

Southern Energy – Revenue Inflated by Five Times

July 29, 2019

| The Basics | |
|---------------|-----------|
| Ticker: | 1573.HK |
| Recent Price: | HK\$9.95 |
| Market Cap: | HK\$7.1bn |

| Emerson Analytics Forecast |
|----------------------------|
| <i>Delisting</i> |

Southern Energy, a producer of anthracite coal in Guizhou Province, was listed in Hong Kong in mid-2016 via an IPO raising Rmb183m net. Our investigations show that the company, with Deloitte Touche Tohmatsu as auditors, has been doctoring its books since the IPO application stage.

- Southern Energy's operations are all carried out by a wholly owned subsidiary, Guizhou Union, whose financial results should be almost the same as those reported by the listed company. However, ECIS filings show that Guizhou Union's revenue in 2016 was only 12% of that reported by Southern Energy while in 2017 it was 21%.
- Our site visits showed that actual output for 2018 at its three mines was probably only one-third of the volume reported by Southern Energy. Luozhou Mine, the worst performer, has been shut down since last August and its actual 2018 output was only 5% of that reported. It was in construction phase in 2016 when there was no production at all, but Southern Energy dared claim it had the largest output of all three mines that year. Each piece of volume information is corroborated by at least two independent sources.
- Southern Energy claims in its IPO prospectus that six major customers accounted for almost three-quarters of its revenue during 2013-15. However, ECIS filings show that four of them consistently had less total revenue than what Southern Energy purported to have sold to them. Of the remaining two, one was recorded as "Operations Ceased" in 2017 and 2018, while the other had

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never bought any anthracite coal. All in all, Southern Energy's actual sales to these customers were only 16% of its claim.

- Southern Energy claims very stable EBIT margins of 50% during 2013-18 even though its closest peer, Feishang Anthracite had to report losses in 2014-15 when coal prices collapsed. Guizhou Union ECIS data reveal a net loss of Rmb21m for 2016-18 rather than the Rmb650m profit claimed by Southern Energy.

All told, Southern Energy has over the 2013-18 period exaggerated its revenue by about five times and that it was not profitable in certain years. By keeping a persistently higher P/E ratio since listing, controlling shareholder Xu Bo has maintained this Ponzi scheme by raising funds through selling and pledging his shares for loan.

Currently, Southern Energy and Xu are both facing financial difficulties as the financial fraud is no longer sustainable. We believe DELISTING is the only proper fate for the stock.

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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.

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Part 1 Losses Masked by Inflated Revenue at Subsidiaries

Southern Energy Holdings Group Limited (Southern Energy, 1573.HK), formerly named China Unienergy Group Limited, is a producer of anthracite coal based in Guizhou Province, the PRC. It was listed in July 2016 in Hong Kong and has always been audited by Deloitte since its IPO application.

Anthracite or hard coal usually refers to the most metamorphosed coal with carbon content of 92-98%. Under China's coal classification standard, anthracite coal has a volatile matter content of 10% or less. Exhibit 1 below sets forth the specific use of different types of anthracite coal.

| <i>Exhibit 1 – Use of anthracite coal</i> | | | |
|---|--|-------------------------------------|--|
| <u>Types of coal</u> | <u>Industrial use</u> | <u>Lumpiness of anthracite coal</u> | <u>Quality requirements</u> |
| Chemical coal | Chemical | Lump coal (+13mm) | Low ash, high fixed carbon content, thermal stability and anti-crushing strength |
| PCI coal | Metallurgy | Fine coal (-13mm) | High grindability, low harmful content, high threshold for ash content and sulfur content |
| Thermal coal | Power Generation Building materials (such as concrete and glass production) | Fine coal (-13mm) | High calorific value and ash fusibility, relatively lower requirement on other indicators such as ash content and sulfur content |

Source: IPO prospectus, p.85

According to Southern Energy's disclosures, the company has been profitable every year since 2013, with accumulated profit of Rmb1,027m during the 2013-18 period. This is in stark contrast to Feishang Anthracite Resources Limited (FS Anthracite, 1738.HK), another Hong Kong-listed company mining anthracite in Guizhou. Due to depressed coal prices, FS Anthracite reported losses during four of the past six years, and was profitable only in 2017 and 2018.

Investigations by Emerson Analytics show that the beautiful picture painted by Southern Energy is a complete lie: its actual revenue is way below the disclosed numbers, the real output at its various coal mines is far less than reported volume, the proportion of the higher-priced chemical lump coal and PCI (pulverized coal injection) fine coal is also fabricated, sales to its so-called major clients are dubious, and the company has been loss-making most of the time rather than profitable.

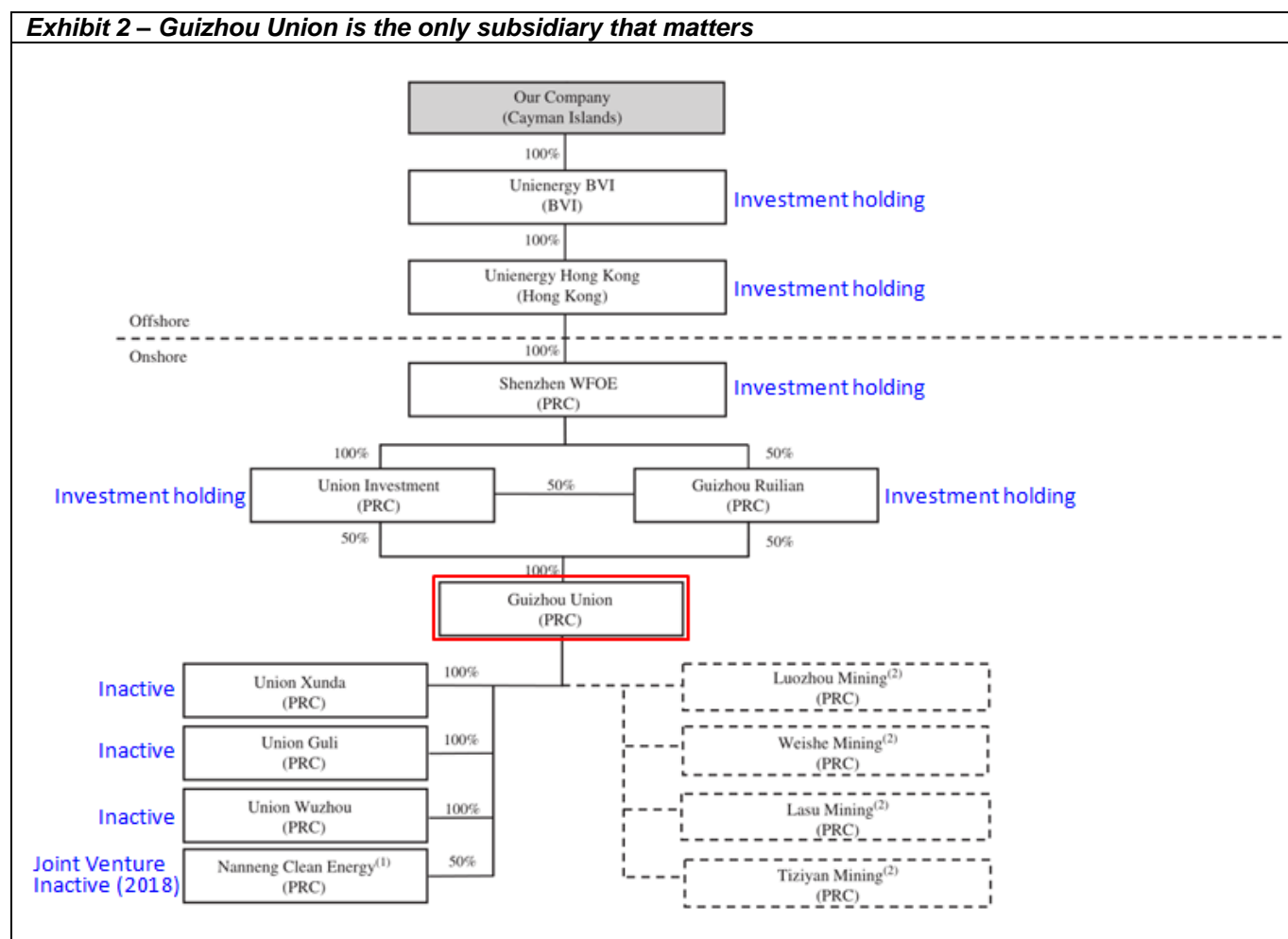
Southern Energy is the second Guizhou-based company whose financial integrity we challenge. In August 2016, we questioned the operations and financial statements of Hua Han Health Industry Holdings

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Limited (0587.HK). The stock has been suspended from trading since September 27, 2016, and on November 20, 2018 the Securities and Futures Commission (SFC) of Hong Kong further imposed a trading halt under section 8(1) of the Securities and Futures (Stock Market Listing) Rules, which deals with false, incomplete or misleading information. We have no doubt that Southern Energy will face the same fate.

1.1 Guizhou Union is the Only Subsidiary That Matters

Exhibit 2 below, taken from its IPO prospectus, shows the corporate structure of Southern Energy (represented by the top grey box) at the time of its listing. There has been no change since then. It can be seen that Guizhou Union (Group) Mining Co., Ltd. (Guizhou Union, 貴州優能(集團)礦業股份有限公司) is the only subsidiary that matters.



Sources: IPO prospectus, p.130, Emerson Analytics

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Luozhou Mining, Weishe Mining, Lasu Mining and Tiziyan Mining are four branches of Guizhou Union that operate Luozhou Mine, Weishe Mine, Lasu Mine and Tiziyan Mine, respectively. With Tiziyan Mine being dormant, output at the other three mines claimed by Southern Energy is shown in Exhibit 3 below.

| | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | Total |
|--------------|------------|------------|------------|--------------|--------------|--------------|--------------|
| Luozhou Mine | 145 | 167 | 224 | 420 | 370 | 373 | 1,699 |
| Weishe Mine | 151 | 159 | 227 | 419 | 396 | 388 | 1,740 |
| Lasu Mine | 24 | 310 | 357 | 419 | 382 | 381 | 1,873 |
| Total | 320 | 636 | 807 | 1,258 | 1,148 | 1,142 | 5,312 |

Sources: IPO prospectus and annual reports

1.2 Revenue Data from ECIS for 2016/17 Merely 12% and 21% of Claimed Numbers

The State Administration of Industry and Commerce (SAIC) publishes key financial data of Chinese business entities through its Enterprise Credibility Information System (ECIS). In our August 2016 report [Hua Han - Bad for Your Financial Health](#), we have demonstrated the accuracy of data reported by Guizhou listed companies through ECIS.

Theoretically, Southern Energy's revenue should be the same as that of Guizhou Union, whose revenue, net income, total assets, total liabilities and total equity figures are available from ECIS.

In Exhibit 4 below, we compare Guizhou Union's revenue and total assets figures obtained from ECIS with those reported by Southern Energy. ECIS has no information on Guizhou Union For the financial years 2013-15. We believe it is highly likely that Southern Energy somehow "arranged" for ECIS to hide Guizhou Union's data for its IPO.

For 2017-18, figures for total assets from these two sources are very similar. For 2016, Guizhou Union's total asset value according to ECIS amounts to about 45% of that reported by Southern Energy. This is probably because the ECIS figure does not include mining rights. If the Rmb897m mining rights reported by Southern Energy is added to Guizhou Union's ECIS number, the two are almost identical.

However, there is a huge gap in the revenue numbers from these two sources. The ECIS revenue for 2016 and 2017 amounts to only 12% and 21%, respectively, of that reported by Southern Energy. In 2018, the two sources reported almost the same revenue.

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Exhibit 4 – ECIS revenue for 2016/17 only 12% and 21% of reported

| Year end Dec 31 (Rmb m) | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 |
|-------------------------|------|-------|-------|-------|-------|-------|
| Revenue - ECIS | — | — | — | 81 | 134 | 642 |
| Revenue - reported | 191 | 379 | 486 | 691 | 642 | 641 |
| ECIS as % of reported | | | | 12% | 21% | 100% |
| Total assets - ECIS | — | — | — | 713 | 1,514 | 1,567 |
| Total assets - reported | 974 | 1,238 | 1,391 | 1,600 | 1,561 | 1,632 |
| ECIS as % of reported | | | | 45% | 97% | 96% |

Sources: Southern Energy, ECIS

1.3 ECIS Shows Net Loss of Rmb21m for 2016-18 Rather than Rmb650m Profit Reported

The two sources reveal diametrically opposite pictures in net profit for 2016-18. Southern Energy has reported net profit of Rmb214m, Rmb230m and Rmb206m, respectively, for the three years in question, with a total of Rmb650m. Conversely, ECIS data show that Guizhou Union was loss-making in each of those three years, totaling Rmb21m, as shown in Exhibit 5 below.

Exhibit 5 – ECIS shows Rmb21m of net loss for 2016-18 against the Rmb650m profit reported

| Year end Dec 31 (Rmb m) | 2016 | 2017 | 2018 | Total |
|-------------------------|------|------|------|------------|
| Net income - ECIS | -11 | -1 | -10 | -21 |
| Net income - reported | 214 | 230 | 206 | 650 |

Sources: Southern Energy, ECIS

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Part 2 Actual Output in 2018 About 1/3 of Reported

We have shown earlier that for 2018, Southern Energy's revenue is almost identical to that of Guizhou Union. Does that mean the company has repented and refrained from doctoring its books?

The answer, unfortunately, is a resounding NO. In this section, we demonstrate with abundant information collected from detailed investigations that the company's actual coal output in 2018 was about 1/3 of its reported volume. This information comes from people who are very familiar with Southern Energy's mining operations – clients, former staff such as coal miners, weighing scale operators and back office workers. Each piece of information is corroborated by at least two independent sources.

We need to point out here that obtaining the actual output data of individual coalmines is a very simple matter, because those who have such information regard it as in plain view. Even local residents know about such information. Take Luozhou Mine, for example.

- A shopkeeper at a small grocery store near the mine told us that "it could not produce any coal and had been shut down for a long time";
- In Weishe town 60 km away, a peasant said, "the mine was closed in 2018 due to losses";
- One local resident in the know told us a scam about this mine. Some time in 2017, Southern Energy tried to sell the mine. Just before the investors arrived for their on-site due diligence, a large amount of coal from the nearby Qingsong Mine was moved and stuffed down the mine. When the investors arrived, they witnessed coal being "mined" from under their feet, with some 20 heavy-duty trucks lining up to transport the coal. Unbeknown to these investors, this coal was sent back to Qingsong Mine.

Southern Energy's auditors, Deloitte, seem oblivious to the exaggerated output data. Have Deloitte gone through similar experiences to those of the above investors? Or did they never bother to go on site? One thing is clear: the Deloitte's understanding of key operational data is inferior to that of a local peasant.

2.1 Luozhou Mine Shut Down since Last August, Actual Output Only 5% of Reported for 2018

During the second quarter of 2019, Emerson Analytics investigators conducted a general on-site survey of the coal mines controlled by Southern Energy. Exhibit 6 below shows the main entrance of Luozhou Mine. The road in the photograph is the only vehicular access for the mine. For several days in a row, we saw that the mine was deathly quiet with no coal miners in sight. Absolutely no coal transport truck was seen.

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Exhibit 6 – Luozhou Mine main entrance is totally deserted



Source: Emerson Analytics

One ex-staff at Luozhou Mine told our investigator that this mine had been shut down since last August, after producing less than 20k tons earlier in the year.

Audio Evidence 1 – Luozhou Mine ex-staff says 2018 output less than 20k tons

| | |
|------------------------|--|
| Emerson investigator: | How much coal did they produce last year at this mine? |
| Luozhou Mine ex-staff: | They just worked for 3-4 months. |
| ... | |
| Emerson investigator: | From when did they begin production? |
| Luozhou Mine ex-staff: | It began in April, and ended in July. |
| ... | |
| Emerson investigator: | How much did they produce a month? |
| Luozhou Mine ex-staff: | Just about 4,000-5,000 tons. |

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| | |
|------------------------|---|
| Emerson investigator: | So that's 20k tons in four months? |
| Luozhou Mine ex-staff: | At most. |
| Emerson investigator: | No more than 20k tons? |
| Luozhou Mine ex-staff: | Exactly. |
| ... | |
| Emerson investigator: | Until when did this Mr. Tian (head of coalmining team) work in 2017? |
| Luozhou Mine ex-staff: | Until July, when a safety incident happened. |
| Emerson investigator: | There was an incident and production was suspended in July 2017? |
| Luozhou Mine ex-staff: | Yes. |
| Emerson investigator: | So this Mr. Zhou (head of another coalmining team) didn't start until April 2018? |
| Luozhou Mine ex-staff: | Correct. |
| ... | |
| Emerson investigator: | So, was 2015 or 2016 any better? |
| Luozhou Mine ex-staff: | No, no production at all. |
| Emerson investigator: | There was no production at that time? |
| Luozhou Mine ex-staff: | They were mainly excavating roadways then. |
| Emerson investigator: | When did they finish? When did they start formal production? |
| Luozhou Mine ex-staff: | There was never any formal production in 2015-16. |

Source: Emerson Analytics

The above information was corroborated by a senior staff at one of Southern Energy's corporate clients. He knows all basic information (such as production volume, quality of coal and coal prices) of Southern Energy's three coalmines in Hezhang County. He told us that there was virtually no production at Luozhou Mine in 2018.

Audio Evidence 2 – Customer's senior staff says Luozhou Mine had virtually no output in 2018

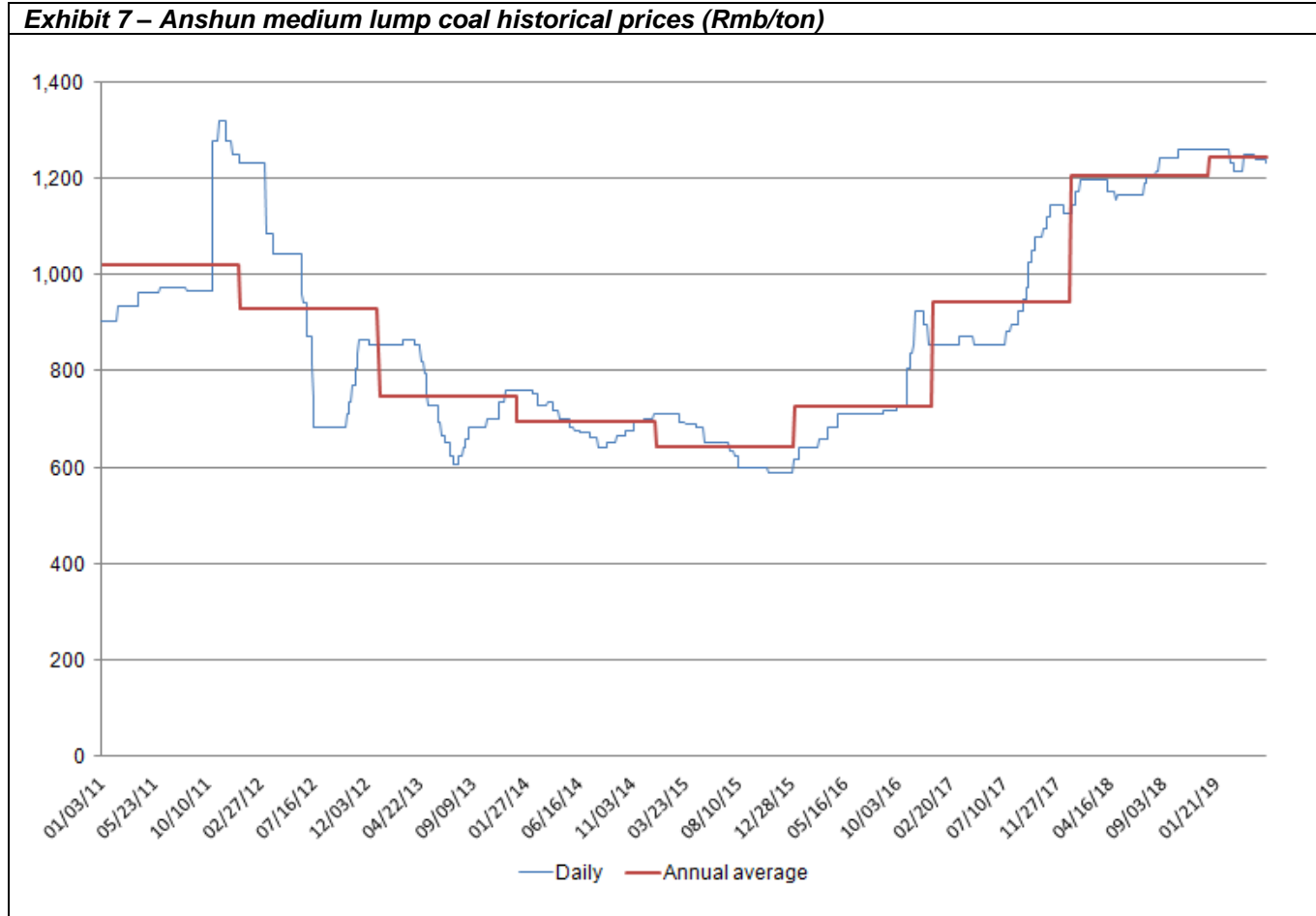
| | |
|--------------------------|---|
| Emerson investigator: | So, Luozhou Mine has stopped production? |
| Customer's senior staff: | Yes, it's stopped, since last year. |
| Emerson investigator: | Since last year? |
| Customer's senior staff: | Yes. |
| Emerson investigator: | Luozhou produced little coal last year? Just a tiny bit? |
| Customer's senior staff: | There was almost no output last year. |
| Emerson investigator: | No output last year? |
| Customer's senior staff: | The year before, initially, it began to have normal operations. Then an incident happened down in the shafts, and it stopped. |
| Emerson investigator: | Was the Luozhou Mine no good? |
| Customer's senior staff: | Correct. The resource was poor. |

Source: Emerson Analytics

Exhibit 7 below presents [Anshun medium lump coal historical prices](http://www.sxcoal.com/), which are obtained from China Coal Resource (<http://www.sxcoal.com/>). The website is operated by Shanxi Fenwei Energy Consulting Co., Ltd (山西汾渭能源諮詢有限公司), the industry consultant for Southern Energy when it applied for the IPO. Why would Luozhou Mine suspend production when coal prices are now at 10-year high? For more discussions on coal prices, please see "Part 4 Abnormally High Coal Prices".

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Exhibit 7 – Anshun medium lump coal historical prices (Rmb/ton)



Source: China Coal Resource

Southern Energy has claimed that it had 33.5m tons of total coal reserves (proved and probable) at the end of 2018, with Luozhou Mine, Weishe Mine and Lasu Mine accounting for 43%, 25% and 32%, respectively. The entire total reserve of 14.3m tons at Luozhou Mine was classified as probable reserve with nil proved reserve. Given the absence of any production at Luozhou Mine and its reserve structure, it is questionable if the reserve volume claimed by Southern Energy really exists.

2.2 Weishe Mine Actual Output of 90k Tons Merely a Quarter of Claim

Weishe Mine produced more coal than Luozhou Mine in 2018, but its real output was far less than the 388k tons claimed by Southern Energy.

An ex-staff at Weishe Mine told Emerson Analytics that it could produce about 10k tons of coal a month under normal circumstances. However, in the second half of 2018, frequent water leakage at the mine disrupted production, sometimes for as long as a whole month.

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Audio Evidence 3 – Weishe Mine ex-staff says normal output was 10k tons a month

Emerson investigator: How was production last year? How do you compare production this year and last?

Weishe Mine ex-staff: Last year was not good. Last year in the second half there were frequent water leakages down in the mine, and this disrupted our work.

Emerson investigator: Okay.

Weishe Mine ex-staff: When there's water leakage at the shaft we have to stop mining. We need to do further exploration to see what's happening.

...

Emerson investigator: How much coal did Weishe Mine produced in 2018?

Weishe Mine ex-staff: This mine is no good. You can't get much out of it a year.

Emerson investigator: What's your guess? How many tons a month?

Weishe Mine ex-staff: Probably 10k tons a month.

Emerson investigator: Oh, 10k tons a month.

Weishe Mine ex-staff: Sometimes not even that.

Emerson investigator: So sometimes you can get to 10k a month, and sometimes not?

Weishe Mine ex-staff: Yes.

Source: Emerson Analytics

One local coal vendor, who provided our investigators with the latest Weishe Mine coal prices, likewise confirmed that this mine could produce 10k tons a month under normal circumstances. He also confirmed that the mine did not operate normally in the second half of 2018.

Audio Evidence 4 – Local coal vendor confirms Weishe Mine output at 10k tons a month

Emerson investigator: How many tons a month did it manage last year?

Local coal vendor: In normal situations, it can reach 10k tons.

Emerson investigator: In a normal situation, 10k tons a month.

Local coal vendor: About 10k tons. There were many accidents in the second half last year and production was not normal.

Emerson investigator: When did this start? What month was it?

Local coal vendor: I'm not sure, perhaps July or August.

Source: Emerson Analytics

The customer's senior staff mentioned earlier supplied a similar figure, saying that Weishe Mine was producing about 200-300 tons a day.

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Audio Evidence 5 – Customer's senior staff says Weishe Mine produces 200-300 tons a day

| | |
|--------------------------|---|
| Customer's senior staff: | Weishe Mine output is not good. |
| Emerson investigator: | Output not good? How much can it produce? |
| Customer's senior staff: | Three to four cart loads, 200-300 tons a day. |
| Emerson investigator: | Was it any better last year? |
| Customer's senior staff: | It's always like that. |

Source: Emerson Analytics

We assume Weishe Mine's monthly output at 10k tons and that it achieved full production in nine months during 2018. This implies full year output of 90k tons, merely 23% of the 388k tons claimed by Southern Energy.

2.3 Lasu Mine Output Also Below Claim

Lasu Mine is the best performer of the three mines in terms of the production volume. Even so, its real output is way below that claimed by Southern Energy.

One ex-staff of Lasu Mine told Emerson Analytics that the mine averages 22k-23k tons a month.

Audio Evidence 6 – Lasu Mine ex-staff says monthly output 22k-23k tons

| | |
|-----------------------|---|
| Emerson investigator: | How much can Lasu Mine produce a month now? |
| Lasu Mine ex-staff: | Our mine normally produces more than 20k tons, about 22k-23k. |
| Emerson investigator: | What about output last year? |
| Lasu Mine ex-staff: | The same. |
| Emerson investigator: | The same? |
| Lasu Mine ex-staff: | Yes. |

Source: Emerson Analytics

Again, the customer's senior staff that we mentioned earlier corroborated Lasu Mine ex-staff's information. He told Emerson Analytics that in a normal day, Lasu Mine produces about 700 tons, which implies a total of just over 20k tons a month.

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Audio Evidence 7 – Customer's senior staff says daily output 700 tons

| | |
|--------------------------|---|
| Emerson investigator: | How much is Lasu Mine's output, on a daily or monthly basis? |
| Customer's senior staff: | On a normal day, about 700 tons. |
| Emerson investigator: | Normally, 700 tons? |
| Customer's senior staff: | Yes. |
| Emerson investigator: | So, how much did it achieve last year on a monthly average basis? |
| Customer's senior staff: | More than 20k (tons). |

Source: Emerson Analytics

Again, using assumptions most advantageous to the company, we can let Lasu Mine's average monthly output be 23k tons, then the full year 2018 production was 276k (= 23 x 12) tons. This is barely three-quarters of the 381k tons claimed by Southern Energy.

The above conversations were recorded in the first half of 2019. We are sharing the audio recordings and relevant information such as the interviewees' names, positions, contact telephone numbers and dates of meeting with the SFC.

2.4 All Told, Actual Output Only 1/3 of Claim

Aggregating the actual output data for the three mines, we can see that they produced about 386k tons in total during 2018. This is just about one-third of Southern Energy's claim. Bear in mind that our estimates are based on assumptions most advantageous to the company.

Exhibit 8 – Actual output in 2018 only 1/3 of claim (k tons)

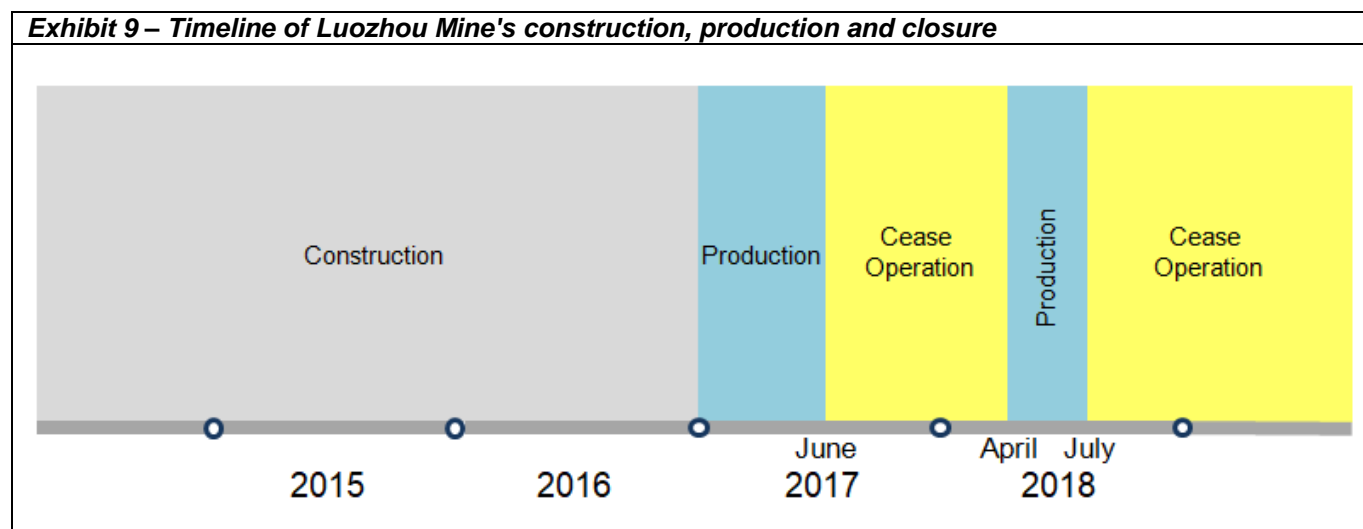
| | Company's claim | Actual data | Actual as % of claim |
|--------------|--------------------|----------------|-------------------------|
| Luozhou Mine | 373 | 20 | 5% |
| Weishe Mine | 388 | 90 | 23% |
| Lasu Mine | 381 | 276 | 72% |
| Total | 1,142 | 386 | 34% |

Sources: Southern Energy, Emerson Analytics

The situation in previous years was similar to or even worse than that in 2018. Our investigations into Luozhou Mine (discussed in section 2.1 above) reveal a timeline of its construction, production and

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closure. Two sources told us the mine ceased operations in mid-2017 after a safety incident. We believe they referred to the collapse of tunnel roof at the coal face July 4, 2017, which resulted in two deaths.¹



Source: Emerson Analytics

Luozhou Mine was still under construction in 2016 when there was no production at all. Southern Energy dared claim it had the largest output of all three mines that year. Luozhou Mine is said to have been in production every year throughout 2013-18, with total output of 1,699k tons. From Exhibit 9, it is clear that the mine was in production only briefly during 2017 and 2018, aggregating not even 10 months. What outrageous lies!

¹ <http://www.bjje.gov.cn/bm/bjsyjglj/gk/xxgkml/tzgg/174656.shtml>

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Part 3 Bogus Sales to Major Clients

In Part 2 earlier, we have provided concrete evidence that actual output volume was way below that claimed by Southern Energy.

In this section, we will analyze the problem from the customers' angle. Our investigations show that much of the sales to Southern Energy's major clients is exaggerated.

3.1 Sales to Major Clients Exceed Clients' Own Revenue

The IPO prospectus discloses the company's six largest customers: (i) Liupanshui Pinggui Trading Company Limited (Liupanshui Pinggui, 六盤水蘋貴經貿有限公司); (ii) Hezhang Tongchuang Mining Company Limited (Hezhang Tongchuang, 赫章縣同創礦業有限公司); (iii) Wuhan Ruierte Industry and Trading Company Limited (Wuhan Ruierte, 武漢銳爾特工貿有限公司); (iv) Guizhou Ruijinhang Trading Company Limited (Guizhou Ruijinhang, 貴州瑞金航貿易有限公司); (v) Guizhou Jinkun Trading Company Limited (Guizhou Jinkun, 貴州金坤貿易有限公司); (vi) Liupanshui Zhongshan Xingfeng Coal Preparation Plant (Xingfeng CPP, 六盤水市鐘山區杏豐洗煤廠).

During 2013-15, Southern Energy sold a total of Rmb114m, Rmb276m and Rmb370m, respectively, to these six clients, accounting for 60%, 73% and 76%, respectively, of its total sales. After the IPO, the company only disclosed "revenue from customers individually contributing over 10% of total", without revealing their names. Based on the trends of the numbers, we know that Southern Energy sold Rmb100m of coal to Liupanshui Pinggui and Rmb72m to Guizhou Ruijinhang in 2016.

The key financial data of these six major customers have been obtained from ECIS. In Exhibit 10 below, we compare Southern Energy's sales to these six customers against their respective revenue. It is evident that four of these companies consistently achieved less revenue than what Southern Energy had purported to have sold to them.

Revenue Inflated by Five Times

Exhibit 10 – Financial abnormality of Southern Energy customers

| Year end Dec 31 (Rmb m) | 2013 | 2014 | 2015 | 2016 |
|--|------|------|------|------|
| Southern Energy's sales to customers (i.e. customers' cost of goods sold) | | | | |
| Liupanshui Pinggui | 24 | 67 | 99 | 100 |
| Hezhang Tongchuang | 28 | 56 | 72 | — |
| Wuhan Ruierte | 18 | 48 | 66 | — |
| Guizhou Ruijinhang | 17 | 49 | 61 | 72 |
| Guizhou Jinkun | 10 | 22 | 47 | — |
| Xingfeng CPP | 17 | 34 | 26 | — |
| Customers' revenue according to ECIS | | | | |
| Liupanshui Pinggui | 280 | 133 | 117 | 70 |
| Hezhang Tongchuang | 2 | 21 | 2 | — |
| Wuhan Ruierte | 10 | 5 | 8 | — |
| Guizhou Ruijinhang | 0 | 6 | 0 | 0 |
| Guizhou Jinkun | 0 | 0 | 0 | — |
| Xingfeng CPP | 147 | 116 | 72 | — |
| Abnormality (Customers' revenue minus COGS) | | | | |
| Liupanshui Pinggui | ✓ | ✓ | ✓ | -31 |
| Hezhang Tongchuang | -26 | -35 | -70 | — |
| Wuhan Ruierte | -9 | -43 | -59 | — |
| Guizhou Ruijinhang | -17 | -43 | -61 | -72 |
| Guizhou Jinkun | -10 | -22 | -47 | — |
| Xingfeng CPP | ✓ | ✓ | ✓ | — |

Sources: Southern Energy, ECIS, Emerson Analytics

Take Wuhan Ruierte for example. During 2013-15 Wuhan Ruierte bought Rmb18m, Rmb48m and Rmb66m, respectively, of coal from Southern Energy. Yet its revenue was merely Rmb10m, Rmb5m and Rmb8m, respectively, during the period. This means that even if Southern Energy were the only supplier to Wuhan Ruierte, which then sold everything at cost, it would have to report negative gross profit of Rmb9m, Rmb43m and Rmb59m, respectively, for the years in question.

3.2 Liupanshui Pinggui Never Bought Anthracite Coal to Make PCI Fine Coal

Exhibit 10 above shows that Liupanshui Pinggui's revenue during 2013-15 exceeded the sales that Southern Energy claimed to have achieved. Does this make Liupanshui Pinggui a bona fide customer for Southern Energy with no monkey business? No. Far from it.

For 2016, Southern Energy claimed that it sold Rmb100m of coal products to Liupanshui Pinggui. However, the latter reported revenue of merely Rmb70m to ECIS.

Revenue Inflated by Five Times

During the first half of 2019, we visited Southern Energy's two major customers in Liupanshui City in western Guizhou Province. Xingfeng CPP is recorded as "Operations Ceased" during 2017-18 in ECIS, and we saw no one at its premises. Nearby, there were several CPPs. Our investigators talked to staff at three of them. They all said that their respective plants mainly worked for Shougang Group Shuicheng Steel Company (Shuicheng Steel, 首鋼水城鋼鐵(集團)有限責任公司) supplying PCI fine coal. Shuicheng Steel is the largest steel producer in Guizhou, ranking 15th among all enterprises in Guizhou in 2017 with revenue of Rmb14.8bn. These people also told us that many CPPs in Liupanshui were suppliers of Shuicheng Steel.

Southern Energy claims that its fine coal is mainly used in the production of PCI coal. It is therefore reasonable to assume that Liupanshui Pinggui buys fine coal from Southern Energy for the same purpose. Surprisingly, one staff at Liupanshui Pinggui's CPP told us that although his company was a supplier of Shuicheng Steel, it had always been producing coking coal (whose raw material is bituminous coal) only, and that it had never bought any anthracite coal. Could it be that Liupanshui Pinggui had bought some just for trading, and not for the manufacture of higher value-added PCI coal?

Audio Evidence 8 – Liupanshui Pinggui staff says they don't do PCI coal

| | |
|---------------------------|---|
| Emerson investigator: | Do you have coal for PCI use for steel plants? The anthracite coal for PCI? |
| Liupanshui Pinggui staff: | No, we don't do PCI. We do coking coal only. |
| Emerson investigator: | Only coking coal? |
| Liupanshui Pinggui staff: | Only coking coal. |
| Emerson investigator: | What about before? Several years ago? Like in 2015, 2016? |
| Liupanshui Pinggui staff: | No. |
| Emerson investigator: | Never did that? |
| Liupanshui Pinggui staff: | Never. |

Source: Emerson Analytics

3.3 The Search for Guizhou Ruijinhang and Guizhou Jinkun

We discuss Guizhou Ruijinhang together with Guizhou Jinkun because of the many links and similarities between the two:

- According to ECIS, except for Guizhou Ruijinhang's Rmb6m revenue in 2014, the two companies achieved zero revenue in 2013-15;
- The two companies share the same contact telephone numbers: +(851) 8861-8776 for fixed telephony and +186-8523-0266 for mobile services. They are both registered in Guiyang, the capital of Guizhou Province;
- The two are often marked as being in a state of "abnormal operations" in their ECIS entries. Guizhou Ruijinhang was placed on the "abnormal operations" list in July 2016 due to its failure to

Revenue Inflated by Five Times

report its 2015 annual report and has remained on the list since then. Guizhou Jinkun was placed on the same list in July 2015 for failing to publish its 2013 and 2014 annual reports. A few months before Southern Energy's IPO, Guizhou Jinkun submitted its 2013 and 2014 annual reports and was then taken off the list;

- The two companies cannot be found at their respective registered addresses. Guizhou Ruijinhang's registered address is 71 Suocao Road, Nanming District, Guiyang City (貴陽市南明區蕘草路71號), where we found a braised meat shop instead, as shown in Exhibit 11 below. Guizhou Jinkun's registered address is Unit 10, Building 340, Fuyuan South Road, Nanming District, Guiyang City (貴陽市南明區富源南路340棟10號). Our investigators spent almost a whole day searching around Fuyuan South Road and could not find this place.

Exhibit 11 – A braised meat shop is located at 71 Suocao Road



Source: Emerson Analytics

We dialed the fixed-line number +(851) 8861-8766, supposedly the contact number shared by the two companies, only to find that it had been disconnected. We also dialed the mobile number +186-8523-0266 that they shared. The person who answered the call quickly hung up without saying anything after

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we asked if we could buy any coal. We called back right away to ask about buying coal, and she simply answered "No" and then hanged up again.

Can you believe such two companies bought Rmb205m worth of coal, 19% of Southern Energy's total, during the 2013-15 period?

3.4 Actual Sales to Six Major Clients only 16% of Claim

We summarize Southern Energy's actual sales to these six major customers in Exhibit 12 below. As explained earlier, Southern Energy in reality made no sales to Liupanshui Pinggui, Guizhou Ruijinhang and Guizhou Jinkun during 2013-15. For Hezhang Tongchuang and Wuhan Ruierte, Southern Energy's sales could not have exceeded their respective revenue, which were reported to ECIS. For Xingfeng CPP, we simply adopt the number disclosed by Southern Energy in the absence of any concrete evidence of forgery.

Thus, Southern Energy's real sales to the six major customers during 2013-15 were Rmb29m, Rmb60m and Rmb35m, respectively, merely 25%, 22% and 10% of reported numbers. In aggregate, the real sales amounted to 16% of reported sales during the three-year period.

| Exhibit 12 – Actual sales to major customers only 16% of reported number | | | | | |
|---|-------------|-------------|-------------|--------------|--------------------------------|
| Year end Dec 31 (Rmb m) | 2013 | 2014 | 2015 | Total | Remarks |
| Liupanshui Pinggui | 0 | 0 | 0 | 0 | See section 3.2 above |
| Hezhang Tongchuang | 2 | 21 | 2 | 25 | Total revenue reported to ECIS |
| Wuhan Ruierte | 10 | 5 | 8 | 23 | Total revenue reported to ECIS |
| Guizhou Ruijinhang | 0 | 0 | 0 | 0 | See section 3.3 above |
| Guizhou Jinkun | 0 | 0 | 0 | 0 | See section 3.3 above |
| Xingfeng CPP | 17 | 34 | 26 | 77 | Southern Energy disclosure |
| Total | 29 | 60 | 35 | 124 | |
| Southern Energy disclosure | 114 | 276 | 370 | 760 | |
| Actual as % of disclosed | 25% | 22% | 10% | 16% | |

Source: Emerson Analytics

Revenue Inflated by Five Times

Part 4 Abnormally High Coal Prices

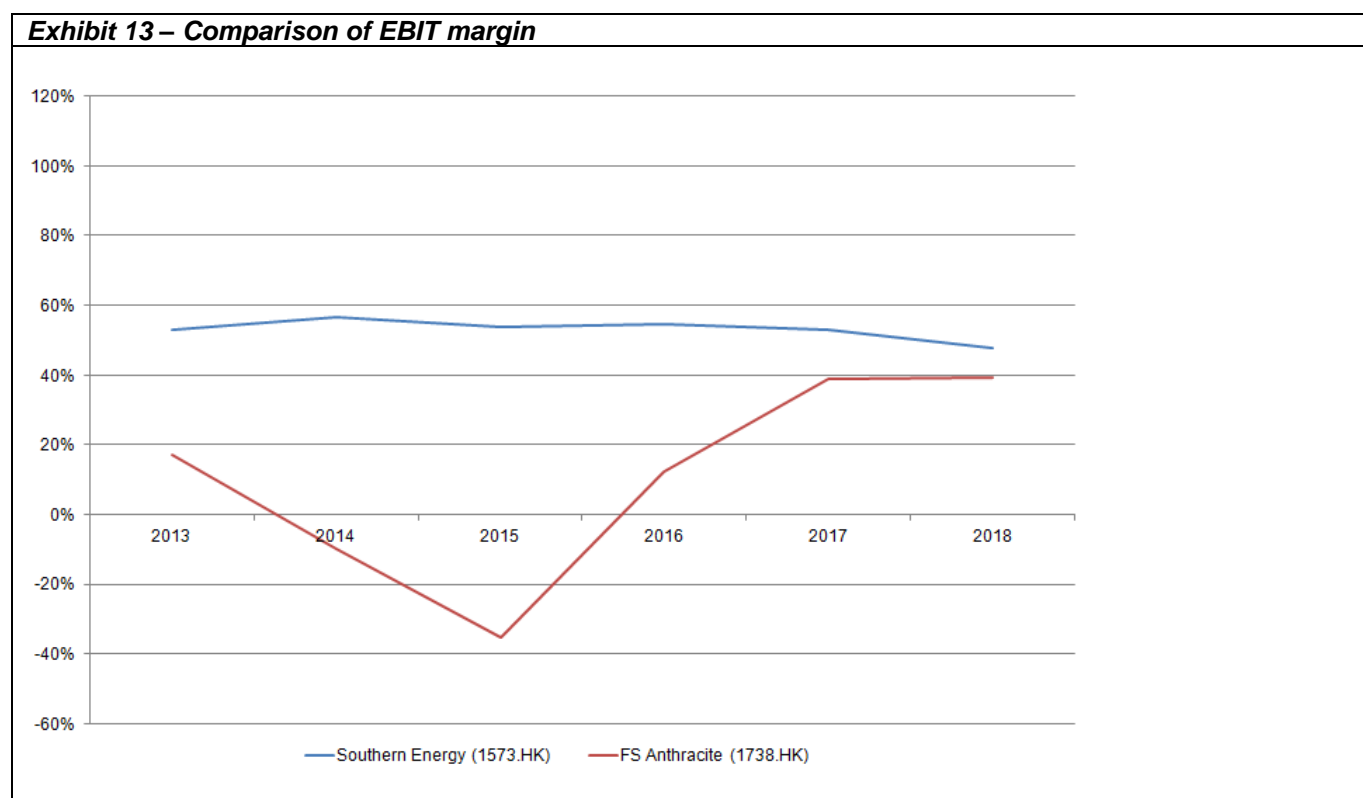
We have earlier analyzed Southern Energy's financial performance from three different angles: ECIS financial data, output at its three coalmines, and sales to major customers. There is little doubt that the company's actual revenue is far below its claims.

In this section, we analyze the average selling prices (ASPs) that Southern Energy purportedly achieved in the last few years. It is obvious that its high ASPs are simply outrageous lies.

4.1 High EBIT Margins Driven by High ASPs

Other than Southern Energy and FS Anthracite, there is a third Guizhou coalmining company listed in Hong Kong: Perennial Energy Holdings Limited (PER Energy, 2798.HK).

FS Anthracite is more comparable to Southern Energy because both are producers of anthracite coal. For PER Energy, its output is coking coal which is a kind of bituminous coal. It also focuses more on processing raw coal. On the other hand, Southern Energy's CPPs merely remove the coal gangue in raw coal. We are therefore leaving out PER Energy in our margin comparison below.



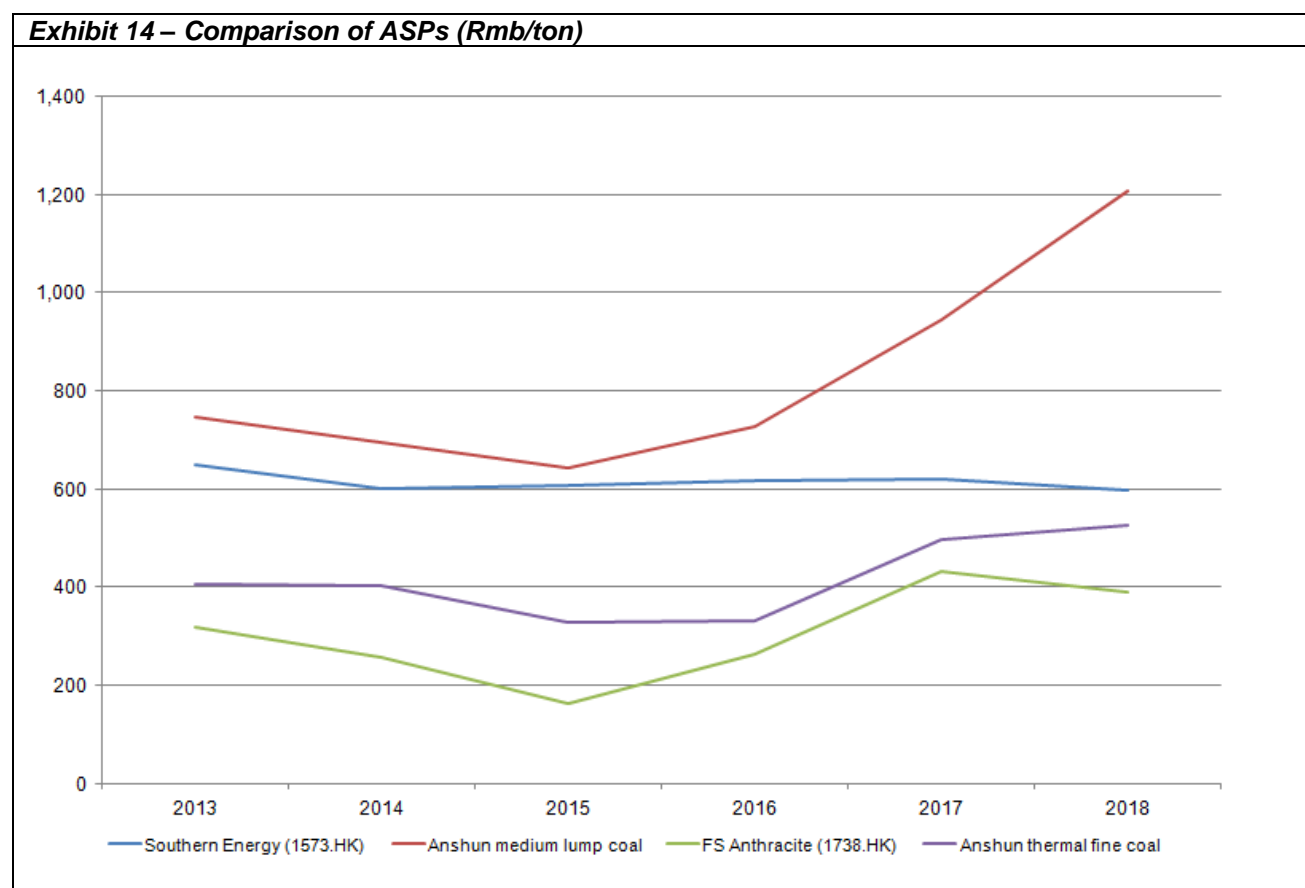
Sources: Southern Energy, FS Anthracite

Revenue Inflated by Five Times

It is clear from Exhibit 13 that Southern Energy's earnings before interest and tax (EBIT) margins have consistently exceeded those of FS Anthracite. In particular, FS Anthracite suffered losses before interest and tax in 2014 and 2015 when coal prices fell substantially. Southern Energy, amazingly, claimed it was immune from price declines. In 2016 and 2017, FS Anthracite's EBIT margins recovered on the back of coal price rebound, but Southern Energy continued to report stable margins.

Note that our margin analysis does not include the massive PPE impairment loss recorded by FS Anthracite during 2013-16. During these four years, FS Anthracite provided for Rmb184m, Rmb66m, Rmb384m and Rmb101m of impairment losses, respectively, equivalent to about 32% of its net fixed asset value at the beginning of 2013.

Southern Energy attributes its superior margins to the higher ASPs than its competitors in the region although the production costs of the coals were similar. In Exhibit 14 below, we can see that Southern Energy had always achieved higher ASPs than FS Anthracite, with a ratio of as much as 3.7x in 2015 and 1.5x in 2018.



Sources: Southern Energy, FS Anthracite, China Coal Resource

Revenue Inflated by Five Times

4.2 Southern Energy ASPs Buck Industry Trend

Exhibit 14 above also presents the market prices of Anshun medium lump coal and Anshun thermal fine coal as benchmarks. Strangely, Southern Energy's ASPs were essentially unaffected by market conditions.

In the face of a shortage of thermal coal for power generation use in 2018, the Guizhou government required every coalmine in the province to supply a certain amount of raw coal to the local power plants. Consequently, Southern Energy said its raw coal sales volume accounted for 47% of total volume that year, compared with only 12% in 2017. The company might therefore argue that this explained the mild decline in its 2018 ASP, which deviated from market trend.

But for 2017, it is difficult to see why Southern Energy's ASP remained static around the 2016 level, when raw coal accounted for a very small proportion of total sales volume. During the year, Anshun medium lump coal saw its average price jumping 30% from the 2016 level, with Anshun thermal fine coal surging 50%.

Could it be possible that Southern Energy's coal quality deteriorated significantly in 2017? No. The company's 2017 annual report says, "We possess scarce anthracite coal resources with the characteristics of high calorific value, low sulfur content and low ash content". This description is exactly the same as that in its IPO prospectus, which indicates that there was not much change in its coal quality.

This significant deviation in Southern Energy's ASPs during 2017-18 from the market trend may well suggest that the company had exaggerated its ASPs in earlier years.

4.3 Investigations Show the Company's High ASP Drivers are Fakes

Southern Energy cites two factors for achieving ASPs far higher than those of its competitors:

- The anthracite products produced by its competitors are mostly thermal coal, while those of Southern Energy are mostly chemical lump coal (74%) and PCI fine coal (25%). The price of chemical lump coal and PCI fine coal is far higher than that of thermal coal; and
- Due to the high strength of Southern Energy's coal, the company maintained large output of big lump coal and medium lump coal which generally command higher selling prices among anthracite coal products.

Exhibit 15 below presents Southern Energy's revenue, sales volume and ASPs as categorized by the size of coal.

Revenue Inflated by Five Times

| Exhibit 15 – Revenue, sales volume and ASPs (2013-18) | | | | | | |
|--|----------------|----------------|----------------|----------------|----------------|----------------|
| | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 |
| Revenue (Rmb k) | 190,776 | 378,721 | 485,874 | 690,985 | 642,432 | 641,191 |
| Coal products | | | | | | |
| Big lump coal (+120mm) | 53,361 | 108,000 | 136,301 | — | — | — |
| Medium lump coal (80-120mm) | 43,247 | 86,249 | 105,879 | — | — | — |
| Clean coal (8-80mm) | 35,211 | 70,062 | 129,229 | — | — | — |
| Fine coal (-8mm) | 58,957 | 114,410 | 114,465 | — | — | — |
| Raw coal | | | | | — | — |
| Sales volume (k tons) | 295 | 630 | 803 | 1,120 | 1,037 | 1,073 |
| Coal products | | | | | | |
| Big lump coal (+120mm) | 56 | 128 | 168 | 235 | 187 | 90 |
| Medium lump coal (80-120mm) | 56 | 123 | 157 | 208 | 169 | 85 |
| Clean coal (8-80mm) | 60 | 126 | 219 | 392 | 319 | 227 |
| Fine coal (-8mm) | 123 | 252 | 258 | 284 | 234 | 165 |
| Raw coal | | | | | 129 | 506 |
| ASP (Rmb/ton) | 647 | 601 | 605 | 617 | 620 | 598 |
| Coal products | | | | | | |
| Big lump coal (+120mm) | 945 | 844 | 812 | — | — | — |
| Medium lump coal (80-120mm) | 779 | 699 | 674 | — | — | — |
| Clean coal (8-80mm) | 591 | 554 | 590 | — | — | — |
| Fine coal (-8mm) | 479 | 454 | 443 | — | — | — |
| Raw coal | | | | | — | — |

Source: Southern Energy

We assume that the 506k tons of raw coal in 2018 had similar proportions of coal products in terms of size, although coal preparation process may affect these proportions a bit. This means 29% of the volume sold was fine coal (-8mm) with the remaining 71% being lump coal (+8mm) in the year.

However, our on-site investigations revealed that the reality was the other way around: the cheaper fine coal accounted for 80% of output, with the higher priced lump coal accounting for some 20%.

Below is a transcript of our conversation with the customer's senior staff mentioned earlier.

Revenue Inflated by Five Times

Audio Evidence 9 – Fine coal accounted for 80% of output

| | |
|--------------------------|---|
| Emerson investigator: | Of their output, fine coal accounted for a bigger proportion? |
| Customer's senior staff: | Fine coal accounted for the majority of output. |
| Emerson investigator: | How much did it account for? |
| Customer's senior staff: | About four-fifths. |
| Emerson investigator: | Four-fifths means fine coal is 80% of total? |
| Customer's senior staff: | Yes. |

Source: Emerson Analytics

According to our investigations, the claimed usage of chemical lump coal and PCI fine coal is also total rubbish. The actual usage of Southern Energy's coal turns out to be thermal fine coal used by power plants nearby, such as Bijie power plant, Dafang power plant and Nayong power plant. This conforms to the fact that Southern Energy mainly produces fine coal.

4.4 Peculiar Benchmark Coal Prices

According to Southern Energy's IPO prospectus, coal products produced in Anshun City, Jinsha County and Zhijin County (all in Guizhou Province) have similar quality to those produced by the company. The ASPs of Anshun big lump coal, Anshun medium lump coal, Jinsha small lump coal, Zhijin PCI fine coal and Anshun thermal fine coal are said to correlate to those of Southern Energy's relevant coal products.

Exhibit 16 below shows technical indicators of the five types of benchmark coal obtained from China Coal Resource. Anshun big lump coal refers to the one with ash 12%; volatility 7.5%; sulfur 0.9%; calorific value 6800kcal/kg and size ~80mm. Technical indicators of the five types of benchmark coal obtained from [China Coal Market](#), another website that provides coal industry data, are virtually identical to data from China Coal Resource.

Exhibit 16 – Technical indicators for benchmark coal

| | Ash (%) | Volatility (%) | Sulfur (%) | Calorific value (kcal/kg) | Size (mm) | IPO prospectus (mm) |
|--------------------------|------------|-------------------|---------------|---------------------------------|--------------|---------------------------|
| Anshun big lump coal | 12 | 7.5 | 0.9 | 6800 | ~80 | +120 |
| Anshun medium lump coal | 11 | <10 | 1 | >7000 | ~55 | 80-120 |
| Jinsha small lump coal | 16-18 | 6.5 | 0.4 | 6600 | ~22 | 8-80 |
| Zhijin PCI fine coal | <13.5 | <10 | <0.8 | >6300 | -13 | -8 |
| Anshun thermal fine coal | 28 | 6 | 0.4 | 5000 | -13 | -8 |

Source: China Coal Resource, IPO prospectus

Revenue Inflated by Five Times

However, Southern Energy "created" its own size categories (red in Exhibit 16) in its IPO prospectus. Thus, we need to distinguish between two types of Anshun big lump coal. ABLC-IC, according to industry consensus, is about 80mm in size. Industry consensus does not provide for another category of bigger lumps. ABLC-SE, as defined by Southern Energy, has exactly the same technical indicators though it is said to be bigger than 120mm in size.

Compared with other technical indicators, the importance of size is relatively low. One can see from Exhibit 17 below that ABLC-IC was priced at a very stable premium of Rmb34/ton or 4% over Anshun medium lump coal-IC during 2016-18. Prices for these five types of benchmark coal in the table come from China Coal Resource, and they deviate only marginally from China Coal Market prices.

We can also see a few abnormalities:

- Prices for ABLC-SE were significantly higher than those for ABLC-IC. During 2013-15, the former was more expensive than the latter by 21%, 19% and 16%, respectively. With identical technical indicators except for size, how could there be such a big price difference?
- Although the technical indicators were different, prices for Anshun medium lump coal-SE were the same as those for ABLC-IC (highlighted in red in Exhibit 17).
- Neither China Coal Resource nor China Coal Market provides any data for ABLC-SE. So where did prices for ABLC-SE come from?

| Exhibit 17 – Coal price comparisons (Rmb/ton) | | | | | | |
|--|-------------|-------------|-------------|-------------|-------------|-------------|
| | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 |
| ABLC-IC | 783 | 730 | 674 | 760 | 977 | 1,241 |
| ABLC-SE | 945 | 866 | 784 | — | — | — |
| Anshun medium lump coal-IC | 746 | 695 | 643 | 727 | 943 | 1,207 |
| Anshun medium lump coal-SE | 783 | 730 | 674 | — | — | — |
| Jinsha small lump coal-IC | 710 | 704 | 631 | 697 | 909 | 1,173 |
| Jinsha small lump coal-SE | 727 | 700 | 637 | — | — | — |
| Zhijin PCI fine coal-IC | 739 | 648 | 575 | 503 | 706 | 870 |
| Zhijin PCI fine coal-SE | 738 | 648 | 576 | — | — | — |
| Anshun thermal fine coal-IC | 406 | 402 | 329 | 331 | 496 | 526 |
| Anshun thermal fine coal-SE | 405 | 402 | 329 | — | — | — |

Sources: China Coal Resource, Southern Energy

Revenue Inflated by Five Times

As can be seen from Exhibit 18 below, Southern Energy claims in its IPO prospectus that its big lump coal has been sold at prices close to its so-called benchmark, ABLC-SE. However, such prices were way higher than the real market benchmark, by 21%, 16% and 20%, respectively, during 2013-15. Clearly, the only rationale for creating its own benchmark is to dress up its bogus claim of achieving higher than market prices.

| | 2013 | 2014 | 2015 |
|---|-------------|-------------|-------------|
| ABLC-IC | 783 | 730 | 674 |
| ABLC-SE | 945 | 866 | 784 |
| Big lump coal ASP claimed | 945 | 844 | 812 |
| Premium of big lump coal ASP claimed over ABLC-IC | 21% | 16% | 20% |
| Premium of big lump coal ASP claimed over ABLC-SE | 0% | -3% | 4% |

Sources: China Coal Resource, Southern Energy

Revenue Inflated by Five Times

Part 5 Financials and Valuation

In the earlier four sections, we have analyzed Southern Energy's outrageous accounting fraud from ECIS revenue, production, customers and market price angles. All told, they suggest that Southern Energy's actual revenue during 2013-18 only amounted to 20% of reported numbers.

By keeping a persistently higher P/E ratio since listing, controlling shareholder Xu Bo has maintained this Ponzi scheme by raising funds through selling and pledging his shares. This is no longer sustainable now.

Because of its serious accounting fraud and liquidity difficulties, we rate Southern Energy as DELISTING.

5.1 Aggregate Revenue 2013-18 Just 20% of Claimed

Applying the same proportion of major clients' sales exaggeration in Part 3 above to other customers, we can deduce that during 2013-15, the company's total revenue was actually Rmb48m, Rmb82m and Rmb46m, respectively.

According to Part 1 above quoting ECIS data, Southern Energy's actual revenue in 2016 was Rmb81m and in 2017 Rmb134m.

From Part 2 above, actual coal output was at most 34% of claimed in 2018. Generously assuming the disclosed ASP as accurate, then the company's actual revenue in 2018 would be only 34% of disclosed numbers.

Exhibit 19 below presents Southern Energy's actual and reported revenue during 2013-18. In aggregate, the company reported Rmb3,030m of revenue for the six-year period, but we estimate that it only achieved sales of Rmb609m, merely 20% of its claim.

| Exhibit 19 – Actual revenue averages 20% of claim historically | | | | | | | |
|---|-------------|-------------|-------------|-------------|-------------|-------------|--------------|
| Year end Dec 31 (Rmb m) | 2013 | 2014 | 2015 | 2016 | 2017 | 2018 | Total |
| Revenue – reported | 191 | 379 | 486 | 691 | 642 | 641 | 3,030 |
| Revenue – actual | 48 | 82 | 46 | 81 | 134 | 217 | 609 |
| Actual as % of reported | 25% | 22% | 10% | 12% | 21% | 34% | 20% |

Sources: Southern Energy, Emerson Analytics

Revenue Inflated by Five Times

With a five-time revenue inflation, it is natural that profit is seriously exaggerated. We have shown in section 1.3 that ECIS data reveal a net loss of Rmb21m for 2016-18 rather than the Rmb650m profit claimed by Southern Energy.

5.2 Share Disposal and Pledge at High Valuations

Exhibit 20 below shows the valuation of three Guizhou coalmining companies that are listed on the Hong Kong market. It is obvious that Southern Energy trades at a P/E that is far higher than its peers. During January 17, 2017 through January 22, 2018, Southern Energy was listed by the Stock Exchange of Hong Kong as a stock with highly concentrated ownership. This is likely a key reason why the shares have tended to trade at such a huge premium over its peers.

| Company | Share price (HK\$) | Market cap (HK\$ m) | 2018 Net income (Rmb m) | P/E (x) |
|---------------------------|-------------------------------|--------------------------------|--|----------------|
| Southern Energy (1573.HK) | 9.95 | 7,144 | 206 | 30.5 |
| FS Anthracite (1738.HK) | 1.00 | 1,381 | 201 | 6.1 |
| PER Energy (2798.HK) | 1.53 | 2,448 | 176 | 12.2 |

Source: Emerson Analytics

To maintain a Ponzi scheme or to eventually take the money and run, a fraudulent controlling shareholder keeps the company stock at inflated levels and then either disposes of his shares and/or puts them up as collaterals for loans in order to raise liquidity. This is the case for Southern Energy.

- In April 2017, just nine months after the IPO, controlling shareholder and chairman Xu pledged 143.6m shares or 20% of total issued capital to CMB International Finance Limited, (CMBI Finance, a sister company of China Merchants Securities (HK) Co., Limited, joint bookrunner and joint lead manager of Southern Energy's IPO). It is not clear how big the loan was. Based on the roughly HK\$6 share price during that time, he probably received HK\$340m on a 40% collateral ratio;
- In May 2018, Xu sold 123.4m shares or 17.2% of total issued capital to Hezhang County Hongyi Construction Engineering Co., Ltd. (赫章縣宏誼建築工程有限責任公司), a company owned by the People's Government of Hezhang County. At HK\$8.70 per share, the sale raised HK\$1.08bn for Xu;

Revenue Inflated by Five Times

- A year later, on June 6, 2019, Xu entered into a framework agreement to sell 143.6m shares to Bijie City Anfang Construction Investment (Group) Co., Ltd.(畢節市安方建設投資(集團)有限公司), a company controlled by the People's Government of Bijie City, where Hezhang County is located. Xu would then be left with about 13.6% of Southern Energy, making him the third largest shareholder. Around the current market price of some HK\$10 a share, the sale proceeds of HK\$1.44bn would go to Xu's pocket entirely.

Why would the local government decision-makers want to buy an over-valued stake in a fraudulent company?

5.3 Southern Energy's Financial Health

Southern Energy itself is also short of funds, just like controlling shareholder Xu. Despite its reported Rmb1.03bn net profit during 2013-18, the company has been trying to raise funds in some strange manners.

- On June 27, 2018, the company announced a small private placement of unlisted warrants to an individual named Yang Wei. The proposed issue of 5m warrants at HK\$2.32 each would raise merely HK\$11.4m after expense. Upon exercise in full on a one-for-one basis at HK\$12 per share, Southern Energy would raise an additional HK\$60m before expenses;
- On June 20, 2019, Southern Energy announced a proposed senior notes program through CMB International Capital Limited (another sister company of China Merchants Securities (HK) Co., Limited) and Standard Chartered Bank. Terms including the amount of issue are yet to be decided. The issue is said to be used for the company's "working capital".

5.4 DELISTING as the Scam Unsustainable

It now appears that Xu and Southern Energy cannot sustain their scam anymore.

Recently, CMBI Finance has sold 160k Southern Energy shares at about HK\$11 each on the market. According to the dealings disclosure, CMBI Finance disposed of such shares because Xu could not repay his debt.

Southern Energy itself is also having difficulties raising funds, as its warrants are yet to be issued one year after the announcement.

Given its seriously fraudulent accounts and liquidity difficulties, we rate Southern Energy a DELISTING.

Revenue Inflated by Five Times

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 \$0.315, 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 | Current share price \$5.92, down 24% 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 \$1.91, down 69%, 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 \$4.47, up 24%, compared with our \$2.40 target | EY | Morgan Stanley Credit Suisse |