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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 TRANSACTION

Reference is made to the prospectus of the Company dated 30 April 2004 which states that the Company and Molong Equipment entered into the Casting Supply Agreement on 20 March 2004. Under the Casting Supply Agreement, Molong Equipment has agreed to supply casting products to the Company for a term from 15 April 2004 to 31 December 2006.

As the term of the Casting Supply Agreement will expire on 31 December 2006, the Company and Molong Equipment entered into the Supplemental Agreement on 22 September 2006 for the purpose of extending the term of the Casting Supply Agreement to 31 December 2007 and providing for the Casting Annual Caps.

Due to the entering into of the Supplemental Agreement, the Company is required to take appropriate steps to comply with Chapter 20 of the GEM Listing Rules.

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 Molong Equipment is a subsidiary of Maolong Machinery, Molong Equipment is deemed to be a connected person of the Company. Molong Equipment was also deemed to be a connected person of the Company at the time of listing of the Company on the GEM in 2004.

As certain applicable percentage ratios calculated on an annual basis are more than 2.5%, the CCT Transaction constitutes a non-exempt continuing connected transaction of the Company under Rule 20.35 of GEM Listing Rules. The CCT Transaction is not only subject to the reporting and announcement requirements under GEM Listing Rules 20.45 to 20.47 but also require the approval of the Independent Shareholders under GEM Listing Rule 20.48.

The terms and conditions of the CCT Transaction have been negotiated on an arm's length basis and are on normal commercial terms. The Board (including the independent non-executive Directors) considers the CCT Transaction to be fair and reasonable, and are in the interests of the Company and the Shareholders, taken as a whole.

The Company will convene an EGM for the purpose of seeking the approval of Independent Shareholders for the CCT Transaction and the Casting Annual Caps. As such, Zhang En Rong, Lin Fu Long, Zhang Yun San, Xie Xin Cang, Liu Yun Long holding approximately 58.7% of the equity interests of the Company and their respective associates (as the case may be) will abstain from voting in respect of above resolution. Zhang En Rong, Lin Fu Long, Zhang Yun San, Xie Xin Cang and Liu Yun Long will abstain from voting in respect of the above resolution because (i) each of them (excluding Zhang En Rong), being the shareholders of the Company, is interested in the equity interests of Maolong Machinery; (ii) the son of Zhang En Rong, Zhang Yun Qi, is interested in 53.15% of the registered capital of Maolong Machinery; and (iii) Molong Equipment is a subsidiary of Maolong Machinery.

The Independent Board Committee will be established to advise the Independent Shareholders in relation to the CCT Transaction and the Casting Annual Caps. China Everbright Capital Limited has been appointed as the Independent Financial Adviser to advise the Independent Board Committee and the Independent Shareholders in relation to the transactions under the Supplemental Agreement and the Casting Annual Caps.

A circular containing, inter alia, further details of the CCT Transaction and the Casting Annual Caps, the letter from the Independent Board Committee to the Independent Shareholders, letter of advice from the Independent Financial Adviser to the Independent Board Committee and Independent Shareholders together with the notice of EGM will be despatched to the Shareholders as soon as practicable.

Particulars of the CCT Transaction are set forth below, and will also be disclosed in the Company's next annual report and accounts.

SUPPLEMENTAL AGREEMENT

Reference is made to the prospectus of the Company dated 30 April 2004 which states that the Company and Molong Equipment entered into the Casting Supply Agreement on 20 March 2004. Under the Casting Supply Agreement, Molong Equipment has agreed to supply casting products to the Company for a term from 15 April 2004 to 31 December 2006.

As the term of the Casting Supply Agreement will expire on 31 December 2006, the Company and Molong Equipment entered into the Supplemental Agreement on 22 September 2006 for the purpose of extending the term of the Casting Supply Agreement to 31 December 2007 and providing for the Casting Annual Caps.

The Casting Annual Caps

For each of the three years ended 31 December 2005, the aggregate purchases of casting made by the Company from Molong Equipment amounted to approximately RMB18,629,000 (or equivalent to approximately HK\$17,913,000), RMB30,408,000 (or equivalent to approximately HK\$29,238,000) and approximately RMB40,760,870 (or equivalent to approximately HK\$39,193,000), respectively.

The reason for the increase of the purchases of casting made by the Company during the three years ended 31 December 2005 was that overseas customers increased their purchase orders for the mud pump steel sleeves and valves manufactured by the Company. The production of mud pump steel sleeves and valves requires casting.

The Directors expect that the annual aggregate purchases of casting from Molong Equipment will not exceed RMB70,000,000 (or equivalent to approximately HK\$67,307,000) and RMB105,000,000 (or equivalent to approximately HK\$100,962,000) (each, a “**Casting Annual Cap**”) respectively for each of the two years ending 31 December 2007.

The Casting Annual Cap for the year ending 31 December 2006 is determined on the basis that the actual aggregate purchases of casting from Molong Equipment have exceeded RMB38,000,000 for the seven months ended 31 July 2006. Therefore, the Directors expect that the annual aggregate purchases of casting from Molong Equipment will not exceed RMB70,000,000.

The Casting Annual Cap for the year ending 31 December 2007 is determined by reference to (i) the average historical growth of the purchase of casting by the Company from Molong Equipment by approximately 50% for the two years ended 31 December 2005; and (ii) the annual growth rate of the turnover of the Company by over 50% for the three years ended 31 December 2005.

Reason for the CCT Transaction

The castings supplied by Molong Equipment are used for the production of exported products of the Group such as steel sleeves and valves. In this regard, the Board considers that the high quality products supplied by Molong Equipment would guarantee the more stringent requirement of exported products. In addition, since Molong Equipment supplies the goods in a timely manner and at the price which is not higher than that offered by independent third parties, the Company shall benefit from continuing purchases of castings from Molong Equipment.

GEM Listing Rules requirements

Due to the entering into of the Supplemental Agreement for extending the term of the Casting Supply Agreement the Company is required to take appropriate steps to comply with Chapter 20 of the GEM Listing Rules.

Zhang En Rong and Zhang Yun San are connected persons of the Company pursuant to Rule 20.11(1) of the GEM Listing Rules because they are directors of the Company. 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 Molong Equipment is a subsidiary of Maolong Machinery, Molong Equipment is also deemed to be a connected person of the Company by the Stock Exchange. Molong Equipment was also deemed to be a connected person of the Company at the time of listing of the Company on the GEM in 2004.

As certain applicable percentage ratios calculated on an annual basis are more than 2.5%, the CCT Transaction constitutes a non-exempt continuing connected transaction of the Company under GEM Listing Rule 20.35. The CCT Transaction is not only subject to the reporting and announcement requirements under GEM Listing Rules 20.45 to 20.47 but also require the approval of the Independent Shareholders under GEM Listing Rule 20.48.

The terms and conditions of the CCT Transaction have been negotiated on an arm's length basis and are on normal commercial terms. The Board (including the independent non-executive Directors) considers the CCT Transaction to be fair and reasonable, and is in the interests of the Company and the Shareholders, taken as a whole.

The Company will convene an EGM for the purpose of seeking the approvals of Independent Shareholders for the CCT Transaction and the Casting Annual Caps. As such, Zhang En Rong, Lin Fu Long, Zhang Yun San, Xie Xin Cang, Liu Yun Long holding approximately 58.7% of the equity interests of the Company and their respective associates (as the case may be) will abstain from voting in respect of above resolution. Zhang En Rong, Lin Fu Long, Zhang Yun San, Xie Xin Cang and Liu Yun Long will abstain from voting in respect of the above resolution because (1) each of them (excluding Zhang En Rong), being the shareholders of the Company, is interested in the equity interests of Maolong Machinery; (2) the son of Zhang En Rong, Zhang Yun Qi, is interested in 53.15% of the registered capital of Maolong Machinery; and (3) Molong Equipment is a subsidiary of Maolong Machinery. Mr. Fang, Zhang Yun Qi, Molong Equipment and Maolong Machinery do not hold any Shares.

The Independent Board Committee will be established to advise the Independent Shareholders in relation to the CCT Transaction and the Casting Annual Caps. China Everbright Capital Limited has been appointed as the Independent Financial Adviser to advise the Independent Board Committee and the Independent Shareholders in relation to the transactions under the Supplemental Agreement and the Casting Annual Caps.

A circular containing, inter alia, further details of the CCT Transaction and the Casting Annual Caps, the letter from the Independent Board Committee to the Independent Shareholders, letter of advice from the Independent Financial Adviser to the Independent Board Committee and Independent Shareholders together with the notice of EGM will be despatched to the Shareholders as soon as practicable.

Particulars of the CCT Transaction will also be disclosed in the Company's next annual report and accounts.

General

The Group is principally engaged in the design, manufacture and sales of petroleum drilling and extracting machinery and related accessories. Molong Equipment is principally engaged in the production and sales of tip thickened oil well pipes, electrical equipment set and castings. Maolong Machinery is principally engaged in the production and sale of oil equipment and accessories, high pressure isolation switches and high pressure electric appliances, related equipment sets and processing and sale of alloy accessories.

DEFINITIONS

“Board”	the board of directors of the Company
“Casting Annual Caps”	the annual caps contemplated under the Supplemental Agreement
“Casting Supply Agreement”	an agreement entered into between the Company and Molong Equipment on 20 March 2004 (as supplemented by an agreement on 20 December 2005) in relation to the supply of casting products to the Company by Molong Equipment
“CCT Transaction”	the transactions contemplated under the Casting Supply Agreement and the Supplemental Agreement
“Company”	山東墨龍石油機械股份有限公司 (Shandong Molong Petroleum Machinery Company Limited)
“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
“Independent Board Committee”	an independent board committee comprising of all the independent non-executive Directors

“Independent Financial Adviser”	China Everbright Capital Limited, a corporation licensed to conduct type 1 (dealing in securities), type 4 (advising on securities) and type 6 (advising on corporate finance) regulated activities under the Securities and Futures Ordinance (Chapter 571) of the Laws of Hong Kong.
“Independent Shareholders”	the shareholders of the Company other than Molong Equipment and its associates (as such term is defined in the GEM Listing Rules)
“Maolong Machinery”	<p>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 張錦生, 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</p>
“Molong Equipment”	<p>壽光墨龍機電設備有限公司 (Shouguang Molong Electromechanical Equipment Company Limited), a Sino-foreign joint venture established in the PRC in which Maolong Machinery and Mr. Fang are interested in 75% and 25% respectively of its registered capital. Molong Equipment is principally engaged in the production and sales of tip thickened oil well pipes, electrical equipment set and castings</p>
“Mr. Fang”	<p>方亨超 (Luke Fang), who is one of the shareholders of Molong Equipment, is not connected with any of the directors, supervisors, chief executive and substantial shareholders of the Company or any of its subsidiaries or any of their respective associates.</p>

“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
“Supplemental Agreement”	a supplemental agreement dated 22 September 2006 and entered into between the Company and Molong Equipment pursuant to which Molong Equipment and the Company agreed to extend the term of the Casting Supply Agreement to 31 December 2007 and providing for the Casting Annual Caps

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, 25 September 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*