



GLAUCUS RESEARCH GROUP

格勞克斯研究

"Things gained through unjust fraud are never secure."

- Sophocles

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COMPANY: China Lumena New Materials Corp. | HK: 0067
INDUSTRY: Chemicals

Recommendation:
Strong Sell

Price:

HKD: 1.36

As of Market Close 3/24/2014

Market Cap:

HKD 7.6 billion

Public Float:

3.7 billion shares

Daily Volume:

24.6 mm shares
(Avg. 10 days)

Auditor:

BDO Limited

Price Target:

HKD: 0.00

CHINA LUMENA NEW MATERIALS CORP ("Lumena" or the "Company") produces and sells thenardite and polyphenylene sulfide ("PPS") products in China. We believe that Lumena has made numerous material misrepresentations to investors and the Hong Kong Stock Exchange ("HKEX"), both in its 2009 IPO prospectus and in subsequent financial statements. In this report we present publicly available tax records and stamped hard copies of SAIC filings which, in our opinion, indicate that Lumena's sales are 90% less than the sales reported to investors and regulators in the Company's Hong Kong filings.

PPS

- PPS Sales and Profitability 90% Less than Reported.** According to Lumena's HKEX filings, its operating subsidiary, Deyang Chemical, accounted for ~72% of its PPS revenues in FYs 2011 and 2012. Yet Deyang Chemical's SAIC filings show that its revenues were only **RMB 189mm** (90% less than reported by Lumena) and **RMB 181mm** (91% less than reported by Lumena) in FYs 2011 and 2012, respectively. SAIC filings also show that contrary to being a profitable enterprise, Deyang Chemical **barely broke a profit before taxes**. This suggests Lumena has been vastly overstating the size and profitability of its primary business segment.
- Deyang Tax Records Undermine Reported PPS Earnings.** A ranking of top taxpaying businesses for 2011 published by the [city of Deyang](#) shows that Lumena's other PPS operating subsidiary, Deyang Materials, is ranked **74th**, which is 58 spots behind a publicly listed company which reported less than RMB 89mm in total taxes paid in 2011 (VAT and income taxes). This means that Deyang Materials paid far less than RMB 89mm in taxes in 2011, even though we estimate that it should have paid over RMB 378mm in taxes in 2011 (VAT and income taxes) for Lumena's reported PPS financials to be true.

THENARDITE

- SAIC Filings of Largest Customer Suggest Fabricated Sales.** Chengdu Yijing, Lumena's largest customer, reportedly purchased RMB 339mm and RMB 443mm of products from the Company in 2009 and 2010, respectively. Yet SAIC filings show that Chengdu Yijing's total cost of goods sold (the amount it purchased from its suppliers) was RMB 37mm and RMB 35mm in 2009 and 2010, respectively, indicating that Lumena's actual sales were **90% less than** Lumena's reported figures.
- Hard Copies of SAIC Filings Suggest Doctored Financials.** In 2010, Lumena had only two operating subsidiaries, both of which sold thenardite products. According to Lumena's HKEX filings, these subsidiaries reportedly generated RMB 2.0 billion in combined revenues and RMB 1.1 billion in combined profits in 2010. Yet SAIC filings for both entities show combined revenues of **only RMB 151mm** (7.7% of reported by Lumena) and **no net profits!**

5. **Is China Really So Constipated?** Lumena claims to sell ~300,000 tons of medical thenardite, primarily used as a laxative, every year. If this is true, we estimate that Lumena would have to sell an average of 30 doses of medical thenardite ever year **to every human being in China over the age of 14**. This simply defies credibility.
6. **Hidden Beneficiary to Suspicious Transaction?** In 2005, Lumena's former Chairman sold an equity stake in a subsidiary to a supposedly independent third party only to buy back the same equity four years later, immediately after going public in 2009, with cash raised from the capital markets, for 3100% percent more than the price at which the former Chairman sold it. Such returns appear too good to be true, raising our suspicions that perhaps an insider was the hidden beneficiary of the transaction.

GLOBAL

7. **Lucrative Commodity Business Too Good to be True.** Lumena's reported EBIT margin of 56% (average 2008-2012) defies credibility when we consider that other large-scale public companies selling thenardite and PPS report EBIT margins of between 5% and 10%. Indeed, Lumena reports similar EBIT margins as Mastercard (NYSE: MA). This does not pass the smell test.
8. **Valuation.** As of June 30, 2013, Lumena had approximately **RMB 4.2 billion** of onshore (PRC) bank debt outstanding and another USD 120 million of convertible bonds due **May 12, 2014** (with an effective interest rate of 25.97%), which we believe Lumena must either restructure or issue over 1 billion shares in new equity in order to pay off. In a liquidation scenario, the holders of onshore liabilities have historically taken priority over offshore equity holders. Because we believe that the Company has significantly overstated its sales and profitability, we doubt the authenticity of its reported receivables, cash balance and PP&E. Given the limited offshore assets available for seizure and the difficulty recovering onshore assets (property and equipment) under China's byzantine judicial system, we have a price target on its shares of **HKD 0.00**.

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We are short sellers. We are biased. So are long investors. So is Lumena. So are the banks that raised money for the Company. If you are invested (either long or short) in Lumena, so are you. Just because we are biased does not mean that we are wrong. We, like everyone else, are entitled to our opinions and to the right to express such opinions in a public forum. We believe that the publication of our opinions about the public companies we research is in the public interest.

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CIRCLING THE DRAIN

CHINA LUMENA NEW MATERIALS CORP. (“Lumena” or the “Company”) mines, processes and sells thenardite for use as medical thenardite (a laxative and anti-inflammatory agent) and powder thenardite (in detergents and textiles). Lumena also produces and sells polyphenylene sulfide (“PPS”), a plastic for industrial use.

Lumena appears to be circling the drain. The Company’s balance sheet is weighed down by RMB 4 billion in current liabilities and **RMB 3 billion in long-term liabilities**. As stated in the Company’s 2013 interim report, Lumena must pay a 19.3% yield to maturity on USD 120 million convertible bonds issued by CITIC and CIC (**with an effective interest rate of 25.97%**), which are **due in May 2014 (45 days from today)**. If Lumena had the available cash that it claims, we believe that it would not have issued debt at such a punitive interest rate. Accordingly, we believe that Lumena must either restructure its 2014 bonds or be forced to issue over 1 billion shares of new equity to pay them off, either of which may prove impossible with financial statements so littered with red flags.



An Imminent Refinancing?

The Company reports similar EBIT margins (56%) from the **mining and manufacturing of two commodities as Mastercard!** Lumena’s reported EBIT margins are five to ten times higher than the margins reported by competitors mining the same commodity (thenardite) and producing the same plastic (PPS). Despite supposedly generating significant cash flow from operations, since going public in 2009 Lumena has been a serial capital raiser.

There is a significant amount of evidence, including publicly available SAIC filings and government tax rankings to suggest both Lumena’s PPS and thenardite businesses are much smaller and less profitable than Lumena claims in its public filings. Even a basic sanity check of Lumena’s financials reveals problems. Lumena claims to sell 300,000 tons of medical thenardite every year, which we estimate is the equivalent of 30 doses of medical thenardite, used primarily as a laxative, to every person over 14 years old in China every year – this seems *prima facie* absurd (and unintentionally humorous).

We believe that Lumena has made numerous material misrepresentations to investors and the Hong Kong Stock Exchange (“HKEX”), both in its 2009 IPO prospectus and in subsequent financial statements regarding the scale of its revenues, earnings, and assets.

We doubt that Lumena will be able to refinance its convertible bonds, due May 12, 2014, at a rate that is not punitive. Indeed, Moody’s [withdrew](#) its B2 corporate rating on Lumena in December 2013, suggesting, in our opinion, that it is simply a matter of time before Lumena implodes.

PPS BUSINESS

In December 2010, in conjunction an equity issuance, Lumena [announced the acquisition](#) of Sino Polymer New Materials Co., Ltd. (“[Sino Polymer](#)”) from a consortium of shareholders including Lumena’s former Chairman (a 38% owner of the target).

Sino Polymer produces polyphenylene sulfide, a crystalline aromatic polymer, used as a substitute for metal, primarily in automobiles, electronics and filter bags. PPS resin (together with fibers and compounds produced from the resin) competes with a number of other thermoplastics (PCT and PBT), nylons, epoxies and metals for use in a variety of industrial applications.

While demand for PPS has been flat or declining in the US and the EU since 2008, demand in China has supposedly risen. According to the Company, China accounts for almost 70% of global PPS demand. Lumena claimed that Sino Polymer was the largest PPS resin producer (by capacity) as of December 31, 2009, supposedly accounting for 30% of the world’s total production and **99.7% of the PRC’s total production capacity**.¹

Sino Polymer, a BVI shell company, held the equity interests of three operating subsidiaries:

- Sichuan Deyang Chemical Co., Ltd. 四川得陽化學有限公司 (“[Deyang Chemical](#)”), incorporated in April 2006;
- Sichuan Deyang Special New Materials Co., Ltd.* 四川得陽特種新材料有限公司 (“[Deyang Materials](#)”), incorporated in June 2007; and
- Sichuan Deyang Engineering Plastic Development Co., Ltd.* 四川得陽工程塑料開發有限公司 (“[Deyang Plastics](#)”), incorporated in March 2008 (not operational).

The growth trajectory of Sino Polymer was equal parts swift and suspicious. In three years **from inception**, Sino Polymer cornered the Chinese market to supposedly become, for all intents and purposes, the **sole producer of PPS resin in the PRC**.² Indeed, at the time of the acquisition, Lumena announced that it was unlikely to face a domestic competitor.

It is also of note that according to Lumena, Sino Polymer’s competitive moat was not derived from **intellectual property (it had only two patents), but rather**, its “technical know-how derived from industry experience, research and development, and recent experience with the expansion of [Sino Polymer’s] production capacity.”³

Put simply, in three years, Sino Polymer built an absolute domestic monopoly in a commoditized product with, it appears, limited intellectual property rights. Suspicious yet?

¹ Company Circular, December 14, 2010, p. 44. (<http://www.lumena.hk/eng/ir/documents/008.pdf>)

² Company Circular, December 14, 2010, p. 24. (<http://www.lumena.hk/eng/ir/documents/008.pdf>)

³ Company Circular, December 14, 2010, p. 48. (<http://www.lumena.hk/eng/ir/documents/008.pdf>)

PPS SALES AND PROFITABILITY LESS THAN REPORTED

Since inception, PPS production capacity was concentrated at two primary subsidiaries, Deyang Materials and Deyang Chemical. Although both production facilities produce PPS Resin, Deyang Chemical produces PPS **Compounds** while Deyang Materials produces PPS Fiber.

Lumena's Reported PPS Production Capacity

Figures are in metric tons per annum

	Location	PPS Product Types	2010	2011	2012
Deyang Materials	Deyang City, Sichuan	Resin	24,000	24,000	24,000
		Fiber	5,000	5,000	5,000
Deyang Chemical	Chengdu City, Sichuan	Resin	6,000	6,000	6,000
		Compounds	30,000	30,000	30,000
Deyang Engineering Plastic	-	<i>Not Operational</i>	-	-	-

Source: December 2010 Company Circular (pg. 50-51); Company Annual Reports

According to Lumena, Deyang Plastics was not engaged in any substantial business activities since inception.⁴ Despite the fact that production capacity appears evenly divided between the other two subsidiaries, Deyang Chemical produces PPS Compounds, which account for roughly 70% of the total revenue generated by the PPS business.

Lumena's Reported PPS Revenue by Product Type and Subsidiary

	Subsidiary	2007	2008	2009	2010**	2011	2012
PPS Resin*	Deyang Chemical	7%	5%	3%	2%	3%	3%
	Deyang Materials	27%	19%	11%	9%	12%	14%
	TOTAL	34%	24%	14%	11%	15%	17%
PPS Compounds	Deyang Chemical	64%	56%	64%	72%	69%	68%
PPS Fiber	Deyang Materials	2%	19%	22%	17%	16%	15%

Subsidiary as a % of PPS Revenue

Deyang Chemical	71%	61%	67%	74%	72%	71%
Deyang Material	29%	38%	33%	26%	28%	29%

Source: December 2010 Company Circular (pg. 45); Company Annual Reports; Glaucus Calculations

* From Production Capacity Chart, we know that Deyang Chemicals produces 20% of Resin and Deyang Materials produces 80% of Resin

** Estimated based on first half of 2010

Given that Lumena's PPS business purportedly generated RMB **2.54 billion** in revenues in FY 2011, Deyang Chemical should have therefore accounted for around **1.825 billion** (72% of PPS revenues).

Yet SAIC filings for Deyang Chemical, which contain FY 2011 financial statements, state that the operating subsidiary's revenue was only **RMB 189 million**, roughly **90% less than the sales reported in the Company's reported financials**.

⁴ Company Circular, December 14, 2010, p. 42. (<http://www.lumena.hk/eng/ir/documents/008.pdf>).

Profit and Profit Distribution Table

Name of enterprise:
Sichuan Deyang Chemical Co., Ltd.

利润及利润分配表

		Year 2011			会年企02表		
编制单位: 四川德阳化学有限公司		Last Year	This Year	2011年度	单位: 元 Unit: Yuan		
行次	项目	上年实际数	本年实际数	备注	行次	上年实际数	本年实际数
一	一、主营业务收入 Sales	178,972,484.93	189,214,241.66	其中: 处置固定资产净收入	33		
	其中: 出口产品(商品)销售收入			处置无形资产损失	34		
	进口产品(商品)销售收入			罚款支出	35		
	减: 折扣与折让			捐赠支出	36		
二	二、主营业务收入净额	178,972,484.93	189,214,241.66	(一) 其他支出	37		
	减: (一) 主营业务成本	102,263,365.50	105,973,163.00	其中: 结转的营业外支出(损失)	38		
	其中: 出口产品(商品)销售成本			五、利润总额 Profit Before Income Tax	39	37,099,327.86	38,032,062.57
	(二) 主营业务税金及附加	984,360.62	1,818.50	减: 所得税	40	4,637,415.98	4,754,007.82
	(三) 销售费用			少数股东损益	41		
	(四) 其他			加: 未确认的投资损失(以“-”号填列)	42		
	加: (一) 递延收益			六、净利润 Net Profit	43	32,461,911.88	33,278,054.75
	(二) 投资收益收入			加: (一) 年初未分配利润	44	349,036,565.76	192,849,146.45
	(三) 其他			(二) 盈余公积补亏	45		
三	三、主营业务利润(Gross Profit) 利	76,724,738.81	83,239,260.16	(三) 其他调整因素	46		
	加: 其他业务利润(亏损以“-”号填列)	6,977,533.15	3,435,685.75	七、可供分配的利润	47	382,068,477.64	226,127,201.20
	减: (一) 营业费用	4,115,261.08	5,903,091.09	减: (一) 准备用过的利润	48		
	(二) 管理费用	27,031,803.44	19,194,995.78	(二) 补充流动资本	49		
	(三) 财务费用	14,217,058.47	23,626,770.55	(三) 提取法定盈余公积	50	3,246,191.19	3,327,805.46
	(四) 其他			(四) 提取法定公益金	51		
四	四、营业利润 Operating Profit	37,338,148.97	37,952,088.48	(五) 提取职工奖励及福利基金	52		
	加: (一) 投资收益(损失以“-”号填列)			(六) 提取储备基金	53		
	(二) 利息收入			(七) 提取企业发展基金	54		
	(三) 补贴收入			(八) 利润归还投资	55		
	其中: 非流动资产处置净收入			(九) 其他	56		
	(四) 营业外收入	68,432.43	92,609.08	八、可供投资者分配的利润	57	378,822,286.45	222,799,395.72
	其中: 处置固定资产净收益			减: (一) 应付优先股股利	58		
	非货币性交易收益			(二) 提取任意盈余公积	59		
	出售无形资产收益			(三) 应付普通股股利	60		
	罚款净收入			(四) 转作资本(股本)的普通股股利	61		
	(五) 其他			(五) 其他	62	185,373,140.00	
	其中: 以前年度会计差错补利回			九、未分配利润	63	192,849,146.45	222,799,395.72
	减: (一) 营业外支出	307,253.54	12,635.00	其中: 应由以后年度损益补的亏损(以“-”号填列)	64		

注: 表中带*科目为合并会计报表专用, 带*的科目由执行新《企业会计准则》的企业填列。

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2011 Deyang Chemical SAIC Filings

Not only do FY 2011 financial statements in Deyang Chemical's SAIC filings indicate that the operating subsidiaries total sales were **90% less than reported**, but SAIC records also show that the operating subsidiary had a **pre-tax profit of only RMB 38 million**. SAIC Filings for FY 2012 tell a similar story.

Profit and Profit Distribution Table
利润及利润分配表

Name of enterprise: Sichuan Deyang Chemical Co., Ltd. Unit: Yuan

		Last Year	This Year	Year 2012	Last Year	This Year
1	营业收入 (Sales)	189,214,241.66	180,676,553.24			
2	营业成本					
3	营业税金及附加					
4	销售费用					
5	管理费用	189,214,241.66	180,676,553.24			
6	财务费用	105,973,163.00	106,154,533.16			
7	资产减值损失				38,032,062.57	20,110,700.36
8	公允价值变动损益					
9	投资收益	1,818.50	1,599,760.47		4,754,007.62	2,513,437.45
10	营业外收入					
11	营业外支出					
12	利润总额 (Profit Before Income Tax)					
13	所得税费用					
14	净利润 (Net Profit)				33,278,054.75	17,596,862.81
15	归属于母公司所有者的净利润				33,278,054.75	17,596,862.81
16	少数股东损益					
17	其他综合收益					
18	综合收益总额					
19	归属于母公司所有者的综合收益总额					
20	归属于少数股东的综合收益总额					
21	所有者权益合计					
22	实收资本					
23	资本公积					
24	盈余公积					
25	未分配利润					
26	所有者权益合计					
27	负债合计					
28	短期借款					
29	应付账款					
30	预收账款					
31	应付职工薪酬					
32	应交税费					
33	其他应付款					
34	长期借款					
35	应付债券					
36	长期应付款					
37	专项应付款					
38	其他非流动负债					
39	流动负债合计					
40	非流动负债合计					
41	负债合计					
42	所有者权益合计					
43	负债和所有者权益合计					

2012 Deyang Chemical SAIC Filings

Lumena's PPS business purportedly generated **RMB 2.93 billion** in revenues in FY 2012. Deyang Chemical should have therefore accounted for around **RMB 2.08 billion** (71% of PPS revenues). Yet 2012 SAIC filings for Deyang Chemical state that the operating subsidiary's revenue was only **RMB 181 million**, again roughly **90% less than the sales reported in the Company's Hong Kong financials**. In addition, 2012 SAIC filings show that after tax profit declined by **47% from 2011 to 2012**.

Deyang Chemical: Disparity between SAIC Filings and Reported Financials

Figures are in RMBmm	2011			2012		
	Revenues	Gross Profit	Profit Before Income Tax	Revenues	Gross Profit	Profit Before Income Tax
Hong Kong Financials*	1,825	1,159	690	2,082	1,249	785
SAIC Filings	189	83	38	181	73	20
% Difference	90%	93%	94%	91%	94%	97%

*Deyang Chemical HK Financials Estimate: 72% of the Total Revenue of Lumena's PPS Business in 2011 (71% in 2012); Gross Profit estimated based on the gross profit margin for Lumens'a consolidated operations (63.5% in 2011, 60% in 2012); Profit Before Income Tax estimated based on profit before income tax margin for Lumena's consolidated operations (37.8% in 2011; 37.7% in 2012).

The SAIC Filings suggests that not only is Lumena fabricating PPS revenue, but that the Company overpaid for the **RMB 10 billion acquisition of the PPS business from the former Chairman and other shareholders in 2011**.

TAX RECORDS UNDERMINE REPORTED PPS SALES

Is it possible that Lumena's other PPS manufacturing subsidiary, Deyang Materials, accounted for almost all of Lumena's PPS revenue and profitability? We do not think so. Publicly available government tax records suggest that Deyang Materials is nowhere close to generating the revenues or profits necessary to account for reported Lumena's PPS figures.

The Sichuan Deyang local taxation bureau publishes an annual ranking, [available to any investor online](#), which details the taxes paid by businesses operating in Deyang. If Deyang Materials accounted for the remaining RMB 2.35 billion in sales for Lumena's PPS business in 2011, it would have paid at least RMB 241mm in VAT and RMB 137mm in income taxes (total of RMB 378mm in taxes).⁵

If Deyang Materials was paying RMB 378mm in income taxes and VAT, then it would certainly appear highly ranked on the Deyang city rankings of top taxpaying companies in 2011. It is not. Rather, it is ranked 74th.

To give investors some context, the 16th ranked company on the 2011 tax list (see next page) is Sichuan Jinlu Resin Co. Ltd. ("[Sichuan Jinlu Resin](#)") a subsidiary of the Sichuan Jinlu Group, a Shenzhen listed company (SHE: 000510) ("[Sichuan Jinlu Group](#)"). According to the 2011 annual report of the Sichuan Jinlu Group, **the entire group paid only RMB 89.7mm** in total taxes in 2011:

Consolidated Statement of Cash Flows

Name of Enterprise: 合并现金流量表		2011 年度	Year 2011	单位: 人民币元	Unit: RMB
编制单位: 四川金路集团股份有限公司					
项 目	附注	本金额	上年金额		
		This Year	Last Year		
一、经营活动产生的现金流量:					
销售商品、提供劳务收到的现金		2,922,068,804.53	2,802,436,527.37		
客户存款和同业存放款项净增加额					
向中央银行借款净增加额					
向其他金融机构拆入资金净增加额					
支付利息、手续费及佣金的现金					
支付保单红利的现金					
支付给职工以及为职工支付的现金		130,313,800.85	151,025,498.80		
支付的各项税费 All types of taxes paid		89,705,436.76	72,715,585.08		
支付其他与经营活动有关的现金	八、44 (2)	68,976,131.80	81,486,099.77		
经营活动现金流出小计		2,983,569,423.57	2,573,959,904.68		

Source: Page 143-144 of the 2011AR, http://pg.irj.com.cn/acc/CN_DISC/STOCK_TIME/2012/04/12/000510_nb_60817301.PDF

⁵ We know from SAIC filings that Deyang Chemical only accounted for RMB 83mm in gross profit in FY 2011. For Lumena's reported financials to be true, Deyang Materials would have had to generate RMB 1.415 billion in gross profit that year (RMB 2.535 billion in PPS segment revenues * 59.1% reported segment margin less 83mm gross profit for Deyang Chemical). Therefore, we can estimate that Deyang Materials paid RMB 241 mm in VAT (RMB 1.415 billion gross profit times 17% VAT) and RMB 137 in income tax (RMB 954mm of PPS segment before tax profit less RMB 38mm Deyang Chemical before tax profit from SAIC filing times Deyang Materials' reported 15% effective income tax rate).

If Sichuan Jinlu Group (the conglomerate) paid RMB 89.7mm in taxes in 2011, then its Deyang city subsidiary, Sichuan Jinlu Resin, must have only paid a fraction of that amount. Yet Sichuan Jinlu Resin appears as the 16th highest taxpayer on the Deyang city taxpayer list for 2011, which is **58 places ahead of Deyang Materials**:

The screenshot shows the official website of the Sichuan Deyang Local Taxation Bureau. The main content area displays a notice regarding the ranking of the top 100 tax-paying enterprises in Deyang City for the year 2011. The notice is dated March 30, 2012, and includes a list of the top 100 companies. The 16th company on the list is Sichuan Jinlu Resin Co., Ltd. The 74th company is Sichuan Deyang Special New Materials Co., Ltd.

四川省德阳市地方税务局
Sichuan Deyang Local Taxation Bureau

德阳市人民政府关于发布德阳市2011年度纳税百强企业排行榜的通知

德府发〔2012〕48号

各县（市、区）政府、德阳经济技术开发区管委会，市级各部门：

近年来，在市委、市政府的正确领导下，德阳经济保持了持续、快速、健康的发展势头，经济结构不断优化，企业规模日益壮大，效益明显提高，涌现了一大批纳税贡献突出的骨干企业，促进了财政收入持续快速增长，为德阳经济社会发展和民生改善奠定了坚实的财力基础。在全国第21个税收宣传月来临之际，市政府决定发布德阳市2011年度纳税百强企业排行榜，彰显纳税百强企业对国家和社会的贡献，激励全市广大纳税人一如既往地依法诚信纳税、积极纳税护税，共同营造良好的发展环境，希望入围德阳市2011年度纳税百强企业的企业再接再厉，再接再厉，发挥好排头兵作用，全市广大纳税人要以纳税百强企业为榜样，守法经营、诚信纳税，为德阳争当四川科学发展排头兵，加快建设中国西部经济文化强市作出新的、更大的贡献！

附件：德阳市2011年度纳税百强企业排行榜

Ranking of the Top 100 Tax Paying Enterprises in Deyang City for Year 2011
March 30, 2012
二〇一二年三月三十日

德阳市 2011 年度纳税百强企业名称

The Top 100 Tax Paying Enterprises in Deyang City for Year 2011

- 1 四川旭光工业有限责任公司
- 2 东方电气集团东方汽轮机有限公司
- 3 东方电气集团东方电机有限公司
- 4 四川绵竹剑南春酒厂有限公司
- 5 二重集团（德阳）重型装备股份有限公司
- 6 四川宏达实业有限公司
- 7 四川剑南春（集团）有限责任公司
- 8 四川省烟草公司德阳市公司
- 9 德阳银行股份有限公司
- 10 四川汇金源有限公司
- 11 华蜀烟花啤酒（德阳）有限责任公司
- 12 四川宏华石油设备有限公司
- 13 中国石油化工股份有限公司西南油气分公司川西采气厂
- 14 四川英杰电气股份有限公司
- 15 绵竹市天益酒业有限公司
- 16 四川省金路树脂有限公司 **Sichuan Jinlu Resin Co., Ltd.**
- 17 四川蜀中制药有限公司
- 73 中国银行股份有限公司德阳分行
- 74 四川德阳特种新材料有限公司 **Sichuan Deyang Special New Materials Co., Ltd.**
- 75 中国石化集团西南石油高寒二物探大队
- 76 四川华仪电器有限公司
- 77 四川广汉恒丰实业房地产开发有限公司
- 78 四川旭光工业有限责任公司剑南春酒厂
- 79 四川隆泰制药有限公司
- 80 中国建设银行股份有限公司德阳分行
- 81 四川省烟草公司德阳市什邡营销部
- 82 德阳市汇友商贸有限公司
- 83 中国人民财产保险股份有限公司德阳市分公司

Source: <http://www.dyltax.gov.cn/?tag=gonggao&id=1385>

If Deyang Materials accounted for the supposed remaining gross profit and earnings before taxes of Lumena's PPS business in 2011 (RMB 1.415 billion in gross profit, RMB 916mm in earnings before taxes), then it would have paid RMB 378mm in taxes that year (including both income taxes and VAT). Yet Deyang Materials appears 74th on Deyang city's rankings of top taxpaying businesses, **58 spots below** a publicly listed subsidiary that we know paid less than **89mm** in 2011. This is further evidence suggesting that Lumena's PPS does not generate the revenues or profitability that Lumena reports to Hong Kong investors.

THENARDITE BUSINESS

SAIC FILINGS OF LARGEST CUSTOMER SUGGEST FABRICATED SALES

Financial statements contained in the SAIC filings of Lumena's largest customer shows that the customer purchased far less thenardite than Lumena claims to have sold to it.

At the time of its August 2009 IPO, Lumena claimed that Chengdu Yijing Trading Chemical Engineering Co., Ltd. ("Chengdu Yijing"), was its largest customer, accounting for 7.7%, 18.1% and 23.2% of the Company's total revenues in the years ended December 31, 2006, 2007 and 2008 respectively.⁶ According to Lumena's prospectus, Chengdu Yijing sold the powder thenardite and specialty thenardite it purchased from the Company to Proctor & Gamble for use in the multinational's detergent products.⁷

We have many reasons to believe that Chengdu Yijing remained Lumena's largest customer in the two fiscal years following its IPO. First, on August 1, 2008, Lumena entered into a new three-year sales contract with Chengdu Yijing through which the customer allegedly agreed to purchase between 5,000 and 10,000 tonnes of powder thenardite **per month** from Lumena at a fixed price.⁸

Second, sell side analysts with access to management confirmed that Chengdu Yijing remained Lumena's largest customer in 2009 and 2010.⁹ Third, Lumena CEO Zhang Daming stated in 2009 that over 20% of the Company's revenue came from sales to Proctor & Gamble, which purchases thenardite through Chengdu Yijing.¹⁰ Fourth, descriptions of the Company confirm that Chengdu Yijing is Lumena's largest customer.¹¹

If, as we have every reason to believe, Chengdu Yijing remained Lumena's top customer in the two fiscal years following the Company's IPO, Lumena supposedly sold Chengdu Yijing 339mm and 443mm of thenardite 2009 and 2010, respectively. Chengdu Yijing's SAIC filings should therefore confirm this level of purchasing activity.

Yet SAIC filings state that Chengdu Yijing's total cost of goods sold (the amount it purchased from its suppliers) was 37mm and 35mm in 2009 and 2010, respectively, **which is 90% less than the amount Lumena claims to have sold to Chengdu Yijing in those years.**

Below we have included excerpts from Chengdu Yijing's 2009 and 2010 SAIC filings showing its cost of goods sold as well as changes to its inventory balance, which together, give investors a picture of the customer's limited purchasing activity.

According to 2009 SAIC filings, Chengdu Yijing reported **RMB 37 million in COGS** and a **decrease** in inventory of RMB 1 million, indicating that it purchased significantly less than the RMB 336 million that Lumena claimed to have sold to it in 2009.

⁶ IPO Prospectus, pg. 121 (<http://www.lumena.hk/eng/ir/prospectus.pdf>)

⁷ IPO Prospectus, pg. 122 (<http://www.lumena.hk/eng/ir/prospectus.pdf>)

⁸ IPO Prospectus, pg. 122 (<http://www.lumena.hk/eng/ir/prospectus.pdf>)

⁹ http://www.cpy.com.hk/CPY/library/database/research_docs/20100723006744590501.pdf

¹⁰ http://www.mpfinance.com/htm/Finance/20090530/ab/ab_ebd1.htm

¹¹ http://cn.reuters.com/article/vbc_rt_interviews/idCNnCH006029320100914

Chengdu Yijing Trading Chemical Engineering Co., Ltd. Balance Sheet

资产负债表

Unit: Yuan

编制单位: 成都艺锦化工有限公司

报表所属日期: 2009-12-31 12/31/2009

单位: 元

资产	行次	年初数	期末数	负债及所有者权益	行次	年初数	期末数
流动资产:		Beginning of Year	End of Year	流动负债:			
货币资金	1	2,498,298.79	1,276,470.78	短期借款	30	4,580,000.00	3,220,000.00
短期投资	2			应付票据	31		
应收票据	3			应付账款	32	-1,556,357.55	-1,574,527.65
应收账款	4	2,798,240.08	5,838,331.43	预收账款	33		
坏账准备	5	13,531.20		其他应付款	34	-329,874.94	-178,656.50
应收账款净额 (4-5)	6	2,692,708.88	5,838,331.43	应付工资	35		
预付账款	7			应付福利费	36		
应收补贴款	8			未交税金	37	228,584.77	287,108.57
其他应收款	9	15,817.00	91,300.00	未付利润	38		
存货	10	1,717,226.75	759,509.66	其他未交款	39	147,129.55	143,630.15
待摊费用	11			预提费用	40		
待处理流动资产净损失	12			一年内到期的长期负债	41		
一年内到期的长期债券投资	13			其他流动负债	42		
其他流动资产	14						

Chengdu Yijing Trading Chemical Engineering Co., Ltd. Income Statement

损益表

Unit: Yuan

编制单位: 成都艺锦化工有限公司

报表所属日期:

12/2009

单位: 元

项 目	行次	本月数	本年累计数 This Year
一、主营业务收入			
减: 主营业务成本 COGS	1	5,113,736.30	71,835,742.31
营业费用	2	2,496,797.94	36,942,914.00
主营业务税金及附加	3	3,719,755.05	30,463,839.27
二、主营业务利润 (5=1-2-3-4)	4	23,490.00	378,122.31
加: 其他业务利润	5	-1,126,306.69	4,050,866.73
减: 管理费用	6		
财务费用	7	78,131.42	433,012.99
三、营业利润 (9=5+6-7-8)	8	-213,120.99	-0.43
加: 投资收益	9	-991,317.12	3,617,854.17
补贴收入	10		
营业外收入	11		
减: 营业外支出	12	5,586.40	5,586.40
加: 以前年度损益调整	13		44,640.00
四、利润总额 (15=9+10+11+12-13+14)	14		
减: 所得税	15	985,730.72	3,578,800.57
五、净利润 (17=15-16)	16	985,730.72	3,578,800.57

单位负责人:

复 核:

财会负责人:

2010 SAIC filings tell a similar story. For 2010, Chengdu Yijing reported **RMB 35 million in COGS** and an increase in inventory of RMB 1 million, indicating that it purchased significantly less than the RMB 443 million that Lumena claimed to have sold to it in 2010.

Year 2010, Balance Sheet

Chengdu Yijing Trading Chemical Engineering Co., Ltd.

Balance Sheet
资产负债表

Unit: Yuan
金额单位: 元

项 目	行次	期初余额	年末余额	项 目	行次	期初余额	年末余额
流动资产	1	↑	↑	流动负债:	47	—	—
货币资金	2	127670.78	3169963.42	短期借款	48	3220000	930000
Δ交易性金融资产	3		End of Year	Δ交易性金融负债	49		
#短期投资		Beginning of Year		#应付权证	50		
应收票据	5			应付票据	51		
应收账款	6	5898391.43	6475185.41	应付账款	52	-1574522.65	1082086
预付款项	7			预收款项	53		
应收股利	8			应付职工薪酬	54		
应收利息	9			其中: 应付工	55		
其他应收款	10	91300.8	15988.12	应付福利	56		
存货 Inventory	11	759609.66	2217994.79	应交税费	57	430638.72	642638.01
其中: 原材料	12			其中: 应交税	58	287108.57	430015.48

Year 2010, Income Statement

Chengdu Yijing Trading Chemical Engineering Co., Ltd.

Income Statement
损益表

项 目	行次	上期金额	本期金额	项 目	行次	上期金额	本期金额
一、营业总收入	1	7315848.69	7315848.69	其中: 对联营企业和合营企业的投资收益	22		
其中: 营业收入	2	7315848.69	7315848.69	营业利润 (亏损以“-”号填列)	23		3825394.89
其中: 主营业	3		7315848.69	加: 营业外收入	24		
其他业	4			其中: 非流动性资产处置利得	25		
二、营业总成本	5		69190453.8	非货币性资产交换利得 (非货币性交易收益)	26		
其中: 营业成本 COGS			34628475.25	政府补助 (补贴收入)	27		
其中: 主营业	7			债务重组利得	28		
其他业	8			减: 营业外支出	29		
营业税金及附加	9		385958.8	其中: 非流动性资产处置损失	30		
销售费用	10		32769153.81	非货币性资产交换损失 (非货币性交易损失)	31		
管理费用	11		1409556.18	债务重组损失	32		
招待费	12		283208	四、利润总额 (亏损总额以“-”号填列)	33		3825394.89
研究与开发费	13			减: 所得税费用	34		969058.47
财务费用	14		-2690.24	加: #未确认的投资损失	35		
其中: 利息	15			五、净利润 (净亏损以“-”号填列)	36		2856336.42
利息	16			减: *少数股东损益	37		
净损失 (净收益以“-”号填列)	17			六、归属于母公司所有者的净利润	38		2856336.42
Δ资产减值损失	18			七、每股收益:	39		
其他	19			基本每股收益	40		
加: 公允价值变动收益 (损失以“-”号填列)	20			稀释每股收益	41		
投资收益 (损失以“-”号填列)	21						

Chengdu Yijing: Purchasing Activity Disparity*Figures are in RMBmm*

	2006	2007	2008	2009	2010
Lumena's Reported Sales to Chengdu Yijing	16	67	266	336	443
SAIC Filing Purchasing Activity†	-	-	-	36	36
% Difference	-	-	-	89%	92%

† Purchasing Activity is calculated by adding COGS to changes in inventory

Put together, SAIC filings indicate that Chengdu Yijing, supposedly Lumena's largest customer, was purchasing **90% less** than Lumena reported in its Hong Kong filings. This is direct and powerful evidence suggesting that Lumena has vastly exaggerated its sales in communications and filings submitted to Hong Kong regulators and investors.

HARD COPIES OF SAIC FILINGS SUPPORT DEBTWIRE ALLEGATIONS

In 2010, before Lumena acquired the PPS business, it operated exclusively through two subsidiaries, Sichuan Chuanmei Mirabilite Co., Ltd. 四川省川眉芒硝有限責任公司 and Sichuan Chuanmei Special Glauber Salt Co., Ltd. 四川川眉特種芒硝有限公司 (collectively, the “Thenardite Operating Subs”), both of which mined and sold thenardite products.¹²

Lumena’s thenardite business has been beset by controversy. In August 2011, an article published by Debtwire and reprinted by the Financial Times (available [here](#)) reported that electronic copies of Lumena’s 2008 and 2009 SAIC filings, apparently sourced from three different credit agencies in China, indicated that contrary to what Lumena was telling investors, the Company’s only two operating **subsidiaries were unprofitable**. Debtwire further reported that Lumena’s reported sales were 8x to 15x larger than the consolidated sales figures in the 2008 and 2009 SAIC filings that Debtwire obtained.

Lumena responded that *electronic depository files – including screenshots with the same exact time stamp – could not be relied upon because they were electronic records and not hard-copy SAIC filings, which bear the official stamp*. Lumena showed Debtwire hard copies of SAIC filings which, according to Lumena, vindicated the Company. Suspiciously, Lumena refused to let Debtwire keep copies of the hard-copy SAIC filings so the market was never in a position to truly evaluate the credibility of the evidence. What was Lumena hiding? Why not simply publish the original hard copies with official stamps?

Taking Lumena’s arguments at face value, we obtained hard copies of SAIC filings for the same operating subsidiaries, both of which bear the official stamp. The hard copies that we obtained confirmed Debtwire’s allegations.



According to its Hong Kong financials, Lumena’s Thenardite Operating Subs supposedly generated **RMB 2.0 billion in revenues and RMB 1.1 billion in profits** in 2010. Yet the hard copies of SAIC filings indicate that in 2010, the Thenardite Operating Subs combined to generate **only RMB 151 million in revenues** and were both **unprofitable!**

Below we present excerpts of the 2010 SAIC filings for the Thenardite Operating Subs showing revenues and profits reported to the Chinese government:

¹² 2010 Annual Report, pg 102 (<http://file.irasia.com/listco/hk/lumena/annual/2010/ar2010.pdf>)

Sichuan Chuanmei Special Glauber Salt Co., Ltd.

Enterprise Name: Sichuan Chuanmei Special Glauber Salt Co., Ltd.

企业名称: 四川川眉特种芒硝有限公司

注册号: 511400400000010

登记机关: 眉山市工商局

Reporting Date: June 27, 2011 填报日期: 2011-06-27

法定代表人签字: _____

企业公章: _____

Corporate Seal: Sichuan Chuanmei Special Glauber Salt Co., Ltd.

Sichuan Meishan Administration For Industry and Commerce

中华人民共和国国家工商行政管理总局制

HTTP://WWW.SAIC.GOV.CN

Production and Operation Table of This Year

五、本年度生产经营情况表

Revenue	销售(营业)收入	103331166.86 元	其中: 服务营业收入	元
	国内销售额	元	其中: 服务营业额	元
	纳税总额	6665522.7 元	其中: 关税	元
	利润总额	-170334121.79 元	净利润 Net Profit	-170334121.79 元
Total Assets	资产总额	3810851386.69 元	其中: 长期投资	元
Total Liabilities	负债总额	3483892754.36 元	其中: 长期负债	元

Sichuan Chuanmei Mirabilite Co., Ltd.

Enterprise Name: Sichuan Chuanmei Mirabilite Co., Ltd.

企业名称: 四川省川眉芒硝有限责任公司

注册号: 511400400000446

Sichuan Meishan
Administration For Industry
and Commerce

登记机关: 眉山市工商局

Reporting Date:
June 27, 2011

填报日期: 2011-06-27

法定代表人签字:

企业公章:

Corporate Seal:
Sichuan Chuanmei
Mirabilite Co., Ltd.

中华人民共和国国家工商行政管理总局制

HTTP://WWW.SAIC.GOV.CN

Production and Operation Table of This Year

五、本年度生产经营情况表

Revenue	销售(营业)收入	47264531.75元	其中: 服务营业收入	元
	国内销售额	元	其中: 服务营业额	元
	纳税总额	979396.19元	其中: 关税	元
	利润总额	-25004073.4元	净利润 Net Profit	-25004073.4元
Total Assets	资产总额	2104958325.05元	其中: 长期投资	6000000元
Total Liabilities	负债总额	2045455968.63元	其中: 长期负债	100000元

There is a stark difference between the revenues and the profitability of the Thenardite Operating Subs reported in the SAIC filings when compared to Lumena's Hong Kong securities filings:

Lumena's Thenardite Operating Subs**SAIC Filing Discrepancy 2010**

Figures are in \$USDmm	Profit Before		
	Revenues	Gross Profit	Income Tax
Hong Kong Financials	1,961	1,143	323
SAIC Filings	151	(195)	-

% Difference	92%	N/A	N/A
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Source: Public Filings; SAIC Filings

SAIC filings indicate that the Thenardite Operating Subs generated 92% less revenue than reported to investors by Lumena and that, rather than making RMB 1.1 billion in profit, they **were unprofitable**. This evidence strongly indicates that Lumena is vastly exaggerating the financial performance of its business. Investors ignore SAIC filings at their peril.

History may not repeat itself, but it rhymes. Glaucus Research published its [first research report](#) on March 8, 2011 (available on our website by clicking [here](#)) warning investors that SAIC filings, auditor and CFO turnover, outlying financial metrics and Chinese web traffic data indicated that UTA was vastly overstating the size and profitability of its business.¹³ Just over one month after the publication of our investment thesis, UTA's auditor resigned and shortly thereafter trading of UTA's shares was halted. The New York Stock Exchange delisted UTA a few months later.

On September 27, 2013, the United States Securities and Exchange Commission (“SEC”) announced fraud charges against Universal Travel Group (“UTA”), and its former CEO and chairwoman, Jiangping Jiang and its former director and interim CFO, Jing Xie.

In early 2011, before the wave of fraud and accounting scandals among US-listed Chinese RTOs crested, many US commentators dismissed SAIC filings as irrelevant and inaccurate. But the fall of UTA is a potent reminder of why SAIC filings are a critical piece of publicly available evidence for investors performing due diligence on Chinese companies. The reasons, which we outlined in our first report, bear repeating:

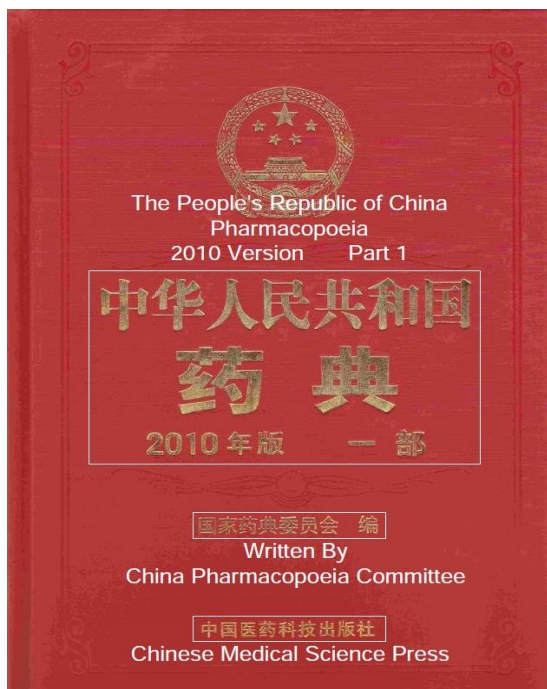
- PRC law requires a company's officer or legal representative to sign SAIC filings under an attestation stating: “I hereby confirm that the contents in the annual inspection report submitted by the company are true.” If SAIC filings are false, that means the company's officer lied in a sworn statement to the PRC government about the veracity of a company's financial statements.
- PRC law requires businesses to file SAIC filings, including financial statements. Why would a government mandate a filing requirement but not care whether they are false?
- Why submit false SAIC filings? Anyone dismissing SAIC filings must answer this question – after all, what possible reason would a company complying with the law have to submit a false financial statement to any regulatory body, whether at home or abroad?
- Do company's doctor financials in their SAIC filings to lower their taxes? SAIC filings are not tax returns. Doctoring financial performance in SAIC filings will not lower a company's tax rate. More importantly, if senior executives falsify regulatory filings to lower its taxes, why would any investor have confidence that the same senior executives would put forth truthful financial statements to the capital markets (especially when the rewards of lying to the capital markets would be so much more lucrative than shaving a few basis points of a company's tax rate).

Because of the differences between PRC GAAP and US GAAP (or the IFRS) and other technical accounting differences under Chinese law, the financial statements found in SAIC filings are not always an **exact match** to the financial statements submitted to public exchanges. So while small discrepancies are to be expected between SAIC filings and a company's publicly filed financial statements, massive differences between the size and profitability of a business are indicative of accounting or other impropriety.

¹³ We would be remiss not to note the excellent research by John Hempton at Bronte capital on UTA, published on his blog in 2010.

IS CHINA REALLY SO CONSTIPATED?

Taken at face value, Lumena's reported sales of medicinal thenardite simply defy credibility. According to the 2010 Chinese Pharmacopoeia, a medical reference guide published by the China Pharmacopoeia Committee, medicinal thenardite is typically prescribed in a dose of 6-12 grams.¹⁴ The primary medicinal use for thenardite is to **cure constipation**, but it is also used as an anti-inflammatory agent.



芒 硝 Mangxiao NATRII SULFAS

本品为硫酸盐类矿物芒硝族芒硝，经加工精制而成的结晶体。主含含水硫酸钠($\text{Na}_2\text{SO}_4 \cdot 10\text{H}_2\text{O}$)。

【性状】 本品为棱柱状、长方形或不规则块状及粒状。无色透明或类白色半透明。质脆，易碎，断面呈玻璃样光泽。气微，味咸。

【鉴别】 本品的水溶液显钠盐(附录IV)与硫酸盐(附录IV)的鉴别反应。

【检查】 铁盐与锌盐 取本品5g，加水20ml溶解后，加硝酸2滴，煮沸5分钟，滴加氢氧化钠试液中和，加稀盐酸1ml、亚铁氰化钾试液1ml与适量的水使成50ml，摇匀，放置10分钟，不得发生浑浊或显蓝色。

镁盐 取本品2g，加水20ml溶解后，加氨试液与磷酸氢二钠试液各1ml，5分钟内不得发生浑浊。

干燥失重 取本品，在105℃干燥至恒重，减失重量应为51.0%~57.0%(附录IX G)。

重金属 取本品2.0g，加稀醋酸试液2ml与适量的水溶解使成25ml，依法检查(附录IX E第一法)，含重金属不得过百万分之十。

砷盐 取本品0.20g，加水23ml溶解后，加盐酸5ml，依法检查(附录IX F)，含砷量不得过百万分之十。

【含量测定】 取本品约0.4g，精密称定，加水200ml溶解后，加盐酸1ml，煮沸，不断搅拌，并缓缓加入热氯化钡试液(约20ml)，至不再生成沉淀，置水浴上加热30分钟，静置1小时，用无灰滤纸或称定重量的古氏坩埚滤过，沉淀用水分次洗涤，至洗液不再显氯化物的反应，干燥，并灼灼至恒重，精密称定，与0.6086相乘，即得供试品中含有硫酸钠(Na_2SO_4)的重量。

本品按干燥品计算，含硫酸钠(Na_2SO_4)不得少于99.0%。

【性味与归经】 咸、苦、寒。归胃、大肠经。

【功能与主治】 泻下通便，润燥软坚，清火消肿。用于实热积滞，腹痛胀满，大便燥结，肠痈肿痛；外治乳痈，痔疮肿痛。

【用法与用量】 6~12g。一般不入煎剂，待汤剂煎得后，溶入汤液中服用。外用适量。

【注意】 孕妇慎用；不宜与硫黄、三棱同用。

【贮藏】 密闭，在30℃以下保存，防风化。

【Usage and dosage】 6 - 12g

Lumena claims to be the only approved and certified medical thenardite producer in the PRC and reported to have sold RMB 872mm of the product in 2012, meaning medicinal thenardite accounted for 55% of the Company's thenardite revenues and 19% of total revenues.¹⁵

In the following table we calculate the number of doses of medicinal thenardite that Lumena claims to sell in China per year, per person. The results are laughable.

Medicinal Thenardite Sanity Check

	2010	2011	2012
Lumena's Reported Medicinal Thenardite Sales ('000 tons)	300	293	258
Avg Dose (grams)	9	9	9
Doses Per Year (in #mm)	33,333	32,556	28,667
Doses per year Per Person in China (>14yrs old)	30	29	26

http://www.indexmundi.com/china/demographics_profile.html

Sources: PRC Pharmacopoeia 2010 Version

Current Estimate that there are 1.1B people in China over the age of 14

¹⁴ <http://www.yaojia.org/article-5402-1.html>.

¹⁵ Lumena 2012 Annual Report, pg 15 (<http://file.irasia.com/listco/hk/lumena/annual/2012/ar2012.pdf>).

If Lumena's reported financials are true, **then Lumena sold the equivalent of 26 doses of thenardite to every person in China above the age of 14 in 2012**. Investors should ask themselves: is China really that constipated? Assuming thenardite is the only cure for constipation and Lumena has 100% of the market share, is every Chinese person taking a thenardite laxative **once every two weeks**? We do not think so.

There is supporting evidence to suggest that the medical thenardite market is nowhere near this size. Although scholarly articles on medical thenardite are rare, a 2007 submission to the Inorganic Chemicals Industry stated that the medical thenardite market was only **50,000 tons** per year.¹⁶

A 2011 feasibility study of medical thenardite which appears to be for Nafine Chemical (SH: 000737), a Lumena competitor and the largest thenardite producer in China, reported that the total demand for medical thenardite in China in 2011 was **50,000 tons**. Investors should also note that this article estimated that Lumena's annual production of medical thenardite was **only 5,000 tons** (the Company claimed to produce 300,000 tons in 2011).¹⁷

According to both articles, the medical thenardite market is roughly 50,000 tons per year, which is the equivalent of **5 doses per year**. This seems much more reasonable and in line with the occurrence of constipation throughout the rest of the world.

Ultimately, the market size of medical thenardite implied by Lumena's reported sales figures appears simply ludicrous. We do not believe that every person in China ingests 25-30 doses of medicinal thenardite per year. Rather, we believe that this is further evidence that Lumena is simply exaggerating the size of its business.

¹⁶ <http://wenku.baidu.com/view/035514e79b89680203d825c9.html>

¹⁷ <http://www.doc88.com/p-177329642878.html>

HIDDEN BENEFICIARY OF A MAJOR TRANSACTION?

Almost immediately after listing on the Hong Kong exchange, Lumena bought out a purportedly ‘independent third party’ who held a minority investment stake in the Company. This transaction netted the seller a 3100% windfall on a four-year investment. Such returns appear too good to be true, raising our suspicions that perhaps an insider was the hidden beneficiary of the transaction.

In June 2005, Sichuan First Silk Printing & Dyeing Co., Ltd. (四川省德陽富斯特新合織有限公司) (“Sichuan First”) [purchased](#) a 10% equity stake in Lumena subsidiary Chuanmei Mirabilite from Sichuan Huatong (四川华通投资控股有限公司) (“Sichuan Huatong”), a company controlled by former Chairman Li Yan (aka Suo Lang Duo Ji, aka, Dominique Shannon).¹⁸ Sichuan First purchased its minority stake for the low price of **RMB 8.2 million**.¹⁹

A mere four years later, Sichuan First sold the minority equity interest *back to Lumena* for **RMB 264 million**, a return of over 3100%! Put simply, Lumena’s former Chairman sold an equity stake in a subsidiary to a supposedly independent third party only to buy back the same equity four years later, immediately after going public, with cash raised from the capital markets, for 3100% percent more than the price at which the former Chairman sold it. Such returns appear too good to be true and the transaction is suspicious for a number of other reasons.

Sichuan First is a limited liability company established in the PRC on March 13, 2003, and according to Lumena is “owned as to 65%, 30% and 5% by Mr. Chen Gang, Mr. Liu Jun and Mr. Zhang Yong, respectively all being PRC individuals and **independent third parties**.”²⁰ There is reason to be skeptical of their independence.

SAIC Filings show that Lumena’s former Chairman appointed Mr. Chen Gang, the majority owner of Sichuan First, to be a director of Chuanmei Mirabilite in July 2004 and that Chen resigned in May 2005, only a month before the equity purchase. It is suspicious because Chen was employed by Lumena’s former Chairman for his privately held company from 2004-2005, and resigned immediately before acquiring the minority equity stake for a song. Did he stop working for Lumena’s former Chairman when he resigned in May 2005, or did Lumena’s former Chairman simply use him and his co-owners as front men while Lumena’s former Chairman remained the secret owner and controller of Sichuan First?

Although we have not found sufficient evidence to close the loop and confirm that this scenario took place, we believe that the transaction is a red flag given the timing of the acquisition and the 3100% returns of the minority investor.

¹⁸ Lumena IPO Prospectus, p. 85.

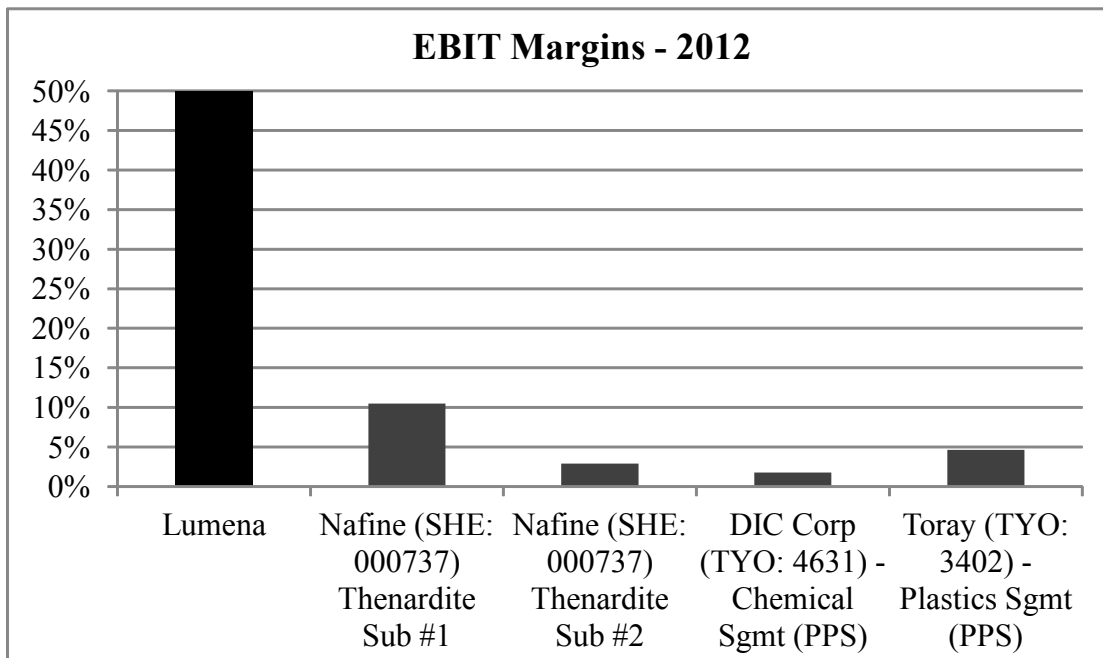
¹⁹ <http://www.hkexnews.hk/listedco/listconews/SEHK/2009/0922/LTN20090922252.pdf>

²⁰ Lumena IPO Prospectus, p. 87.

REPORTED FINANCIALS TOO GOOD TO BE TRUE

Investors may come to the conclusion that Lumena is fabricating its financial statements without the amount of due diligence that we performed. For example, we should not expect commodity chemicals such as thenardite (35% of 2012 Lumena sales) and PPS (65%) to consistently earn double-digit margins, nor should we expect one player within a commoditized industry to significantly outperform its peer group.

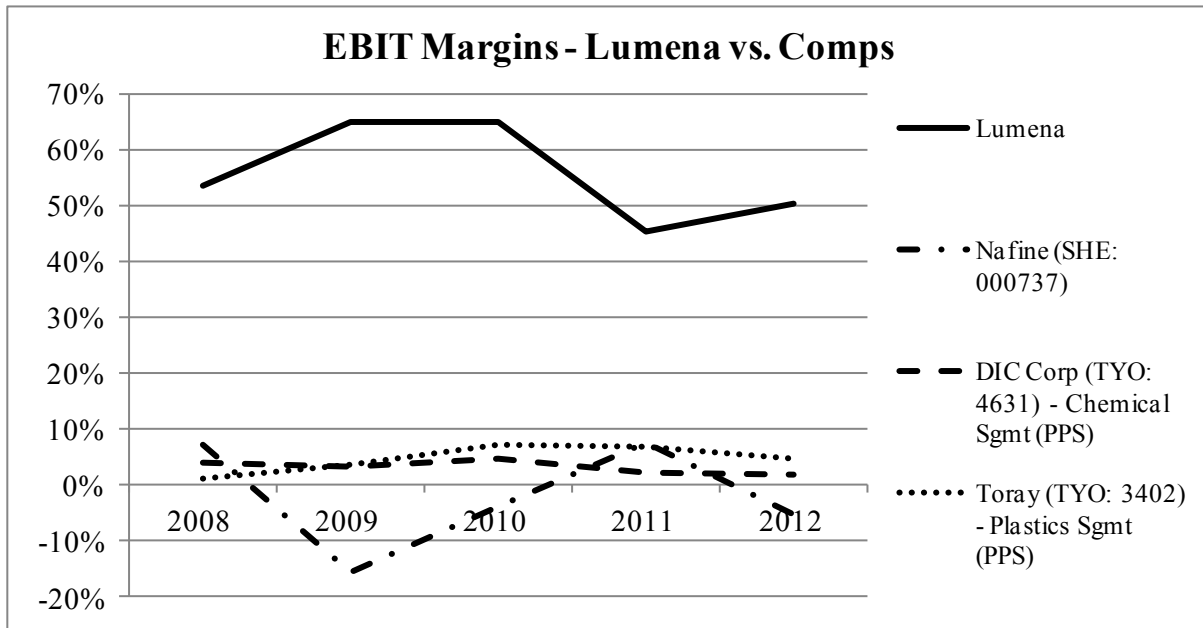
Yet Lumena's EBIT margin for 2012 is so far superior to its peers, including Japan's DIC Corporation, which has a 25% global market share in PPS,²¹ that Lumena's reported financial performance simply defies credibility.



Note: Nafine Thenardite Sub #1 = Nafine Group Huaian Sodium Sulfate Co. Ltd. (2012 Sales of RMB 115 mm); Nafine Thenardite Sub #2 = Sichuan Tong Qing Nafine Co. Ltd. (2012 Sales of RMB 206 mm) ; DIC Corp's Chemical Solutions Materials segment sells PPS and several other chemicals; Toray Plastic & Chemicals segment sells PPS and several other chemicals. Source: Company filings.

A historical comparison reveals much the same: Lumena's EBIT margins hover between 50% and 65% (truly astonishing) while other companies manufacturing thenardite or PPS chemicals squeak by with EBIT margins of between 3% and 10%.

²¹ DIC Corp FY2012 annual report, p. 4



VALUATION

Lumena appears to be circling the drain. Moody's [withdrew](#) its B2 corporate rating on Lumena in December 2013, the timing of which could not be worse considering Lumena must soon redeem its May 2014 convertible bonds. Lumena must pay a 19.3% yield to maturity on the convertible bonds (**with an effective interest rate of 25.97%**), suggesting that the market already considers the Company to be a significant credit risk.

In this report, we presented a wealth of publicly available evidence to support our opinion that Lumena's sales are 90% less than the sales reported to investors and regulators in the Company's Hong Kong filings. We also believe that the Company has inflated the value of assets such as its cash, receivables, and the value of its property, plant and equipment. After all, if a company is booking fake sales, such receipts must be accounted for on the balance sheet.

In our valuation, we estimate that Lumena's revenues are 10% of reported (an opinion based on the evidence presented in this report) and that Lumena's actual EBIT margin for PPS/thenardite is 5% (based on the margins reported by its competitors).

Valuation

Figures are in RMBmm

<i>Assumptions</i>	
Est. % of Sales are Real	10%
Est. % of Cash Recovered	10%
Est. EBIT Margin	5%
<i>Valuation Metrics</i>	
Reported Sales - 2012	4,507
Estimated Actual Sales	451
Estimated EBIT	23
EBIT Multiple	10x
Enterprise Value	225
Plus: estimated cash recovered*†	408
Less: bank borrowings*	(5,161)
Equity Value (RMBmm)	(4,528)
Shares Outstanding (#mm)	5,594
Equity Value per Share (HKD)	(1.01)

* As of 6/30/2013

† Reported Cash balance is RMB4.075B

Exchange rate is RMB1 = HKD1.25

Given the limited offshore assets available for seizure and the difficulty recovering onshore assets (property and equipment) under China's byzantine judicial system, our price target on its HKEX-listed shares is **HKD 0.00**.