



COMPANY: China Harmony Auto Holding Ltd. (3836 HK)
INDUSTRY: Automobile Dealerships

<u>Price</u> <small>(as of 13Nov2020 close)</small>	<u>Market Cap</u>	<u>Average Daily Value</u> <u>Traded (30-Day)</u>
HK\$ 3.44	HK\$ ~ 5.5 billion	HK\$ ~ 20 million

HARMONY UPDATE – Monday November 16, 2020

The Overworked Auditor Excuse

On November 12, 2020 we published our report (the “Report”) on **China Harmony Auto Holding Limited (HKEX: 3836)** (“Harmony” or the “Company”) which highlighted evidence that Chairman Feng defrauded investors and fabricated Harmony’s financial statements.

1. OVERWORKED AUDITORS:

The next day Harmony responded (“Harmony’s Response”) with one of the most laughable rationales for auditor turnover we have ever heard. Harmony claimed that it needed to divide the labor amongst more audit firms because Harmony’s growth was too much for one auditor to handle. Harmony needed a third auditor because it overworked its two other auditors, Ernst & Young and Zhonghui Anda CPA Limited.

To think that a Big 4 auditor cannot handle additional audit work beyond its primary audit responsibilities is ridiculous. Especially when Harmony had zero business combinations in either 2018 or 2019 and only spent RMB 154 million on acquisitions so far in 2020.

2. TAX DISPUTES WITH CHINESE AUTHORITIES FOR 15 YEARS:

Do you think its possible to get away with not paying Chinese Authorities taxes for 15 years?

Harmony’s Response claimed that it was unable to come to an agreement with local tax collection agencies about the amount of tax Harmony owed since 2005.

Why in 2019 does Chairman Feng think that he will be more successful at reaching a settlement with local tax authorities than Harmony would be at settling its own tax liabilities? Why would Chairman Feng pay the tax instead of Harmony just paying the tax itself?

Harmony’s Response did not refute that Chairman Feng was the recipient of RMB 1 billion and instead focused on its rationale for the sham tax liabilities transfer.

This transaction had serious negative repercussions for Harmony’s minority shareholders as it effectively erased the contractual obligation for Chairman Feng to repay RMB 1 billion to Harmony. We suspect that both auditor resignations were related to the write-off of the RMB 1 billion loan to Chairman Feng.

The Company needs to explain how RMB 1 billion of cash went to Chairman Feng and why he doesn’t have to pay it back anymore.

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3. SHARE PRICE SUPPORT:

On the day of our Report, Chairman Feng's Eagle Seeker Company Limited ("Eagle Seeker") purchased 15% of daily traded volume (7.6 mm shares). The day after our Report, Harmony purchased 15% of daily traded volume (2.4mm shares).

We do not believe that these share purchases were made because of Chairman Feng's confidence in Harmony's growth story. Instead, we continue to believe that Chairman Feng, whether directly or via his trust Eagle Seeker, maintains undisclosed pledges against Harmony shares.

4. HARMONY LIED ABOUT THE FMC TRANSFER:

Evidence revealed that Chairman Feng bought Future Mobility Corporation Limited Cayman ("FMC") shares from Harmony at a 90% discount for an immediate RMB 236 million gain.

Harmony's Response claimed that it "*signed an agreement with Mr. Feng Changge before confirming the investment*" to mitigate its own investment risk exposure in FMC.

On December 28, 2016 Harmony made an announcement ("FMC Announcement") in respect of its investment in FMC which did not mention any prior agreement with Chairman Feng.¹

Suddenly after our Report Harmony claimed an agreement existed with Chairman Feng prior to December 28, 2016 which would have made FMC a connected transaction and required shareholder approval.

Harmony cannot have both. It cannot claim no connected transactions in 2016 and then suddenly claim there was a connected transaction in Harmony's Response.

Either Harmony lied in the FMC Announcement to avoid shareholders' scrutiny and approval, or Harmony lied in Harmony's Response. Both would constitute clear breaches of listing rules.

5. CONCLUSION:

We leave it to the facts.

In our Report we presented independent evidence from the PRC State Administration for Industry and Commerce, Credit Reports and the PRC court judgement which showed that Harmony falsified its cash balance and lied about its profits.

Harmony's Response failed to address any of this evidence.

Harmony failed to consolidate operating expenses for its primary subsidiaries and failed to write down failed investments.

We remain short Harmony and believe its stock is worthless.

¹ <https://www1.hkexnews.hk/listedco/listconews/sehk/2016/1228/tn20161228043.pdf>

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