deemed acquisition of asset", it valued the properties with the present value method. Using this valuation as a benchmark, we believe the true net asset value of the company is probably negative \$3,196m.

In other words, there's really nothing left in Realord Group except for the huge debts incurred from buying out the controlling shareholder, who has taken the money and can run any time. The only fate awaiting the company is BANKRUPTCY.

### 5.1 Dwindling Revenue and Unbearable Burden of Interest

In the first half of 2019, we visited several other Realord Group properties in mainland China. Among them, Unit 3306-3310 at Excellence Time Square (carried on the books at \$92m) in central Futian District was vacant. The piece of paper framed in red on the door is a log of daily inspection of vacant office by the security staff of the building's management company. They told us that the last tenant left at the end of 2018.

**Exhibit 31 – Unit 3306-3310, Excellence Time Square is vacant**



Source: Emerson Analytics

## Realord Group – Real Lord of the Lies

This property has a total GFA of 1,019sm<sup>18</sup>. According to the sales staff of the property management company, rentals of this property are about Rmb280/sm/month. This yields annual revenue of about \$4m, or 21% of the 2018 property investment revenue.

Assuming the vacancy continues till the end of the year, and that revenue from other investment properties remains unchanged, then the property investment revenue is about \$15m in 2019.

In Exhibit 32 below, we compare the reported and actual revenue of Realord Group in 2018 and our estimate for 2019. We calculate that the company achieved \$349m of revenue last year, just 43% of its claim. For 2019, we believe the company is likely to achieve some \$109m in revenue, down a massive 87% from its reported 2018 level.

<b>Year end Dec 31 (HK\$ m)</b>	<b>2018 reported</b>	<b>2018 actual</b>	<b>2019 estimate</b>	<b>Remarks</b>
Commercial printing	82	82	82	Assume 2018 number accurate, 2019 unchanged
Hangtag	1	1	1	Assume 2018 number accurate, 2019 unchanged
MVP	127	42	0	See section 4.4
Financial services	10	10	10	Assume 2018 number accurate, 2019 unchanged
Property investment	20	20	15	See section 5.1
EP	571	194	0	See section 4.3 for 2018 and section 4.2 for 2019
<b>Total</b>	<b>811</b>	<b>349</b>	<b>109</b>	

Source: Emerson Analytics

At the end of 2018, Realord Group had interest-bearing debts of \$7,675m. Based on the latest interest rate of 5.7%<sup>19</sup> for the company, its interest expense would amount to \$437m this year. Given the expected \$109m revenue this year, how can Realord Group possibly meet its interest obligations? The company's cash of \$897m can only afford bank interest this year and next.

About three months after our on-site investigations in 1H19, we revisited the Guanlan and Guangming Properties and other relevant properties mentioned in this report. We discerned no material change to their previous conditions, with the Excellence Time Square property remaining vacant and the Guanlan shopping arcade still having only one retail shop in operation, for example.

The sales staff of Excellence Time Square also told us that the office space there was selling at about Rmb75,000/sm. As shown earlier, office space near the Guangming Property was asking for Rmb40/sm/month in rentals, equivalent to 1/7 of the Rmb280/sm/month at Excellence Time Square. By

<sup>18</sup> <https://www1.hkexnews.hk/listedco/listconews/sehk/2006/1211/1tn20061211105.pdf>, p.4

<sup>19</sup> <https://www1.hkexnews.hk/listedco/listconews/sehk/2019/0426/1tn201904262653.pdf>, p.204

# Realord Group – Real Lord of the Lies

simple extrapolation, Guangming Property's office space should worth about Rmb10,714/sm, 21% of the appraised value.

## 5.2 Net Asset Value is Negative \$3,196m

Realord Group bought the Guanlan and Guangming Properties at hugely inflated prices from controlling shareholder Lin. So how much are these assets really worth? Here, we will use a recent transaction to demonstrate the true value of something said to worth Rmb52,000/sm at the time of the acquisition.

February 22, 2019, Jiahua Stores Holdings Limited (Jiahua Stores, 0602.HK) entered into long-term agreements to lease three properties. Pursuant to HKFRS 16, the lessee needs to recognize the premises as right-of-use assets, and the relevant transactions are regarded as deemed acquisition of asset by the lessee. The consideration of the premise is the aggregated present value of the fixed lease payments as discounted by a discount rate of 4.9% equivalent to Jiahua Stores' incremental borrowing rate.

The three properties leased by Jiahua Stores are all located in Shenzhen. One of them, the Guanlan Shopping Mall, is highly comparable to Guanlan Property's commercial space.

- Both properties are located in Guanlan Town of Longhua District. The Guanlan Shopping Mall is 5km away from the Guanlan Property and its location is better than the latter;
- The Guanlan Shopping Mall consists of two parts completed in 2017 and 2018, respectively. The Guanlan Property was completed in June 2017; and
- The Guanlan Shopping Mall has a total GFA of 25,168sm, compared with Guanlan Property's commercial space of 16,716sm.

We therefore regard the valuation of the Guanlan Shopping Mall will provide a useful reference to that of Guanlan Property's commercial space. The Guanlan Shopping Mall's initial monthly rent is Rmb45/sm/month, which will go up 5% every three years. We apply the same rental structure to Guanlan Property's commercial space, which we believe is advantageous to Realord Group, though there are two adjustments necessary:

- The Guanlan Shopping Mall lease is for eight years, whereas the Guanlan Property still has 63 years of land-use rights;
- Realord Group's latest long-term debt carries an interest rate of 5.7%, which we will take as the discount rate for the valuation.

Accordingly, Guanlan Property's commercial space is worth Rmb11,982/sm. Using 3.0% instead of 5.7% as the discount rate, Guanlan Property's commercial space is worth merely Rmb22,159/sm or 43% of the acquisition valuation. In reality, the Rmb52,000/sm acquisition valuation implies a discount rate of only 0.29%.

## Realord Group – Real Lord of the Lies

We can estimate the true value of carpark in the Guanlan and Guangming Properties with initial monthly rent of Rmb230/lot/month. The different valuations we estimate for carpark in the Guanlan and Guangming Properties are a result of their different remaining lives of land use rights.

	True valuation	Acquisition valuation	True valuation as % of acquisition valuation
Guangming Property's office space (Rmb/sm)	10,714	51,700	21%
Guanlan Property's commercial space (Rmb/sm)	11,982	52,000	23%
Guanlan Property carpark (Rmb/lot)	61,240	400,000	15%
Guangming Property carpark (Rmb/lot)	52,956	400,000	13%

Source: Emerson Analytics

Applying the highest 23% ratio in the above table on assets other than carpark, we can estimate the overall true value of the two properties. The calculations are shown below in Exhibit 34. All in all, this gives rise to an aggregate value of Rmb1,430m or \$1,632m for the two properties, equivalent to 3.8x of the actual invested amount. Considering that the properties are having difficulties securing tenants, this is a generous valuation.

	Guanlan Property	Guangming Property	Total / Average
<b>sm/lot</b>			
Retail use	9,671	-	<b>9,671</b>
Commercial use	16,716	-	<b>16,716</b>
Office use	24,652	53,973	<b>78,625</b>
Carpark	1,012	315	<b>1,327</b>
<b>Rmb/sm (Rmb/lot)</b>			
Retail use	21,429	-	<b>21,429</b>
Commercial use	11,982	-	<b>11,982</b>
Office use	12,212	11,913	<b>12,006</b>
Carpark	61,240	52,956	<b>59,273</b>
<b>Valuation (Rmb m)</b>	<b>771</b>	<b>660</b>	<b>1,430</b>
Retail use	207	-	<b>207</b>
Commercial use	200	-	<b>200</b>
Office use	301	643	<b>944</b>
Carpark	62	17	<b>79</b>

Source: Emerson Analytics

## Realord Group – Real Lord of the Lies

Realord Group reported net asset value of \$2,932m as at the end of 2018. If we re-state the Guanlan and Guangming Properties at our \$1,632m aggregate valuation rather than the \$7,761m carried on the balance sheet, the net asset value of the company becomes negative \$3,196m.

### **Exhibit 35 – True net asset value is negative \$3,196m**

<b>Year end Dec 31 (HK\$ m)</b>	<b>2018</b>
Net assets – reported	2,932
- Guanlan and Guangming Properties book value	-7,761
+ Guanlan and Guangming Properties true valuation	1,632
= Net assets – actual	-3,196

Source: Emerson Analytics

### **5.3 Valuation: Bankruptcy**

There is no doubt Realord Group's financial statements are seriously fraudulent, to the extent that there is simply no need for a valuation analysis. As none of the company's various divisions is able to generate any meaningful revenue, Realord Group cannot possibly sustain its interest payments. Having ripped the minority shareholders off, is Lin able to rescue Realord Group? We rather suspect the only fate awaiting the company is bankruptcy.

# Realord Group – Real Lord of the Lies

## Appendix II List of Companies Challenged by Emerson Analytics

Company (ticker)	First report		Current situation	IPO Auditors	IPO sponsor
	Date	Share price			
China Lumena New Materials Corp. (0067.HK)	Apr 1, 2014	\$1.25	In the third delisting stage, pending a restructuring via a new listing application following liquidation of original operations	Grant Thornton, replaced by BDO in 2010	Credit Suisse Somerley Limited
Shenguan Holdings (Group) Limited (0829.HK)	Sep 2, 2014	\$2.80	Current share price \$0.30, down 89% and below our \$1.1 target price	EY	Macquarie China Merchants Securities
Sound Global Ltd. (0967.HK)	Feb 4, 2015	\$8.00	Last price \$2.98 before SFC halted trading Apr 13, 2016 under section 8(1) of the Securities and Futures (Stock Market Listing) Rules	Deloitte	Morgan Stanley
China Fiber Optic Network System Group Limited (3777.HK)	Aug 7, 2015	\$1.57	Hong Kong court ordered liquidation Jun 1, 2017, listing canceled Feb 14, 2019	EY	BOCI
Hua Han Health Industry Holdings Limited (0587.HK)	Aug 10, 2016	\$0.68	Last traded \$0.53 before the company requested a trading halt Sep 27, 2016. SFC further halted trading under section 8(1) of the Securities and Futures (Stock Market Listing) Rules from Nov 20, 2018	EY	Deloitte & Touche Corporate Finance Ltd
China Hongqiao Group Limited (1378.HK)	Feb 28, 2017	\$7.80	EY and Baker Tilly resigned consecutively after our report. Current share price \$5.31, down 32% but above our \$3.1 target price	Deloitte, replaced by EY in 2015	JP Morgan
Tian Ge Interactive Holdings Limited (1980.HK)	Aug 16, 2017	\$6.17	Current share price \$1.61, down 74%, compared with our delisting target	PWC	UBS CICC
Zhou Hei Ya International Holdings Company Limited (1458.HK)	Mar 1, 2019	\$3.60	Current share price \$3.52, down 2%, compared with our \$2.40 target	EY	Morgan Stanley Credit Suisse
Southern Energy Holdings Group Limited (1573.HK)	Jul 29, 2019	\$9.95	Current share price \$0.44, down 96%, compared with our delisting target	Deloitte	Haitong