



Emerson Analytics Co., Ltd.
www.emersonanalytics.cloud
emersonanalyticscoltd@gmail.com

Zhou Hei Ya – Phantom "Customers"

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Zhou Hei Ya published an amazing "clarification" March 6. To begin with, we just sample two of the many mistakes in the "clarification" announcement:

- The last paragraph in p.4 of the "clarification" says, "The Report alleged that the Group's Central China ADSV for the three months ended 30 September 2018 is inflated by 28%". The management must be seeing things. The fourth paragraph on the cover of our March 1 report says clearly Central China ADSV "was 38.7% more than the true ADSV..."
- The first paragraph in p.6 of the "clarification" says, "The Report is also unclear as to how the 11 stores subject to real time monitoring were picked...the Group assumes that the author of the Report did not maliciously pick lower performing stores". The first paragraph in p.12 of our March 1 report states clearly that "we conducted real-time monitoring on 11 retail stores with relatively large business volume". And data in Exhibit 13 in p.18 shows that the nine Hunan stores being monitored accounted for 56% of total sales volume in this province.

The "clarification" also makes some stand-alone assertions, including a claim in the third paragraph of p.4 that "the Group's Central China ASPO was approximately Rmb10 higher than the national average". Based on Zhou Hei Ya's disclosed ASPO of Rmb65.8 in 1H18 for the company as a whole, the Central China performance was 15.2% higher. However, according to Zhou Hei Ya's investors relations department (see p.7 of our March 1 report), "the Central China ASPO do (*sic*) not have big difference from other areas". Our March 1 report contains detailed analysis and calculations based on our survey of Zhou Hei Ya retail stores across the region, where there are numerous under-performing shops located in Tier 3-5 cities. We are sure investors can judge whether this Rmb10 difference is a credible claim.

The "clarification" questions whether our sampling is sufficiently representative. This is totally absurd. Daily volume of a retail store is affected by many factors, and probably one of the more prominent ones is the weekend factor. As shown in p.20 of our March 1 report, the impact of weekend factor is negligible. Given our rather large sample size, our counts are sufficiently representative.

The "clarification" claims that order suspension is the reason behind a large number of consecutive "Deal Canceled" sales slips. We will show in the following pages that this explanation is an outrageous lie, and it has everything to do with our accusation that "Central China volume was exaggerated by 38.7%".

According to the "clarification":

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From time to time, the Group's sales clerks assist the customers at the check-out counter to suspend an order to allow them to shop for additional items...In peak hours, the sales clerk would normally suspend the order being processed...which allow the sales clerk to service the next customer in the long waiting line.

...Once the customer returns, the sales clerk would reactivate the suspended order and complete the sale. The sales slip would then show the number on the suspended order as an "original sale slip number".

...Some of the Group's sales clerks take advantage of this design and utilize non-peak hours to complete the cancelation process for the suspended orders generated in peak hours in bulk.

Thus, there are three relevant time points according to the "clarification", chronologically as follows:

1. When the customer first approaches the POS machine and an order is triggered (though it is soon suspended);
2. When the customer returns to finish his/her purchase; and
3. When the sales clerk has time to finalize the cancelation of the suspended order.

Exhibit 2 below shows a "Deal Canceled" sales slip and its corresponding transaction sales slip. The time stamp on the "Deal Canceled" sales slip is 13:45:02, ahead of the 17:55:16 time stamp on the corresponding transaction sales slip. All similarly paired sales slips that we have obtained show a similar pattern in their time stamps. Therefore, even if the sales clerk would "utilize non-peak hours to complete the cancelation process in bulk", the time stamp on the "Deal Canceled" sales slip must show the first time point as described above, when the customer approached the POS machine for the first time.

If the "clarification" were true, one would see **many "customers" placing orders in unbelievably high efficiency and then suspending their transactions upon hearing the promotion news from the sales clerks. Inexplicably, they then have to linger around for hours or even overnight before they are able to make up their mind and buy more. We can only imagine that these are phantom "customers"**. What a horror movie the company is presenting to us!

Below, we will illustrate the process as described in Zhou Hei Ya's "clarification" with the sales slips from one of its railway stores in Changsha, Hunan province. There are two POS machines at this store, and we will show you 300 sales slips from this store to prove Zhou Hei Ya is simply lying through its teeth!

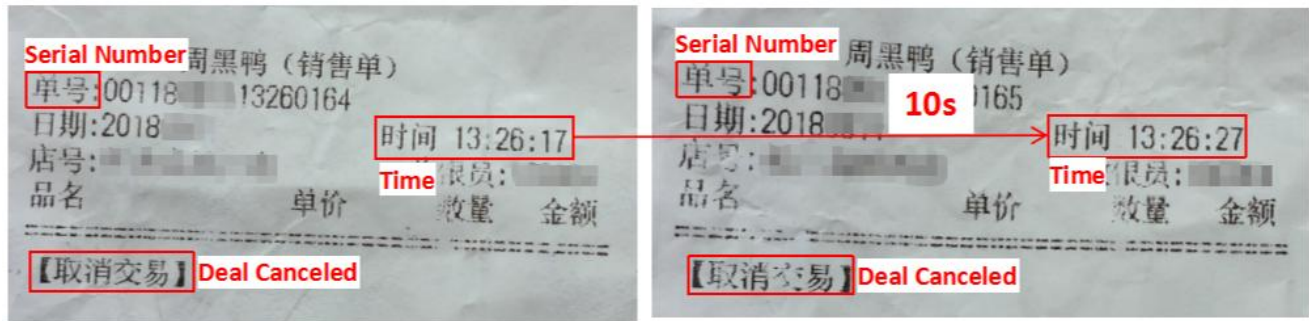
➤ Large numbers of consecutive orders at 13-second intervals

In [Appendix I: Consecutive "Deal Canceled"](#), we present the longest series of consecutive "Deal Canceled" sales slips from each of these two POS machines. POS machine No.1 generated 36 consecutive "Deal Canceled" sales slips numbered 0164-0199 from 13:26:17 to 13:34:05. How do they fit in with Zhou Hei Ya's "clarification"?

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According to the "clarification", there were 36 real but suspended transactions in those eight minutes. Let us illustrate the process with the sales slip numbered 0164. The transaction, 0164, was started at 13:26:17. Ten seconds later, at 13:26:27, the next transaction, 0165 was started, as can be seen in Exhibit 1 below.

Exhibit 1 – Transaction within 10 seconds



Source: Emerson Analytics

Here's what happened during this short period of 10 seconds:

1. Sales Clerk initiated a sales order for Customer A (13:26:17) ;
2. Customer A placed an order;
3. Sales Clerk input Customer A's order into the POS machine;
4. Sales Clerk noted that Customer A's order was not sufficient to enjoy the price break promotion and advised Customer A of the details of the promotion;
5. Customer A said he/she would need some time to consider amending the purchase;
6. Customer A stepped aside to allow the next person, Customer B, to approach Sales Clerk;
7. Sales Clerk suspended the transaction of Customer A;
8. Sales clerk initiated a new sales order for Customer B (13:26:27) .

Clearly, Sales Clerk and Customer A were fast-talkers, fast-thinkers and fast-movers to have done all of the above in 10 seconds.

Amazingly, Customer A was not alone: 34 other "customers" swamped the shop right behind him/her, doing exactly the same thing. The slowest "customer" took 35 seconds to complete the above routine, while the fastest "customer" took just eight seconds to do so. On average, they took 13 seconds to place an order and then suspend their purchase. Were they zombies on the assault?

Can you imagine three dozen customers gathering around this Zhou Hei Ya retail store, placing orders and then holding off their purchases all at the same time?

According to the "clarification", once the customer returns, the sales clerk will reactivate the suspended order and complete the sale. Clearly, this particular Sales Clerk who had been swamped by 36 customers

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was a Memory Master gifted in correctly identifying each and every one of 36 customers orders based on their appearance!

Our surveillance of the retail store shows that the POS machine No.1 registered a transaction at about 13:23. The next transaction took place at about 13:35. There was no customer during the intervening 12 minutes, and certainly no queue was formed.

➤ **"Customers" usually came back to complete purchase after an hour!**

According to the "clarification", an order suspension is done to allow the customer to decide if he/she wants to purchase additional items. And how much time does a normal person need to consider making additional purchases of some ordinary and small-ticket item? Five minutes? 10 minutes? A normal person tends to decide right away, and we observed that most of Zhou Hei Ya's customers behaved similarly. The order suspension according to the "clarification" was a rare occurrence.

In [Appendix II: Time Gap Over One Hour](#), we pair the "Deal Canceled" sales slips with their corresponding transaction sales slips and compare their time stamps. As can be seen from Appendix II, 89 "customers" returned to complete their transactions after an hour. The longest interval was four hours 10 minutes, as shown in Exhibit 2 below:

Exhibit 2 – Interval of four hours 10 minutes

The image shows two sales slips from Zhou Hei Ya. The left slip is a "Deal Canceled" receipt with a time stamp of 13:45:02. The right slip is a completed receipt with a time stamp of 17:55:16. A red arrow points from the "Deal Canceled" slip to the completed slip, indicating a time gap of four hours and ten minutes.

Serial Number	黑鸭 (销售单)		
单号: 00118	17550302		
原单号: 00118	13450219		
Original Serial Number			
店号:	Time 收银:		
品名	单价	数量	金额
小购物袋	0.1	1.0	0.1
卤鸭锁骨【大盒】	25.0	1.0	25.0
卤鸭脖【大盒】	36.0	1.0	36.0
应收合计:61.1			
折扣:0.1			
实收合计:61.00			

Source: Emerson Analytics

Analyzing these sales slips in line with Zhou Hei Ya's "clarification", one is supposed to believe that when their customers are advised of a price break promotion while making a purchase, nearly half of them will disappear for more than an hour before coming back with a new instruction. We can only imagine that they are phantom "customers".

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➤ Flood of "Deal Canceled" sales slips after stock-taking

But the farce did not stop with these elusive zombies. Our investigators saw that the sales clerks diligently printed out numerous "Deal Canceled" sales slips right after completing stock-taking for the day, and we have 71 such sales slips to prove it, as can be seen in [Appendix III: "Deal Canceled" Next Day](#).

Exhibit 3 below shows the first sales slip printed from POS machine No.1 after stock-taking was completed on the night. As we have explained in p.9 of our March 1 report, the long serial number is made up of the POS number, date, time and finally the order number (last four digits). We can therefore see that this particular sales slip was printed at 20:12 that night. The order number 0001 indicates that it was treated as the first order of the next day.

Exhibit 3 – First sales slip after stock-taking



Source: Emerson Analytics

These 71 sales slips suggest that the "customers" could only be phantom.

- Normally, there are few customers just before closing time when stock-taking of the day takes place. It is unlikely for any shop to see much business at this time;
- Before these 71 "Deal Canceled" sales slips were printed out, there must have been a series of activities involving order placing, suspension and returning to buy as the "clarification" says. But how could all this happen at the closing time?

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- For the sales clerk to diligently print out a large number of "Deal Canceled" sales slips right after he/she has completed stock-taking, when did he/she receive those "customers"?
- Such suspended transactions were actually reactivated the next day, which means "customers" had to linger around for the night before coming back to complete the transactions the next day.

Our analysis above, supported by hundreds of sales slips, proves that Zhou Hei Ya's order suspension story is just a shameless lie. The only purpose of this "Deal Canceled" operation is to inflate the sales volume. How dare the management come up with such a ridiculous lie with such a big hole?

Some may ask, why worry about "Deal Canceled" sales slips if Zhou Hei Ya has "clarified" that it "does not record canceled order as sales"? Well, we have shown clearly, in our March 1 report and further in this report, that there is an elaborate and extensive effort to create "Deal Canceled" sales slips out of thin air, and the order suspension is a totally illogical cover-up. Why would its claim of not recording canceled order as sales be credible?

As always, we have passed on the relevant evidence to the Securities and Futures Commission. We look forward to SFC's investigations into Zhou Hei Ya in order to safeguard the reputation of the Hong Kong capital markets.

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.

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