

China Natural Gas, Inc.  
Form 424B5  
September 01, 2009

The information in this preliminary prospectus supplement is not complete and may be changed. This preliminary prospectus supplement and the accompanying prospectus are not an offer to sell these securities and we are not soliciting offers to buy these securities in any state where the offer or sale is not permitted.

**Filed Pursuant to Rule 424(b)(5)  
Registration No. 333-160150**

# **SUBJECT TO COMPLETION, DATED SEPTEMBER 1, 2009**

**PROSPECTUS SUPPLEMENT  
(to prospectus dated August 20, 2009)**

## **SHARES**

### **CHINA NATURAL GAS, INC.**

#### **Common Stock**

We are selling \_\_\_\_\_ shares of our common stock.

Shares of our common stock are currently traded on the Nasdaq Global Market under the symbol CHNG. On August 28, 2009, the closing price of our common stock was \$9.71 per share.

**INVESTING IN OUR SECURITIES INVOLVES A HIGH DEGREE OF RISK. SEE RISK FACTORS BEGINNING ON PAGE S-10 OF THIS PROSPECTUS SUPPLEMENT.**

	Per Share	Total
Public Offering Price	\$	\$
Underwriting Discount	\$	\$
Proceeds, before expenses, to us	\$	\$

We have granted the underwriters a 30-day option to purchase up to an additional \_\_\_\_\_ shares from us to cover over-allotments, if any. If the underwriters exercise this option in full, the total underwriting discounts and commissions will be \$ \_\_\_\_\_, and our total proceeds, before expenses, will be \$ \_\_\_\_\_.

We expect to deliver the shares of our common stock to purchasers on or about September \_\_\_\_\_, 2009.

**Neither the Securities and Exchange Commission nor any state securities commission has approved or disapproved of these securities or determined if this prospectus is truthful or complete. Any representation to the contrary is a criminal offense.**

**Roth Capital Partners**

**Simmons & Company  
International**

**The date of this prospectus is September 1, 2009.**

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## Prospectus

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**You should rely only on the information provided or incorporated by reference in this prospectus supplement and the accompanying base prospectus. We have not authorized anyone to provide you with information different from that contained in this prospectus supplement and the accompanying base prospectus or such incorporated documents. We are not making an offer to sell these shares of common stock in any jurisdiction where the offer is not permitted. The information contained in or incorporated by reference into this prospectus supplement and the accompanying base prospectus is accurate only as of the date of this prospectus supplement and the accompanying base prospectus or the documents incorporated by reference therein, regardless of when this prospectus supplement and the accompanying base prospectus is delivered or when any sale of the common stock occurs. Our business, financial condition, results of operations and prospects may have changed since that date.**



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## **ABOUT THIS PROSPECTUS SUPPLEMENT**

If information in this prospectus supplement is inconsistent with the accompanying base prospectus or the information incorporated by reference, you should rely on this prospectus supplement. You should read both the prospectus supplement and the accompanying base prospectus together with the additional information about us to which we refer you in the section of the accompanying base prospectus entitled **Where You Can Find More Information**.

This prospectus supplement and the accompanying base prospectus are part of a **shelf** registration statement that we have filed with the Securities and Exchange Commission (the **SEC**). Each time we sell securities under the accompanying base prospectus, we will provide a prospectus supplement that will contain specific information about the terms of that offering, including the price, the amount of securities being offered and the plan of distribution. The **shelf** registration statement was declared effective by the SEC on August 20, 2009. This prospectus supplement describes the specific details regarding this offering, including the price, the amount of common stock being offered, the risks of investing in our common stock and the underwriting arrangements. The accompanying base prospectus provides general information about us, some of which, such as the section entitled **Plan of Distribution**, or descriptions of unissued securities other than our common stock, may not apply to this offering.

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## PROSPECTUS SUPPLEMENT SUMMARY

*You should read the following summary together with the more detailed information concerning us, the common stock being sold in this offering and our financial statements appearing in this prospectus supplement and the accompanying base prospectus and in the documents incorporated by reference in this prospectus supplement and the accompanying base prospectus. Because this is only a summary, you should read the rest of this prospectus supplement and the accompanying base prospectus, including all documents incorporated by reference, before you invest in our common stock. Read this entire prospectus supplement and the accompanying base prospectus carefully, especially the risks described under Risk Factors and the financial statements and related notes, before making an investment decision.*

### Overview

We are a distributor of compressed natural gas ( CNG ) in China, which we primarily distribute through our Company-owned CNG fueling stations. As of June 30, 2009, we operated 23 CNG fueling stations in Shaanxi province and 12 CNG fueling stations in Henan province. We own our CNG fueling stations while we lease the land upon which our CNG fueling stations operate. For the three and six months ended June 30, 2009, we sold CNG of 41,152,513 and 80,446,633 cubic meters, respectively, through our fueling stations, compared to 37,304,556 and 67,844,028 cubic meters for the three and six months ended June 30, 2008, respectively. We also transport, distribute and sell piped natural gas to residential and commercial customers in the Xi'an area, including Lantian County, and the districts of Lintong and Baqiao, in Shaanxi province through a high pressure pipeline network of approximately 120 kilometers.

We operate four main business lines:

Distribution and sale of compressed natural gas through Company-owned CNG fueling stations for hybrid (natural gas/gasoline) powered vehicles (35 stations as of June 30, 2009);

Installation, distribution and sale of piped natural gas to residential and commercial customers through Company-owned pipelines. We distributed and sold piped natural gas to approximately 103,343 residential customers as of June 30, 2009;

Distribution and sale of gasoline through Company-owned CNG fueling stations for gasoline and hybrid (natural gas/gasoline) powered vehicles (seven of our CNG fueling stations sold gasoline as of June 30, 2009); and

Conversion of gasoline-fueled vehicles to hybrid (natural gas/gasoline) powered vehicles at our auto conversion sites. We buy all of the natural gas that we sell and distribute to our customers. We do not mine or produce any of our own natural gas and have no plans to do so during the next 12 months. We currently sell our natural gas in two forms: (i) CNG and (ii) piped natural gas.

On October 24, 2006, our variable interest entity, Xi'an Xilan Natural Gas Co., Ltd. ( XXNGC ), formed a wholly-owned subsidiary, Shaanxi Jingbian Liquefied Natural Gas Co., Ltd. ( SJLNG ), for the purpose of constructing a liquefied natural gas ( LNG ) facility to be located in Jingbian, Shaanxi province. We plan to invest approximately \$45 million to construct this facility, a portion of which was funded through the sale of senior notes to Abax Lotus Ltd. ( Abax ), and the remainder of which will be funded by our cash flows from operations. The LNG plant is under construction and is expected to be completed and fully operational by the end of 2009. Once completed, the plant is expected to have a LNG processing capacity of 500,000 cubic meters per day, or approximately 150 million cubic meters on an annual basis.

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We had total revenues of \$20,742,520 and \$16,890,486 for the three months ended June 30, 2009 and 2008, respectively, total revenues of \$39,270,186 and \$30,916,160 for the six months ended June 30, 2009 and 2008, respectively, and total revenues of \$67,720,659 and \$35,392,053 for the years ended December 31, 2008 and 2007, respectively. We had net income of \$3,862,756 and \$3,512,892 for the three months ended June 30, 2009 and 2008 respectively, net income of \$8,064,379 and \$6,321,463 for the six months ended June 30, 2009 and 2008, respectively, and net income of \$15,190,368 and \$9,116,070 for the years ended December 31, 2008 and 2007, respectively.

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## **Our Products, Services and Customers**

### **CNG and Gasoline Fueling Stations**

As of June 30, 2009, we operated 23 CNG fueling stations in Shaanxi province and 12 CNG fueling stations in Henan province. Through these Company-owned fueling stations, CNG is sold to taxis, buses and private cars that operate with CNG technology. During the year ended December 31, 2008, we purchased natural gas at an average cost of RMB1.11/cubic meter and sold each cubic meter for RMB2.34 net of value added taxes in Shaanxi province and we purchased natural gas at an average cost of RMB1.31/cubic meter and sold each cubic meter for RMB2.83 net of value added taxes in Henan province.

We continue to expand our CNG fueling station base by constructing new stations as well as acquiring existing stations. We can obtain approvals and construct a CNG fueling station in Shaanxi province in approximately 60 days for a cost of approximately US\$1,300,000 to US\$1,500,000. We are evaluating additional sites for CNG fueling stations in Shaanxi, Henan and in other regions.

We also own three natural gas compressor stations. Two are located in Xi'an: Hongqing station, acquired in July 2005, near our pipeline; and Changsheng station, acquired in September 2008. The third station is located in Xianyang city and was acquired in January 2008. A compressor station compresses natural gas and allows trucks to transport CNG to fueling stations. We currently have a daily processing capacity of 250,000 cubic meters of CNG.

We began to distribute and sell gasoline during the fourth quarter of 2007 in an effort to support our sales of CNG by attracting more natural gas/gasoline hybrid car owners through providing a one-stop refueling option for such customers. Our gasoline facilities were either installed by us at our existing CNG stations or acquired through our acquisition of CNG fueling stations that have both CNG and gasoline fueling capability. As of June 30, 2009, we distributed and sold gasoline at seven of our Company-owned CNG fueling stations for gasoline and hybrid (natural gas/gasoline) powered vehicles in Xi'an. During the year ended December 31, 2008, we purchased gasoline at an average cost of RMB3.95/liter and sold each liter at an average price of RMB4.65 net of value added taxes in Xi'an.

### **Our Pipeline Distribution System**

We own and operate a high pressure pipeline network of approximately 120 kilometers in the Xi'an area. The network connects to a high pressure government pipeline network operated by Shaanxi Natural Gas Company, which supplies natural gas directly from a gas field in the northern region of the province. Our high pressure pipeline then feeds into city-gate let-down stations at Hongqing and Lantian County, where the pressure is reduced and natural gas is transported through a network of low-pressure distribution pipes to supply our residential and commercial customers in Lantian County and the Lintong and Baqiao Districts. The supply also feeds our compressor stations at Hongqing and Xianyan where CNG is collected by tankers to supply our CNG fueling stations.

Each of our pipeline customers is physically connected to our pipeline network through Company installed and maintained piping and natural gas usage gauges. We generate revenues both from the sale of natural gas to these customers and the installation and maintenance of this equipment.

We believe we are currently the sole authorized provider of natural gas to residential customers in our service areas and the only privately owned company in Shaanxi province to own and operate this type of high pressure pipeline.



## **Our Automobile Conversion Sites**

We began our automobile conversion business during the second quarter of 2007. Our automobile conversion sites convert gasoline-fueled vehicles to hybrid (natural gas/gasoline) powered vehicles. As of June 30, 2009, we had four auto conversion sites, all in the Xi'an area.

## **Our CNG Market**

As of December 31, 2008, we estimate that there were approximately 14,285 vehicles using CNG in the Xi'an area of which 3,639 were buses and 10,646 were taxis. Each bus uses an average of approximately 100 cubic meters of CNG per day and each taxi uses an average of approximately 40 cubic meters of CNG per

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day (Source: Xi'an Clean Fuel Vehicles Commission 2007 and PRC Ministry of Science and Technology). The PRC government estimates in its Eleventh Five Year Plan (2006-2010) that current total demand for CNG as a vehicular fuel in the Xi'an area will reach approximately 1,070,000 cubic meters per day by 2010. Compared to gasoline and diesel, we believe natural gas as vehicular fuel is cheaper, cleaner and safer. The PRC government's Clean Energy Policy encourages the use of CNG as a vehicular fuel.

We estimate that the average CNG station in Xi'an pumped approximately 11,000 cubic meters of CNG per day in 2008. As of December 31, 2008, there were 71 CNG fueling stations in Xi'an and we estimate that approximately 781,000 cubic meters of CNG was pumped per day during 2008, a figure below estimated total demand. As a result, we believe that there is unmet demand for CNG as vehicular fuel in the Xi'an area.

As of December 31, 2008, there were approximately 7,500 vehicles using CNG in Henan province, of which 3,000 were buses and 4,500 were taxis. (Source: Zhengzhou Vehicle Administration Bureau). We estimate each bus uses an average of approximately 100 cubic meters of CNG per day and each taxi uses an average of approximately 40 cubic meters of CNG per day.

We estimate that the average CNG station in Henan pumped approximately 11,000 cubic meters of CNG per day in 2008. As of December 31, 2008, there were 40 CNG fueling stations in Henan and we estimate that approximately 440,000 cubic meters of CNG was pumped per day during 2008, a figure below estimated total demand. As a result, we believe that there is unmet demand for CNG as vehicular fuel in the Xi'an area.

On July 22, 2009, we, through our variable interest entity, XXNGC, entered into a joint venture agreement (Joint Venture Agreement) with China National Petroleum Corporation Kunlun Natural Gas Co., Ltd. (Kunlun). Pursuant to the Joint Venture Agreement, XXNGC will form a joint venture company with Kunlun (the Joint Venture Company) to construct and operate CNG stations, conduct sales of CNG, convert gasoline fueled vehicles to hybrid (natural gas/gasoline) powered vehicles and other related technical services in Henan province, China.

The Joint Venture Company will have an initial registered capital of RMB50,000,000 (approximately US\$7,350,000).

Kunlun will contribute RMB25,500,000 in cash, representing 51% of the Joint Venture Company's total registered capital, upon the approval of the governing officers of Kunlun. XXNGC will contribute RMB24,500,000, representing 49% of the Joint Venture Company's total registered capital, in two installments. The first installment will be RMB10,000,000 in cash and the second installment of RMB14,500,000 will be either cash, property (currently expected to be a fleet of tankers consisting of two locomotives and four tanks) or a combination of cash and property.

Both parties will share the management responsibilities of the operations of the Joint Venture Company. The Joint Venture Company has a term of 20 years commencing on August 1, 2009 and terminating on July 31, 2029.

While there are many competitors in the distribution and sale of CNG in China, we believe we are well positioned in the market through our cooperation with local natural gas suppliers and our experience in Shaanxi and Henan.

## **Our Pipeline Network Customers**

As of June 30, 2009, we had 103,343 customers, including residential and commercial customers. We continue to expand our customer base in Xi'an's newly developed business and residential areas including Xihan and Chanliu. Our commercial customers, including the Xiwei Aluminum Company and the Hungtian Company, use natural gas as a raw material for their production process. We are not dependent upon any single customer or group of customers for a material portion of our natural gas sales or revenues.

Our pipeline customers purchase natural gas by prepaid cards that can be inserted into the connection equipment to initiate gas flow.

We entered into agreements with the Xi'an International Port Administrative Committee (the Port Committee) and the town of Tangyu, China, in April 2008 and October 2008, respectively, to provide natural gas to local residents and businesses. The international port project is estimated to involve the development of approximately 13.5 square miles of business district and the investment of up to \$30 million over the next several years, based on the Port Committee's planning schedule. The Tangyu project involves supplying

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natural gas to potentially 50,000 residential and commercial users at a tourist site undergoing development and expansion. Our agreement with the Port Committee is currently being challenged by the Xi'an Municipal Administration Commission for violating an exclusive agreement between the municipal government and Qin Hua Gas Company, one of our major competitors in our pipeline natural gas business. We disagree with the Xi'an Municipal Administration Commission's assessment and are currently in negotiations with it to resolve its assessment.

## **Our Liquefied Natural Gas ( LNG ) Project**

In September 2007, we began the construction of an LNG processing and distribution plant in Jingbian, Shaanxi province (the LNG Project ). We estimate that the LNG Project will cost approximately \$45 million (RMB309 million), a portion of which was funded by funds raised through the sale of senior notes to Abax, and the remainder of which will be funded by our cash flows from operations. We believe we have obtained all the required permits and approvals to build the LNG plant.

During 2008, we made significant progress towards completing the LNG Project and spent approximately \$20 million in constructing our LNG facility, acquiring technology licenses, prepaying for equipment purchases and acquiring land use rights. We believe that adding LNG to our product offerings will expand our geographic sales footprint and improve our revenues and profitability as well as diversify our revenue and profit structure. The facility construction work is expected to be completed in October 2009, and processing equipment installation and testing is expected to be completed in December 2009. We anticipate commencing commercial operation during the first quarter of 2010 and we anticipate purchasing transport tankers for our LNG facility during the fourth quarter of 2010.

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## THE OFFERING

Common stock offered by us

shares

Over-allotment option

shares

Common stock to be outstanding after this offering

shares ( shares if over-allotment option is exercised in full)

Use of proceeds

We estimate that the net proceeds from this offering, after deducting underwriting discounts and commissions and estimated offering expenses payable by us, will be approximately \$ million. We intend to apply all net proceeds of this offering to the construction of our LNG facility, the acquisition of eight CNG fueling stations, the purchase of eight CNG trucks to transport CNG and the establishment of the Joint Venture Company with Kunlun as well as for general working capital purposes. See Use of Proceeds.

Risk Factors

See Risk Factors beginning on page S-10 for a discussion of factors you should consider before purchasing shares of our common stock.

Nasdaq Global Market Symbol

CHNG

The above information is based upon 14,600,154 shares of our common stock outstanding as of August 20, 2009. Unless otherwise indicated, the number of shares of common stock presented in this prospectus supplement excludes the following:

318,850 shares of our common stock issuable upon exercise of options outstanding under our employee stock option plan as of August 20, 2009, at a weighted-average exercise price of \$4.90;

1,141,165 shares of our common stock available for future issuance as of August 20, 2009 for future grant or issuance pursuant to our employee stock option plan;

1,833,654 shares of our common stock issuable upon exercise of outstanding warrants as of August 20, 2009, at a weighted-average exercise price of \$8.93; and

shares of our common stock that may be purchased by the underwriters to cover over-allotments, if any.

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*The following table sets forth our summary consolidated financial data as of the dates and for the periods indicated. The consolidated statement of operations for each of the years in the three-year period ended December 31, 2008, have been derived from our audited financial statements, which are incorporated by reference into this prospectus supplement and accompanying prospectus. The consolidated statement of operations data for each of the six month periods ended June 30, 2009 and 2008, and the balance sheet data as of June 30, 2009, have been derived from our unaudited financial statements, which are also incorporated by reference into this prospectus supplement and accompanying prospectus and which include, in the opinion of management, all adjustments, consisting of normal, recurring adjustments, necessary for a fair presentation of such data. You should read this summary of consolidated financial data with the sections entitled Management's Discussion and Analysis of Financial Condition and Results of Operations and our consolidated financial statements and the related notes, each incorporated by reference into this prospectus supplement and accompanying prospectus. These operating results are not necessarily indicative of our operating results for any future period.*

**Consolidated Statement of Operations Data:**

	Six Months Ended June 30, (Unaudited)		Year Ended December 31,		
	2009	2008	2008	2007	2006
<b>STATEMENT OF OPERATIONS:</b>					
<b>Revenue</b>					
Natural gas revenue	\$30,686,498	\$25,140,185	\$55,746,893	\$28,278,033	\$13,713,145
Gasoline revenue	2,807,414	2,278,847	4,616,052	38,486	
Construction/installation and other	5,776,274	3,497,128	7,357,714	7,075,534	5,115,645
<b>Total revenue</b>	<b>39,270,186</b>	<b>30,916,160</b>	<b>67,720,659</b>	<b>35,392,053</b>	<b>18,828,790</b>
<b>Cost of revenue</b>					
Natural gas cost	14,237,447	13,396,743	27,234,508	14,838,997	7,663,060
Gasoline cost	2,659,809	2,123,015	4,277,458	34,747	
Construction/installation and other	2,461,088	1,642,163	3,469,671	3,151,331	2,054,940
<b>Total cost of revenue</b>	<b>19,358,344</b>	<b>17,161,921</b>	<b>34,981,637</b>	<b>18,025,075</b>	<b>9,718,000</b>
<b>Gross profit</b>	<b>19,911,842</b>	<b>13,754,239</b>	<b>32,739,022</b>	<b>17,366,978</b>	<b>9,110,790</b>
<b>Operating expenses</b>					