



山東墨龍石油機械股份有限公司

Shandong Molong Petroleum Machinery Company Limited

(a Sino-foreign joint stock limited company incorporated in the People's Republic of China with limited liability)

2005

FIRST QUARTERLY REPORT

Characteristics of the Growth Enterprise Market (“GEM”) of The Stock Exchange of Hong Kong Limited (the “Stock Exchange”)

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This report, for which the directors of Shandong Molong Petroleum Machinery Company Limited (the “Company”) collectively and individually accept full responsibility, includes particulars given in compliance with the Rules Governing the Listing of Securities on the GEM of the Stock Exchange (the “GEM Listing Rules”) for the purpose of giving information with regard to the Company. The directors of the Company (the “Directors”), having made all reasonable enquiries, confirm that, to the best of their knowledge and belief:— (1) the information contained in this report is accurate and complete in all material respects and not misleading; (2) there are no other matters the omission of which would make any statement in this report misleading; and (3) all opinions expressed in this report have been arrived at after due and careful consideration and are founded on bases and assumptions that are fair and reasonable.

HIGHLIGHTS

- Achieved a turnover of approximately RMB158,000,000 for the three months ended 31 March 2005, representing an increase in turnover of approximately RMB73,474,000 as compared with the turnover for the corresponding period in 2004.
- Accomplished a net profit of approximately RMB16,704,000 for the three months ended 31 March 2005, representing an increase in net profit of approximately RMB4,932,000 as compared with the net profit for the corresponding period in 2004.
- Earnings per share of the Group was approximately RMB3.1 cents for the three months ended 31 March 2005.
- The Directors do not recommend the payment of an interim dividend for the three months ended 31 March 2005.

FIRST QUARTERLY RESULTS (UNAUDITED)

The board ("Board") of directors ("Directors") of the Company is pleased to announce the unaudited results of the Company and its subsidiary (the "Group") for the three months ended 31 March 2005.

For the three months ended 31 March 2005, the unaudited turnover of the Group was approximately RMB158,000,000, representing a growth of approximately RMB73,474,000 or 86.9% in turnover as compared with that of the same period in 2004.

Due to the growth in turnover, the unaudited net profit of the Group for the three months ended 31 March 2005 was approximately RMB16,704,000, representing a substantial growth of approximately RMB4,932,000 or 41.9% as compared with that of the same period in 2004.

CONDENSED CONSOLIDATED PROFIT AND LOSS ACCOUNT (UNAUDITED)

For the three months ended 31 March 2005

The unaudited results of the Group for the three months ended 31 March 2005 together with the unaudited comparative figures for the corresponding period in 2004 are as follows:

	Note	Three months ended 31 March	
		2005 RMB'000	2004 RMB'000
Turnover	(2)	158,000	84,526
Cost of sales		(126,725)	(64,102)
Gross profit		31,275	20,424
Other revenue and gains		2,969	6,298
Selling and distribution costs		(4,067)	(2,259)
Administrative expenses		(4,772)	(3,176)
Other operating expenses		(1,484)	(1,080)
Profit from operating activities		23,921	20,207
Finance costs		(1,023)	(1,324)
Profit before tax		22,898	18,883
Tax	(3)	(5,562)	(6,413)
Profit before minority interests		17,336	12,470
Minority interests		(632)	(698)
Net profit from ordinary activities attributable to shareholders		16,704	11,772
Earnings per share — basic (RMB cents)	(4)	3.1	2.9

Notes:

1. **Basis of presentation**

The unaudited results of the Group have been prepared in accordance with Hong Kong Financial Reporting Standards (which also include Statements of Standard Accounting Practice and Interpretations) issued by the Hong Kong Institute of Certified Public Accountants, accounting principles generally accepted in Hong Kong and the disclosure requirements of the Hong Kong Companies Ordinance and the GEM Listing Rules.

The Company was incorporated as a joint stock company with limited liability in the People's Republic of China (the "PRC") on 30 December 2001 and its H shares were listed on the GEM (the "Listing") on 15 April 2004. On 16 August 2004, the Company became a Sino-foreign joint stock limited company.

2. **Turnover & segment information**

Turnover represents the invoiced value of goods sold, and after allowances for goods returned and trade discounts. All significant intra-group transactions have been eliminated on consolidation.

The Group's operating business is with customers based in the PRC, the United States and other countries. Each of the Group's geographical segments represents customer destinations to which the Group sells products or provides services which are subject to risks and returns that are different from those of the other geographical segments. Save as disclosed below, no further business segment information is presented as over 90% of the Group's revenue and assets relate to the sale of petroleum machineries.

By geographical area	Three months ended 31 March	
	2005	2004
	RMB'000	RMB'000
PRC	96,550	69,787
United States	19,652	12,395
Others	41,798	2,344
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Total	158,000	84,526
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3. Tax

	Three months ended 31 March	
	2005	2004
	RMB'000	RMB'000
Charge comprising PRC income tax	5,562	6,413

The Company is located in the PRC and as a result is subject to PRC corporate income tax at a rate of 33% on its assessable profits. No provision for Hong Kong profits tax has been made as the Group did not generate any assessable profits in Hong Kong during the period.

The subsidiary of the Company, namely, Weifang Molong Drilling Equipment Company Limited ("Molong Drilling Equipment") has been approved by the Ministry of Civil Affairs of Shandong Province (山東省民政廳) as a welfare (民政福利企業) enterprise and hence has been entitled to a full exemption from corporate income tax.

The Group had no significant unprovided deferred tax as at 31 March 2005 and 2004.

4. Earnings per share

The calculation of the basic earnings per share is based on the net profit attributable to shareholders of approximately RMB16,704,000 for the three months ended 31 March 2005 (2004: RMB11,772,000) and the weighted average of 540,000,000 (2004: 405,000,000) ordinary shares in issue during the period.

No diluted earnings per share amounts have been presented for the three months ended 31 March 2005 and 2004 as no diluting events existed during the relevant periods.

5. Reserves

There were no movements in reserves of the Group for the three months ended 31 March in 2005.

6. Capital commitments

As at 31 March 2005, the Group had capital commitments amounting to RMB121,108,000 (2004: RMB3,283,600).

7. Contingent liabilities

As at 31 March 2005, the Group did not have any significant contingent liabilities.

8. Interim Dividend

The Directors do not recommend the payment of an interim dividend for the three months ended 31 March 2005 (2004: Nil).

MANAGEMENT DISCUSSION AND ANALYSIS

Financial review

During the period under review, the Group achieved encouraging results. For the three months ended 31 March 2005, the Group recorded unaudited turnover of approximately RMB158,000,000 (2004: RMB84,526,000), representing an increase in turnover of approximately RMB73,474,000 or 86.9% over the corresponding period in the previous year.

Along with the growth in turnover, the Group recorded unaudited net profit attributable to shareholders of approximately RMB16,704,000 for the three months ended 31 March 2005 (2004: RMB11,772,000), representing an increase of approximately 41.9% over the corresponding period in the previous year.

Business review

During the period under review, the Group was engaged in the design, manufacture and sale of petroleum extraction machinery and related accessories. Its major products can be grouped into five categories, namely oil well pipes, oil well sucker rods, oil well pumps, oil well pumping machines and other drilling and extraction machinery accessories respectively, which are primarily used in upstream petroleum extraction engineering and are the necessary equipment in the petroleum extraction industry.

Following the implementation of the Group's strategies such as enhancement in the research and development capabilities, improvement to the existing products, expansion of sales networks, at the same time leveraging on the Group's excellent quality products and upgraded services, the Group's products have achieved strong competitive edges in the market and have recorded steadily increasing domestic and overseas sales and significant growth in turnover and profits.

During the period, the Group's domestic customers were mainly oil fields of the subsidiaries or branches of PetroChina Company Limited ("PetroChina") and China Petroleum & Chemical Corporation ("Sinopec"), including Daqing Oil Field (大慶油田), Shengli Oil Field (勝利油田), Xinjiang Oil Field (新疆油田), Zhongyuan Oil Field (中原油田), Liaohe Oil Field (遼河油田) and Changqing Oil Field (長慶油田). Overseas customers were mainly distributors in North America, the United Kingdom, Russia, France, Indonesia, Middle East, Brunei, Egypt and Syria. During the period, the Group has also successfully entered the petroleum machinery market of Algeria through the cooperation with the Gulf and West Trade Group of Lebanon, which is a subsidiary of HSC Group of France, an international trading company specialising in petroleum machinery.

Future outlook

With global oil prices standing at a high level, it is expected that demands for crude oil in the international and domestic markets will continue to increase and demands for petroleum extraction machinery industry will correspondingly continue to grow, providing substantial business opportunities to the Group.

Active research and development

In order to cope with the ever-changing market demands, the Group is dedicated in the research and development of new products, at the same time improving the quality and functions of the existing products. After entering into the “Strategic Cooperation Agreement” with Dongbei Special Steel Holding Company Limited (東北特鋼集團有限公司) last year, the quality and supply of raw materials to the Group were ensured, which helped the Group to maintain the quality of its products.

In addition, in order to enhance its research and development capability, the Group will recruit additional personnel with appropriate professional expertise, conduct product research and development by amalgamating international and domestic technology, so as to maintain the Group's leading position in the market.

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Exploration of domestic and overseas markets

During the period under review, the sales of the Group generated from the domestic market and the overseas market was approximately 61.1% and approximately 38.9% respectively.

Growing forward, the Group will continue to consolidate its existing customers base, and will hold regular promotion activities in the PRC to enhance brand awareness of the Group, at the same time will regularly visit the customers so as to maintain the good relationship with customers and to collect feedbacks and latest market information to enhance the quality of after-sale services and expand market share in the PRC.

In respect of overseas market, we believe that following further implementation of the Group's market exploration strategies such as appointment of more sales agents in strategic regions in South East Asia and the Middle East, the Group's overseas market will continue to expand, setting a solid foundation for the rapid growth of the Group's international sales.

Enhancement of production capacity

Supply of petroleum has been outpaced by demands and prices continued to rise correspondingly. With the continued extraction of new oil fields, exploration and production costs of petroleum and natural gas is expected to increase, bringing tremendous development opportunities to the petroleum extraction machinery.

The Group has long been aware of this and has continued to enhance its production capacity so as to satisfy strong market demands.

Besides consolidating its existing business, the Group will seek to capture emerging new market opportunities and develop more favorable models of operation and to create satisfactory return to shareholders.

MATERIAL ACQUISITION/DISPOSAL AND SIGNIFICANT INVESTMENT

During the period under review, the Group had no material acquisition or disposal and significant investments.

BANK FACILITIES AND PLEDGE OF ASSETS

As at 31 March 2005, the Group had bank loans amounting to RMB70,000,000 including a loan amounting to RMB15,000,000 secured by certain equipment of the Group and an unsecured loan amounting to RMB55,000,000 of the Company. In addition, the Agricultural Bank of China, CITIC Industrial Bank and Weifang Commercial Bank has granted credit facilities amounting to RMB65,000,000, RMB30,000,000 and RMB95,000,000 to the Group respectively, which have not been utilised.

EMPLOYEES

A breakdown of the number of employees of the Group by function as at 31 March 2005 were set out below:

	Three months ended 31 March	
	2005	2004
Research and development	48	40
Production	1,077	790
Quality control	78	77
Sales and marketing	52	45
Administration	158	153
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Total	1,413	1,105
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The Group keeps a close watch on the levels of the employees' remuneration and benefits and staff are rewarded on a performance related basis and in accordance with the Group's employment policy. It also offers employees training and development.

ADVANCE TO ENTITIES

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Advance to PetroChina

Trade receivables in the amount of approximately RMB29.4 million were owed from an independent party, PetroChina Company Limited and its subsidiaries (collectively, "PetroChina") as at 31 March 2005.

Advances to Sinopec

Trade receivables and note receivables in the amounts of approximately RMB28.7 million and RMB1.2 million were owed from an independent party, China Petroleum & Chemical Corporation and its subsidiaries (collectively, "Sinopec") as at 31 March 2005.

As confirmed by the Directors, the trade receivables and note receivables referred to above were resulted from the sale of the Group's products to such customers in the ordinary course of business of the Group. The trade receivables were unsecured, interest free and had a credit terms of between 30 to 150 days.

DISCLOSURE OF DIRECTORS' INTERESTS IN SHARES

As at 31 March 2005, the interest and short positions of the Directors and chief executives in the shares, underlying shares or debentures of the Company or any of its associated corporations (within the meaning of Part XV of the Securities and Futures Ordinance (the "SFO")), which will be required to be notified to the Company and the Stock Exchange pursuant to Divisions 7 and 8 of Part XV of the SFO (including interests or short positions which they are taken or deemed to have under such provisions of the SFO) or which will be required, pursuant to section 352 of the SFO, to be entered in the register referred to therein, or which will be required pursuant to Rules 5.46 to 5.68 of the GEM Listing Rules, to be notified to the Company and to the Stock Exchange, were as follows:

Long positions in shares of the Company

Name	Type of Interest	Number of domestic shares	Percentage of domestic shares	Percentage of total registered share capital
Zhang En Rong	Personal	279,517,000	69.58%	51.76%
Lin Fu Long	Personal	34,216,000	8.52%	6.34%
Zhang Yun San	Personal	30,608,000	7.62%	5.67%
Xie Xin Cang	Personal	21,410,000	5.33%	3.96%

Other than as disclosed above, none of the Directors and chief executives had any interests or short position in the shares, underlying shares or debentures of the Company or any of its associated corporations (within the meaning of Part XV of the SFO), will have to be notified to the Company and the Stock Exchange under Divisions 7 and 8 of Part XV of the SFO (including interests and short positions which they are taken or deemed to have under the SFO) or will be required pursuant to the required standard of dealings by Directors as referred to in Rule 5.46 to 5.48 of the GEM Listing Rules or section 352 the SFO to be entered in the register of interests referred to therein.

DIRECTORS' AND SUPERVISORS' RIGHTS TO ACQUIRE H SHARES OR DEBENTURES

None of the Directors and supervisors of the Company or their respective associates (as defined under the GEM Listing Rules) was granted by the Company or its subsidiaries any rights or options to acquire any shares in or debentures of the Company or had exercised any such rights as at 31 March 2005.

SHARE OPTION SCHEME

The Company does not have any share option schemes.

SUBSTANTIAL SHAREHOLDERS

As at 31 March 2005, so far as the Directors are aware, the following persons (other than Directors or chief executive of the Company) had interests or short positions in the shares and underlying shares and debentures of the Company which would fall to be disclosed to the Company under the provisions of Divisions 2 and 3 of Part XV of the SFO and required to be recorded in the register to be kept under section 336 of the SFO:

Long positions in shares

Name	Type of interests	Number of shares	Percentage of domestic shares	Percentage of H shares	Percentage of total registered capital
Zhang Xiu Lan (Note 1)	Interests of spouse	279,517,000	69.58%	—	51.76%
Li Xiu Fen (Note 2)	Interests of spouse	34,216,000	8.52%	—	6.34%
Zhang Xin Lan (Note 3)	Interests of spouse	30,608,000	7.62%	—	5.67%
Li Bao Hui (Note 4)	Interests of spouse	21,410,000	5.33%	—	3.96%
Peter Cundill & Associates (Bermuda) Ltd. (Note 5)	Investment manager	63,700,000	—	46.07%	11.80%

Note 1: Zhang Xiu Lan is the wife of Zhang En Rong and is taken to be interested in the 279,517,000 domestic shares held by Zhang En Rong under the SFO.

Note 2: Li Xiu Fen is the wife of Lin Fu Long and is taken to be interested in the 34,216,000 domestic shares held by Lin Fu Long under the SFO.

Note 3: Zhang Xin Lan is the wife of Zhang Yun San and is taken to be interested in the 30,608,000 domestic shares held by Zhang Yun San under the SFO.

Note 4: Li Bao Hui is the wife of Xie Xin Cang and is taken to be interested in the 21,410,000 domestic shares held by Xie Xin Cang under the SFO.

Note 5: Interests in H shares.

SUBSTANTIAL SHAREHOLDERS (CONTINUED)

Save as disclosed above, so far as the Directors are aware, there are no other persons not being a Director or chief executive of the Company who had interests or short positions in the shares, underlying shares or debentures of the Company which would fall to be disclosed to the Company under the provisions of Divisions 2 and 3 of Part XV of the SFO and required to be recorded in the register required to be kept under section 336 of the SFO.

COMPETING INTERESTS

None of the Directors or the management shareholders of the Company and their respective associates (as defined in the GEM Listing Rules) had any interest in a business which competes or may compete with the business of the Group.

COMPLIANCE ADVISER'S INTEREST

As updated and notified by the Company's Compliance Adviser, Deloitte & Touche Corporate Finance Limited (the "Compliance Adviser"), neither the Compliance Adviser, nor its directors, employees or associates (as defined under the GEM Listing Rules) had any interest in the share capital of the Company as at 31 March 2005 pursuant to Rule 6.36 of the GEM Listing Rules.

Pursuant to an agreement dated 29 March 2004 entered into between the Company and the Compliance Adviser, the Compliance Adviser will receive a fee for acting as the Company's retained sponsor for the period from 15 April 2004 to 31 December 2006 or until the agreement is terminated in accordance with the terms and conditions set out therein.

AUDIT COMMITTEE

The Company established an audit committee on 20 March 2004 with written terms of reference in compliance with the requirements as set out in Rules 5.28 and 5.29 of the GEM Listing Rules. The primary duties of the audit committee are to review and provide supervision over the financial reporting procedures and internal control system of the Group. The audit committee comprises the three independent non-executive Directors, namely Mr. Qin Xue Chang, Mr. Yan Yi Zhuang and Mr. Loke Yu alias Loke Hoi Lam. Mr. Qin Xue Chang is the chairman of the audit committee.

The audit committee has reviewed with the management the accounting principles and practices adopted by the Group and discussed internal controls and financial reporting matters, including a review of the unaudited results of the Group for the three months ended 31 March 2005.

PURCHASE, SALE OR REDEMPTION OF SECURITIES

Neither the Company nor its subsidiary has purchased, sold or redeemed any listed securities of the Company during the three months ended 31 March 2005.

12 DIRECTORS

As at the date of this report, the executive Directors of the Company are Mr. Zhang En Rong, Mr. Zhang Yun San, Mr. Lin Fu Long and Mr. Xie Xin Cang, the non-executive Directors are Mr. Chen Jian Xiong and Mr. Wang Ping and the independent non-executive Directors are Mr. Qin Xue Chang, Mr. Yan Yi Zhuang and Mr. Loke Yu alias Loke Hoi Lam.

By order of the Board

Shandong Molong Petroleum Machinery Company Limited

Zhang En Rong

Chairman

25 April 2005

Shandong, the PRC