

Fool's Gold?

(Part 2)

It appears Kingold Jewelry Inc. is inflating its #'s.



Kingold Jewelry Inc.

(NASDAQ: KGJI)

Recommendation: Strong Sell

Target Price: \$0.40-\$0.50



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Executive Summary:

Company:

Kingold Jewelry Inc.,
(NASDAQ:KGJI)

Industry:

Jewelry Fabrication

Recommendation:

Strong Sell

Estimated Value:

\$0.40-\$0.50

Report Date:

July 28th

Price:

\$1.75

Market Cap:

90M

- Chinese subsidiary shareholder offering shares on Beijing Equity Exchange at substantial discount
- **Smoking gun evidence:** Net Income reported on Beijing Equity Exchange is less than half of what KGJI filed with SEC
- Financials are domestically audited and officially filed with the Beijing Equity Exchange
- KGJI could now face substantial litigation risk for not actually achieving 2010 make good targets & again raising capital from investors who may have been materially misled
- Serious risk of trading suspension by SEC. Rare case of contradicting filings challenging the legitimacy of both exchanges
- Chairman & the Company have a troubled history in China including a suspicious founding and a denied domestic listing attempt
- Domestic SAT tax filings align with domestic shareholders lower net income

Foreword:

To address some concerns of intention, shorting stocks isn't my game. These reports were never going to be lucrative for me relative to my other options, but I was still hoping they will bring some clarity because what I believe I'm seeing here is absolutely ludicrous.

Commentary:

This can all be boiled down to a simple question; Why would a Chinese shareholder liquidating his position sell his shares based on a net profit of 9M USD instead of 19M USD? In other words; the thesis here is not in conflicting tax filings, or the subsidiary selling at a lower price, the issue is two separate shareholders with conflicting claims of how much profit KGJI actually generated in 2010.

What we have here ladies and gentlemen,,,, is a good 'ol fashioned Mexican Standoff!

In the red white & blue *corner*, we have the audit of Friedman LLP and the actions of Mr. Zhihong's share buy-back with a supposed 19M USD in net profit. In the red & yellow *corner*, we have the audit of Wuhan Tinali Accountants and the actions of Beijing Shouchuang selling it's stake based on 9M USD in net profit.

Which *corner* is using the real net profits? 19M USD or 9M USD

There are two scenarios here. (1.) Mr. Zhihong is correct, the SEC filings are accurate and Beijing Shouchuang is massively short-changing themselves by selling at a valuation by using only half the company's profits. Or (2.) Mr. Zhihong has inflated the company's profits on paper and his personal buy-back program is just essentially him 'doubling-down' on a bluff he made long ago. (keep in mind, he will be buying back stock with cash he raised from public investors)

Let's look at the tail of the tape and examine both parties incentives: Mr. Zhihong has been married to Kingold since 2002. It's his baby and his fate is tied to it. Conversely, Beijing Shouchuang has been with Kingold for at least 4 years, however, Beijing Shouchuang is not tied to Kingold like Mr. Zhihong is. This is just business as usual for Beijing Shouchuang, whom can, and are, simply walking away.

So if Kingold isn't lying, why then would Beijing Shouchuang claim Kingold had only 9M USD in net profits as it was exiting it's position?

This is all I want Kingold's management to explain.

Kingold managed to send me a cease and desist letter in less than 24 hours, and yet after ten weeks and counting, they haven't been able to draft an explanation as to why one of their oldest and most connected shareholders would chop their reported profits in half.

Worth Considering - Kingold's Troubled History



On Aug. 4th 2008 Kingold was denied a domestic IPO in China by the China Securities Regulatory Commission (CSRC). On Aug. 7th a formal letter from the CSRC (File No. [2008] 178) said the main reason for the denial was doubt that the company would be able to hire and train enough technicians to fulfill their business plan. In the CSRC's opinion, the company would have to hire an additional 359 technicians in one year to reach its prospectus targets, given that it had taken the company 4 years to recruit & train its then current 141 technicians.

That was the official reason, however, at the time of this failed domestic listing, the Chinese media, lead by economist Xia Cao (夏草), nicknamed 'the financial detective', asserted allegations as to why Kingold was actually denied its allegations:

- The origin of KGJI's seed capital was considered very suspect. Chairman and founder Jia Zhihong (贾志宏) claimed to have acquired his 100M RMB from speculative stock market trading. (His source was never clarified)¹
- Coincidentally, the company from which Kingold bought their machines from (Xiamen Ximei Jewelry Co., Ltd (厦门喜美首饰有限公司)), vanished abruptly with some claiming it was still in operation behind the scenes.²
- There were also allegations that Jia Zhihong personally evaded taxes (publicly alleged by Xia Cao, but never confirmed)³
- And lastly there were suspect stock transfers by Jia Zhihong (贾志宏) and Chenwei (陈炜) in order to satisfy minimum # of shareholder requirements.⁴

After the denial, the company quickly went dark and stopped answering questions from reporters.⁵ Was this non-listing ruling just a result an ill timed application during rapid growth or a result of jumping through one too many legal loop-holes?

¹ Source: <http://finance.sina.com.cn/stock/newstock/20080806/03005171039.shtml>

² Source: <http://finance.sina.com.cn/stock/newstock/20080806/03005171039.shtml>

³ Sources: <http://money.163.com/08/0805/03/4116GVGS00251RJ2.html> & <http://finance.sina.com.cn/stock/newstock/20080806/03005171039.shtml>

⁴ <http://money.163.com/08/0805/03/4116GVGS00251RJ2.html> & <http://finance.sina.com.cn/stock/newstock/20080805/02405167297.shtml>

⁵ Source: <http://money.163.com/08/0805/03/4116GVGS00251RJ2.html> & <http://finance.sina.com.cn/stock/newstock/20080806/03005171039.shtml>



SAIC & SAT Filings

My normal channel to acquire SAIC filings was unable to retrieve Wuhan Kingold's SAIC financials. Even my secondary alternative channel was unable to get the SAIC filings. These same channels that were able to get many other Chinese RTO SAIC filings came up empty handed. All these agents came back saying that the local authorities had the SAIC filings under a 'protected status'. However my SAT guy was able to get the SAT numbers, most likely since SAT numbers are always safeguarded, his channel to SAT figures was unabated by 'protected status'. Another source for financials was the balance sheet KGJI reported to the National Statistics Bureau, which I've included below. A data-point which I was unable to attain was Kingold's monthly or annual gold volume purchases from the Shanghai Gold Exchange. The Shanghai Gold Exchange confirmed that Wuhan Kingold is a member, however the Shanghai Gold Exchange is very tight lipped about it's members transaction volumes. (Gold purchases would only help verify revenue and still leave questions for the profits)

KGJI Financials in Millions of USD					
	Filed with National Statistics Bureau for 2009	Filed with SAT for 2009	Filed with SEC for 2009	Reported by Beijing Capital for 2010	Filed with SEC for 2010
Revenue	-	73.7	250.5	389.5	523
Operating Profit	-	6.5	15.7	12	31
Net Profit	-	1.46	9.1	9	19
Total Assets	69.5	70.4	62.3	54.2	84.3
Total Liabilities	34.7	36	10.6	5.2	10.5
Total Equity	34.9	34.3	62.3	48.9	73.8

As you can see from the table we have uncovered another discrepancy worth noting, specifically, Kingold's 2009 domestic SAT reported net profits reported to the Chinese tax authorities of 1.46M USD are materially lower than the 9.1 M USD Kingold reported to the SEC. Furthermore, the SAT filings we were able to obtain outlined a balance sheet that reasonably matched the numbers reported to the National Statistics Bureau. It would seem that Kingold significantly inflated both their 2009 and 2010 profits reported to the SEC.

Conclusion



The net profits is the litmus test of a company's health. When the difference of numbers reported ranges from 9 to 19, the long term level headed investors will flee and only speculators will remain. Perhaps that is what's already happened here and I'm simply just late to the party. In any case, without any explanation of Beijing Shouchuang's actions, Kingold's stock should stay stuck somewhere in this Nash-equilibrium purgatory.

I'm not trying to game the system here, I'm hoping to make enough of a stink so that the company and/or it's independent directors' will do something more proactive than simply have DLA Piper send me a cease & desist letter calling me a liar. (I believe DLA Piper should also send a CC to KGJI's shareholder, Beijing Shouchuang) This is normally where one would hope for Mr. David Sherman to come in like a white knight and set the record straight. Hopefully this will happen. All it will take is an explanation and then I'll look like an idiot. Or maybe Mr. Sherman won't pick up the reigns. Maybe this skeleton will just get stashed in KGJI's closet and everyone will forget until the next time the chinks in the IR armor start to show.

In conclusion, I still strongly suggest you get someone you trust who reads Chinese to go over Beijing Shouchuang's posting and contact the relevant parties. In the yahoo forums someone has found another Chinese news report here: I have included the posting in its entirety in the appendix. (Note: the #'s on the Chinese site are in 10,000's of RMB).

I believe there is litigation risk here, and until this issue gets clarified, I see nothing but downward pressure. I do not imagine any 'big money' will enter the stock with this issue unsettled.

The fund manager I'm employed by is short the stock.

Pete

Appendix

For your convenience:

Kingold's 10-K filing can be accessed here:

http://www.sec.gov/Archives/edgar/data/1089531/000114420411018554/v216529_10k.htm

Chart of Chinese and English Business names translations:

Entity	English Name	Chinese Characters	Chinese Phonetics ('ping-ying')	Web Links
4.17% owner of equity interest in Wuhan Kingold (as listed in 10-K)	<i>Beijing Shouchuang Investment Co. Ltd./ Beijing Capital Investment Co. Ltd.</i>	北京首创创业投资有限公司	Beijing Shouchuang Chuangye Touzi Youxian Gongsi	http://capitalvc.com/
4.17% owner of equity interest in Wuhan Kingold as listed on Beijing Equity Exchange (technically the holding company of the fund listed in KGJI's 10-K)	Beijing Capital Group	北京首都创业集团有限公司	Beijing Shoudu Chuangye Jituan Youxian Gongsi	Official: http://www.bjcapital.com/ Overview: http://baike.baidu.com/view/108134.htm
Domestic Auditing firm	Wuhan Tianli Partners Accounting Firm	武汉天立合伙会计师事务所	Wuhan Tianli Hehuo Kuaijishi Shiwusuo	Listing: http://4692400.71ab.com/ 2 nd : Listing http://www.71ab.com/view_4692400.htm
Kingold Jewelry Inc's mainland subsidiary. The subject of the VIE Contracts.	Wuhan Kingold Co., Ltd.	武汉金凰珠宝股份有限公司	Wuhan Jinhuang Zhubao Gufen Youxian Gongsi	Chinese Site: http://kingold.com.cn/ (Western Site for KGJI: http://www.kingoldjewelry.com/s/History.asp)
Exchange where this 4.17% stake in the subsidiary is listed for sale	China Beijing Equity Exchange	北京产权交易所	Beijing Chanquan Jiaoyisuo	Official: http://www.cbex.com.cn 2 nd link
Kingold Founder	Zhihong Jia	贾志宏	Jia Zhihong	
Kingold GM	Bin Zhao	赵彬	Zhao Bin	

Clarification that this posting is for KGJI's subsidiary:

- Both Beijing Capital's posting and KGJI's 10-K list Wuhan Kingold's date of incorporation as: August 2 2002.
- Both Beijing Capital's posting and KGJI's S-1 list the original registered capital of of Wuhan Kingold as 120M RMB.
- Both Beijing Capital's posting and KGJI's 10-K both list the same shareholder %'s for Jia Zhihong, Zhao Bin & Beijing Capital all match up with KGJI's 10-K filing:
 - **From the 10-K:** Wuhan Kingold is 55.31% owned by Zhihong Jia, our founder, chairman and chief executive officer; 1.67% owned by Bin Zhao, our general manager and director; 4.17% owned by Beijing Shouchuang Investment Co. Ltd., a PRC state owned enterprise, with the balance of 38.85% owned by a total of 44 other shareholders, who are all PRC citizens. All of Wuhan Kingold's shareholders, other than Beijing Shouchuang Investment Co. Ltd., have entered into the VIE agreements. (source: [10-K](#) page 13.)
 - **From Beijing Capital's post on the Beijing Equity Exchange:**

No.	Wuahn Kingold Top Ten Shareholders	Stake
1	Jia Zhihong	55.3054%
2	Tianjin Fortune wealth equity investment fund center (limited partnership)	10.7292%
3	Beijing Capital Group Ltd. / Beijing Shouchuang Investment Co., Ltd.)	4.1667%
4	Dai Garden	3.3333%
5	TANG Po	3.3333%
6	Shenzhen, Dong Fang Anying invested enterprises (limited partnership)	2.6042%
7	Yellow River	2.5%
8	Shenzhen Venture Capital Management Co., Ltd. Huayang St.	2.3438%
9	Zhao	2.0833%
10	Zhao Bin	1.6667%

The Beijing Capital Offering Its 4.1667% Holding on the China Beijing Equity Exchange

The Original Beijing Capital Posting was here (<http://www.cbex.com.cn/G3/2011010285.shtml>) and was taken down after it's June 15th expiry. Here is a link to picture of the full webpage: <http://i.imgur.com/Ps8AV.png> And below it is pasted in sections. (Here is another Chinese news source citing this posting: <http://finance.ifeng.com/gem/hwdt/20110522/4053980.shtml>)


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CHINA BEIJING EQUITY EXCHANGE

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武汉金凰珠宝股份有限公司500万股股份(4.1667%股权)
→ [我对此项目感兴趣](#)

标的名称	武汉金凰珠宝股份有限公司500万股股份(4.1667%股权) (点击数: 989次)		
项目编号	G311BJ1004331	挂牌价格	2945万元
首次登报报刊	上海证券报	挂牌公告期	自公告之日起20个工作日
挂牌起始日期	2011-05-18	挂牌期满日期	2011-06-15
标的所在地区	中国-湖北省-武汉市	标的所属行业	其他行业

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二、标的企业简介

标的企业名称	武汉金凰珠宝股份有限公司		
注册地(住所)	中国-湖北省-武汉市(江岸区黄浦科技园特15号)		
法定代表人	贾志宏		
成立时间	2002-08-02		
注册资本(万元)	人民币 12000		
经济类型	国有参股企业		
公司类型(经济性质)	股份有限公司		
所属行业	其他行业		
组织机构代码	74140273-6		
经营规模	小型		
经营范围	铂金饰品的生产、加工、销售;黄金、白银饰品的生产、加工、批发兼零售及回收、以旧换新业务及境外黄金、铂金和白银的来料加工业务;黄金交易代理;黄金交易业务咨询;钻石饰品的加工、销售;氯化金加工及销售;贵金属的生产、加工、批零兼营;经营本公司和成员企业科研生产所需的原辅材料、仪器仪表、机械设备、零配件(经营期限、经营范围与许可证件核定的期限、范围一致);货物进出口、技术进出口、代理进出口业务。(不含国家禁止或限制进出口的货物或技术)(国家有专项审批的项目经审批后方可经营)。****		
职工人数	450人		
是否含有国有划拨土地	否		

标的企业原股东是否放弃行使优先购买权

是

序号	前10位股东名称	持股比例
1	贾志宏	55.3054%
2	天津达晨创富股权投资基金中心(有限合伙)	10.7292%
3	北京首创业投资有限公司	4.1667%
4	戴翠园	3.3333%
5	唐永宝	3.3333%
6	深圳市创东方安盈投资企业(有限合伙)	2.6042%
7	黄泛	2.5%
8	深圳市圣华羊创业投资管理有限公司	2.3438%
9	赵金	2.0833%
10	赵彬	1.6667%

以下数据出自企业年度审计报告

	营业收入	营业利润	净利润

	10	赵彬	1.6667%	
主要财务指标 (万元)	以下数据出自企业年度审计报告			
	2010年度	营业收入	营业利润	净利润
		253980	7883	5873
		资产总计	负债总计	所有者权益
	35330	3415	31915	
	审计机构	武汉天立合伙会计师事务所		
	以下数据出自企业财务报表			
	报表日期	营业收入	营业利润	净利润
	2011-04-30	83251	2748	1808
	报表类型	资产总计	负债总计	所有者权益
月报	37020	3297	33724	
资产评估情况 (万元)	评估机构	北京天健兴业资产评估有限公司		
	核准(备案)机构	北京首都创业集团有限公司		
	核准(备案)日期	2011-05-13		
	评估基准日	2010-12-31		
	项目	账面价值	评估价值	
	资产总计(万元)	-	-	
	负债总计(万元)	-	-	
	净资产(万元)	37199.7	63383.5	
转让标的对应评估值	2641(万元)			
评估基准日审计机构	武汉天立合伙会计师事务所			
律师事务所	北京市信裕律师事务所			
内部审议情况	董事会决议			
重要信息披露	其他披露内容	详见《资产评估报告》、《审计报告》。		
	管理层拟参与受让意向	否		
三、转让方简况				
转让方基本情况	转让方名称	北京首创业投资有限公司		
	注册地(住所)	中国[156]北京市[110000]市辖区[110100]海淀区[110108]北京市海淀区紫竹院路69号18层1808室		
	法定代表人	李松平		
	注册资本(万元)	人民币 4843		
	经济类型	国有控股企业		
	公司类型(经济性质)	有限责任公司		
	所属行业	投资与资产管理		
	组织机构代码	63370630-2		
	经营规模	小型		
	持有产(股)权比例	4.17%		
	拟转让产(股)权比例	4.17%		
产权转让行为批准情况	国资监管机构	省级国资委		
	所属集团或主管部门名称	北京首都创业集团有限公司		
	组织机构代码	101138949		
	批准单位名称	北京首创业投资有限公司董事会		
	决议类型	董事会决议		
四、交易条件与受让方资格条件				
交易条件	挂牌价格(万元)	2945		
	价款支付方式	一次性付款		
	与转让相关其他条件	1、意向受让方资格确认后3个工作日内, 应交纳883.5万元交易保证金至北交所的指定账户; 2、意向受让方自被确定为最终受让方后, 须在10个工作日内签订《产权交易合同》, 全部转让价款须在产权交易合同签订后5个工作日内一次性付清; 3、如本项目在挂牌期间只产生一家符合条件的意向受让方则采取协议转让方式, 该交易保证金在《产权交易合同》签订后可转为履约的部分价款。如产生两家及以上符合条件的意向受让方, 则采取竞价方式, 该交易保证金转为竞价保证金。意向受让方被确定为最终受让方的, 其竞价保证金可转为履约的部分价款; 4、如非转让方原因, 出现以下任何一种情况时, 转让方有权扣除意向受让方所交纳的保证金作为补偿金: ①意向受让方提出受让申请且交纳保证金后单方撤回受让申请的。②挂牌期满后, 产生两家及以上符合条件的意向受让方时未参加后续竞价程序的。③被确认为最终受让方后未能在十个工作日内与转让方签订《产权交易合同》的。④未能在签订《产权交易合同》后5个工作日内付清交易价款的。		
受让方资格条件	国家法律、行政法规规定的其他条件。			

	批准单位名称	北京首创创业投资有限公司董事会
	决议类型	董事会决议
四、交易条件与受让方资格条件		
交易条件	挂牌价格 (万元)	2945
	价款支付方式	一次性付款
	与转让相关其他条件	1、意向受让方资格确认后3个工作日内，应交纳883.5万元交易保证金至北交所的指定账户； 2、意向受让方自被确定为最终受让方后，须在10个工作日内签订《产权交易合同》，全部转让价款须在产权交易合同签订后5个工作日内一次性付清； 3、如本项目在挂牌期间只产生一家符合条件的意向受让方则采取协议转让方式，该交易保证金在《产权交易合同》签订后可转为履约的部分价款。如产生两家及以上符合条件的意向受让方，则采取竞价方式，该交易保证金转为竞价保证金。意向受让方被确定为最终受让方的，其竞价保证金可转为履约的部分价款； 4、如非转让方原因，出现以下任何一种情况时，转让方有权扣除意向受让方所交纳的保证金作为补偿金：①意向受让方提出受让申请且交纳保证金后单方撤回受让申请的。②挂牌期满后，产生两家及以上符合条件的意向受让方时未参加后续竞价程序的。③被确认为最终受让方后未能在十个工作日内与转让方签订《产权交易合同》的。④未能在签订《产权交易合同》后5个工作日内付清交易价款的。
受让方资格条件		国家法律、行政法规规定的其他条件。
保证金设定	是否交纳保证金	是
	交纳金额	883.5万元
	交纳方式	支票、电汇、网上银行支付。

五、挂牌信息	
挂牌公告期 (信息发布期)	自公告之日起20个工作日
挂牌期满后，如未征集到意向受让方	信息发布终结
交易方式	挂牌期满，如征集到两个及以上符合条件的意向受让方，选择以下交易方式确定受让方： 网络竞价(多次报价)
权重报价、招投标或动态报价实施方案主要内容	

受托会员	经纪会员名称	北京首都创业集团有限公司	
	经纪会员联系人	马赫	联系电话 58385566-1726
交易机构	交易机构名称	北京产权交易所	
	交易机构联系人	赵璇	联系电话 010-66295566
	交易机构部门负责人	付奇	联系电话 010-66295717
	交易机构传真	010-66295588	

→ 我对此项目感兴趣

项目反馈: 请以不超过200字发表您的反馈信息。 剩 <input type="text" value="200"/>	<input type="text"/>
您的姓名:	<input type="text"/> 您的电话: <input type="text"/>
您的Email:	<input type="text"/>
<input type="button" value="提交"/> <input type="button" value="重置"/>	

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