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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)

(Stock Code: 8261)

CONTINUING CONNECTED TRANSACTIONS

On 12 July 2006, Molong Drilling Equipment and Ya Long Oil Well Pump entered into the Co-operative Agreement for the supply of oil well pumps and related accessories (including but not limited to pump pipes, plunger assembly, pump rods, snap ring, rods, polished rod grips, oil well pipe couplings, standing valve assembly, stationary valve seats and draining valve covers) by Molong Drilling Equipment to Ya Long Oil Well Pump. It has been agreed that the supply price of the oil well pumps charged by Molong Drilling Equipment to Ya Long Oil Well Pump will make reference to the then prevailing market price from time to time. The Co-operative Agreement has become effective from 1 January 2006 and remain in force up to 31 December 2007.

Zhang En Rong and Zhang Yun San are connected persons of the Company pursuant to Rule 20.11(1) of the GEM Listing Rules. Pursuant to Rule 20.11(4)(b) of the GEM Listing Rules, as Zhang Yun Qi is the son of Zhang En Rong and the brother of Zhang Yun San, he is regarded as the associate of the Directors and accordingly, is also a connected person of the Company. As Zhang Yun Qi is interested in approximately 53.15% of the equity interest in Maolong Machinery, Maolong Machinery is deemed to be a connected person of the Company.

Given that Ya Long Oil Well Pump is owned as to 30% by Maolong Machinery and Zhang Yun Qi is indirectly interested so as to exercise or control the exercise of 30% of the voting power at general meeting of Ya Long Oil Well Pump, Ya Long Oil Well Pump is deemed to be a connected person of the Company.

As certain applicable percentage ratios are more than 0.1% but less than 2.5%, the transactions under the Co-operative Agreement will constitute continuing connected transactions of the Company under the GEM Listing Rules and will be subject to the requirements of reporting and announcement as required by Rules 20.45, 20.46 and 20.47 of the GEM Listing Rules but exempt from the requirements of independent shareholders' approval under Rule 20.48 of the GEM Listing Rules.

CO-OPERATIVE AGREEMENT

Date of the Co-operative Agreement

12 July 2006

Parties to the Oil Well Pipe and Casing Billets Supply Agreement

Seller: Molong Drilling Equipment, a non wholly-owned subsidiary of the Company, is principally engaged in the business of oil well sucker rods, oil well pumps and related accessories

Purchaser: Ya Long Oil Well Pump, a company principally engaged in the business of oil well pumps and related accessories

Oil well pumps and their accessories to be supplied to Ya Long Oil Well Pump

Pursuant to the Co-operative Agreement, Molong Drilling Equipment has agreed to sell and Ya Long Oil Well Pump has agreed to purchase oil well pumps and related accessories in accordance with the following terms:

Parties: Molong Drilling Equipment as seller

Ya Long Oil Well Pump as purchaser

Subject: Pursuant to the Co-operative Agreement, Molong Drilling Equipment has agreed to supply to Ya Long Oil Well Pump oil well pumps and related accessories (including but not limited to pump pipes, plunger assembly, pump rods, snap ring, rods, polished rod grips, oil well pipe couplings, standing valve assembly, stationary valve seats, draining valve covers).

Term: The Co-operative Agreement has been effective from 1 January 2006 to 31 December 2007 (both dates inclusive).

Price: Pursuant to the Co-operative Agreement, it has been agreed that the supply price of oil well pumps charged by Molong Drilling Equipment to Ya Long Oil Well Pump would make reference to the then prevailing market price from time to time.

Historical figures: For the year ended 31 December 2004, the total sales of the oil well pumps and related accessories by the Group to Ya Long Oil Well Pump were approximately RMB896,000 (equivalent to approximately HK\$861,500). There were no sales of oil well pumps and accessories by the Group to Ya Long Oil Well Pump for the year ended 31 December 2005 on the basis that (i) the total sales of oil well pumps and related accessories by the Group to Ya Long Oil Well Pump were small for the year ended 31 December 2004; (ii) the location of Ya Long Oil Well Pump was far from the Group geographically; and (iii) the limitation of sales volume by the small production capacity of oil well pumps and accessories by the Group for the year ended 31 December 2005. Therefore, the Group did not sell any oil well pumps and related accessories to Ya Long Oil Well Pump for the year ended 31 December 2005.

Other significant terms:

- (1) Ya Long Oil Well Pump shall make payments to Molong Drilling Equipment in cash upon delivery;
- (2) Ya Long Oil Well Pump shall inspect the oil well pumps and related accessories in accordance with the PRC national standards. In the event that defects are found by Ya Long Oil Well Pump, Molong Drilling Equipment has agreed to exchange them with the qualified oil well pumps and related accessories to Ya Long Oil Well Pump; and
- (3) The parties will enter into separate agreements from time to time in respect of the actual market price and quantities of oil well pumps and related accessories to be transacted.

The Oil Well Pump Annual Cap Amounts

The Directors expect that the maximum aggregate annual value of sales of oil well pumps and related accessories by Molong Drilling Equipment to Ya Long Oil Well Pump under the Co-operative Agreement is estimated not to exceed RMB14,500,000 (equivalent to approximately HK\$13,942,000) and RMB19,000,000 (equivalent to approximately HK\$18,269,000) (each, an “**Oil Well Pump Annual Cap Amount**”) respectively for each of the two years ending 31 December 2007, which represents the target supplies agreed between Molong Drilling Equipment and Ya Long Oil Well Pump.

The Oil Well Pump Annual Cap Amount is reached on the basis of (i) the expected demand of Ya Long Oil Well Pump for the oil well pumps and related accessories for each of the 2 years ending 31 December 2007; (ii) the oil well pump and related accessories production capacity of Molong Drilling Equipment for each of the 2 years ending 31 December 2007; and (iii) a buffer of not more than 5% in excess of Molong Drilling Equipment’s expected total value of the supplies to Ya Long Oil Well Pump.

The significant increase in Oil Well Pump Annual Cap Amount for the year ended 31 December 2006, as compared with the historical figures for each of two years ended 31 December 2005, was because (i) the Group invested approximately RMB2,500,000 (or approximately HK\$2,404,000) to purchase 7 sets of production facilities at the end of 2005 which enhanced the production capacity of oil well pump and accessories by Molong Drilling Equipment for the year ended 31 December 2006. For instance, after the production enhancement, Molong Drilling Equipment expects to produce 12,000 pump pipes annually, as compared with 4000 pump pipes for the year ended 31 December 2005. Due to the increase in the production capacity, Molong Drilling Equipment has been eager to explore new markets and strengthen the business relationships with existing customers (including Ya Long Oil Well Pump); (ii) Ya Long Oil Well Pump increased its production capacity and expanded its market scale for the year ended 31 December 2006. As compared with other suppliers, due to the superior quality of products and timely fulfillment of orders by Molong Drilling Equipment, Ya Long Oil Well Pump would like to develop closer business relationship with Molong Drilling Equipment. It has expected to shift orders from other suppliers to Molong Drilling Equipment. Ya Long Oil Well Pump has therefore significantly increased its expected purchases from Molong Drilling Equipment for the year ended 31 December 2006.

The projected increase of 31% in the Oil Well Pump Annual Cap Amount for the year ending 31 December 2007 is determined on the basis of the increase in the turnover of Ya Long Oil Well Pump for the year ended 31 December 2005 by 35% and the corresponding projected increase in the turnover and demand for the oil well pump and related accessories by Ya Long Oil Well Pump for the year ending 31 December 2007.

Reasons for the transaction

The Board believes that since Ya Long Oil Well Pump has the local expertise and sales and marketing advantage in Kelamayi Oilfield (克拉瑪依油田), the co-operation with Ya Long Oil Well Pump to explore the local market at Kelamayi Oilfield would be beneficial to the Group and the shareholders as a whole. In addition, as the annual volume of oil well pumps and related accessories produced by Molong Drilling Equipment has increased and is expected to increase, the exploration of market such as Kelamayi Oilfield would enhance the sales of Molong Drilling Equipment.

The Board (including the independent non-executive Directors) also believes that the terms and conditions of the Co-operative Agreement have been negotiated on an arm's length basis, on normal commercial terms which are no less favourable than terms available to independent third parties and are fair and reasonable. In this connection, the Board (including the independent non-executive Directors) considers that the Co-operative Agreement is made in the ordinary and usual course of business of Molong Drilling Equipment and the terms of the Co-operative Agreement would be beneficial to the operation of Molong Drilling Equipment in terms of supply of oil well pumps and related accessories and are in the interest of the Company and its Shareholders, taken as a whole.

Compliance requirements

Zhang En Rong and Zhang Yun San are connected persons of the Company pursuant to Rule 20.11(1) of the GEM Listing Rules. Pursuant to Rule 20.11(4)(b) of the GEM Listing Rules, as Zhang Yun Qi is the son of Zhang En Rong and the brother of Zhang Yun San, he is regarded as the associate of the Directors and accordingly, is also a connected person of the Company. As Zhang Yun Qi is interested in approximately 53.15% of the equity interest in Maolong Machinery, Maolong Machinery is deemed to be a connected person of the Company. Maolong Machinery was also deemed to be a connected person of the Company at the time of listing of the Company on the GEM in 2004.

Given that Ya Long Oil Well Pump is owned as to 30% by Maolong Machinery and Zhang Yun Qi is indirectly interested so as to exercise or control the exercise of 30% of the voting power at general meeting of Ya Long Oil Well Pump, Ya Long Oil Well Pump is deemed to be a connected person of the Company.

As certain applicable percentage ratios are more than 0.1% but less than 2.5%, the transactions under the Co-operative Agreement will constitute continuing connected transactions of the Company under the GEM Listing Rules and will be subject to the requirements of reporting and announcement as required by Rules 20.45, 20.46 and 20.47 of

the GEM Listing Rules but exempt from the requirements of independent shareholders' approval under Rule 20.48 of the GEM Listing Rules. Relevant details will be included in the next published annual report and accounts of the Company in accordance with the GEM Listing Rule 20.45.

DEFINITIONS

“Board”	the board of directors of the Company
“Company”	山東墨龍石油機械股份有限公司 (Shandong Molong Petroleum Machinery Company Limited)
“Co-operative Agreement”	An agreement entered into between Molong Drilling Equipment and Ya Long Oil Well Pipe on 12 July 2006 in relation to the supply of oil well pumps and related accessories by Molong Drilling Equipment to Ya Long Oil Well Pipe
“Director(s)”	director(s) of the Company
“GEM”	the Growth Enterprise Market of The Stock Exchange of Hong Kong Limited
“GEM Listing Rules”	the Rules Governing the Listing of Securities on GEM
“Group”	the Company and its subsidiaries
“Maolong Machinery”	壽光懋隆機械電氣有限公司 (Shouguang Maolong Machinery Company Limited), a limited liability company established in the PRC. The shareholders of Maolong Machinery are Zhang Zhi Jun (張志軍), Zhang Guang He 張光和, Zhang Jin Sheng 張金生, Guo Huan Ran 國煥然, Ren Chun Qing 任春清, Li Bao Hui 李寶惠, Zhang Jin Chuan 張金川, Zhang Yun Qi 張雲起, Lin Fu Long 林福龍, Zhang Yun San 張雲三, Xie Xin Cang 謝新倉, Liu Yun Long 劉雲龍 and Cui Huan You 崔煥友, who are interested in 1.96%, 2.10%, 1.86%, 4.85%, 1.86%, 6.11%, 6.46%, 53.15%, 6.46%, 6.46%, 1.94%, 4.85% and 1.94% respectively of the registered capital of Maolong Machinery. Among the shareholders of Maolong Machinery, (i) Lin Fu Long 林福龍, Zhang Yun San 張雲三, Xie Xin Cang 謝新倉, Liu Yun Long 劉雲龍 and Cui Huan You 崔煥友 are also shareholders of the Company who are interested in 5.28%, 4.72%, 3.30%, 2.26% and 1.43% respectively of the registered capital of the Company; (ii) Lin Fu Long 林福龍, Zhang Yun San 張雲三 and Xie Xin Cang 謝新倉 are Directors; and (iii) Li Bao Hui 李寶惠 is the supervisor of the Company and the wife of Xie Xin Cang 謝新倉

“Molong Drilling Equipment”	濰坊墨龍鑽採設備有限公司 (Weifang Molong Drilling Equipment Company Limited), a limited liability company established in the PRC on 29 September 2004 with a registered capital of RMB6,000,000, which is owned as to 90% by the Company and 10% by Shangkok Town People’s Government
“PRC” or “China”	the People’s Republic of China and for the purpose of this announcement excludes Hong Kong, Macau Special Administrative Region and Taiwan
“RMB”	Renminbi, the lawful currency of the PRC
“Shareholders”	shareholders of the Company
“Stock Exchange”	The Stock Exchange of Hong Kong Limited
“Ya Long Oil Well Pump”	克拉瑪依亞龍石油泵有限公司 (Kelamayi Ya Long Oil Well Pump Company Limited), a limited liability company established in the PRC in which Maolong Machinery and 克拉瑪依亞東有限責任公司 (Kelamayi Ya Dong Company Limited) is interested in 30% and 70%, respectively, of its registered capital. Kelamayi Ya Dong Company Limited is an independent third party.

Unless otherwise defined, an exchange rate of HK\$1.00 = RMB1.04 is adopted in this announcement, for illustration purposes only.

By Order of the Board
Shandong Molong Petroleum Machinery Company Limited
Chan Wing Nang, Billy
Company Secretary

PRC, 12 July 2006

The announcement, for which the Directors of the Company collectively and individually accept full responsibility, includes particulars given in compliance with the Rules Governing the Listing of Securities on the Growth Enterprise Market of The Stock Exchange of Hong Kong Limited for the purpose of giving information with regard to 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 announcement 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 announcement misleading; and (3) all opinions expressed in this announcement have been arrived at after due and careful consideration and are founded on bases and assumptions that are fair and reasonable.

As at the date of this announcement, the executive directors of the Company are Mr. Zhang En Rong, Mr. Lin Fu Long, Mr. Zhang Yun San and Mr. Xie Xin Cang, the non-executive directors of the Company 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.

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* *for identification purpose only*