

THIS CIRCULAR IS IMPORTANT AND REQUIRES YOUR IMMEDIATE ATTENTION

If you are in any doubt as to any aspect of this circular or as to the action to be taken, you should consult your stockbroker or other registered dealer in securities, bank manager, solicitor, professional accountant or other professional adviser.

If you have sold or transferred all your H shares in **Shandong Molong Petroleum Machinery Company Limited** (the “Company”), you should at once hand this circular and the accompanying forms of proxy and reply slips to the purchaser or the transferee or to the bank, stockbroker or other agent through whom the sale was effected for transmission to the purchaser or the transferee.

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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)

**PROPOSED VOLUNTARY WITHDRAWAL OF LISTING
ON THE GROWTH ENTERPRISE MARKET OF
THE STOCK EXCHANGE OF HONG KONG LIMITED,
PROPOSED LISTING ON THE MAIN BOARD OF
THE STOCK EXCHANGE OF HONG KONG LIMITED
BY WAY OF INTRODUCTION,
PROPOSED REDUCTION OF THE MINIMUM NOTICE PERIOD
IN RESPECT OF THE PROPOSED WITHDRAWAL,
PROPOSED GRANT OF NEW GENERAL MANDATE
AND PROPOSED REVOCATION OF EXISTING GENERAL MANDATE,
PROPOSED AMENDMENTS TO THE ARTICLES
OF ASSOCIATION OF THE COMPANY,
CONTINUING CONNECTED TRANSACTION,
PROPOSED DECLARATION OF INTERIM DIVIDEND AND
CLOSURE OF REGISTER OF MEMBERS**

Sponsor



Guotai Junan Capital Limited

A letter from the board of directors of the Company dated 19 October 2006 is set out on pages 7 to 20 of this circular.

The notices convening the EGM and the separate Class Meetings of holders of H Shares and holders of Domestic Shares to be held at No. 99 Beihai Road, Shouguang City, Shandong Province, the People's Republic of China on 5 December 2006 at 9:00 a.m., 10:00 a.m. and 11:00 a.m. respectively are set out on pages 37 to 50 of this circular.

Whether or not you are able to attend the meetings, you are reminded to complete the forms of proxy enclosed with this circular, in accordance with the instructions printed thereon and send the relevant forms of proxy to the registered office of the Company at No. 99 Beihai Road, Shouguang City, Shandong Province, the People's Republic of China (for holders of Domestic Shares), or to the office of the Company's H Share Registrar, Tricor Investor Services Limited on the 26th Floor, Tesbury Centre, 28 Queen's Road East, Hong Kong (for holders of H Shares) as soon as practicable and in any event not later than 24 hours before the respective time appointed for the holding of the separate Class Meetings of holders of H Shares and holders of Domestic Shares and the EGM. Completion and return of the relevant forms of proxy will not preclude you from attending and voting in person at the meetings or at any adjourned meetings should you so wish.

Reply slips for each of the EGM and the separate Class Meetings have also been enclosed. You are reminded to complete and sign the relevant reply slips (if you are entitled to attend the relevant meetings) and return the signed slips to the Company's registered office (for holders of Domestic Shares), or to the office of the Company's H Share Registrar, Tricor Investor Services Limited on the 26th Floor, Tesbury Centre, 28 Queen's Road East, Hong Kong (for holders of H Shares) on or before 14 November 2006 in accordance with the instructions printed thereon.

This circular will remain on the “Latest Company Announcements” page of the GEM website at “www.hkgem.com” for 7 days from the day of its posting.

* For identification purpose only

19 October 2006

CHARACTERISTICS OF GEM

GEM has been established as a market designed to accommodate companies to which a high investment risk may be attached. In particular, companies may list on GEM with neither a track record of profitability nor any obligation to forecast future profitability. Furthermore, there may be risks arising out of the emerging nature of companies listed on GEM and the business sectors or countries in which the companies operate. Prospective investors should be aware of the potential risks of investing in such companies and should make the decision to invest only after due and careful consideration. The greater risk profile and other characteristics of GEM mean that it is a market more suited to professional and other sophisticated investors.

Given the emerging nature of companies listed on GEM, there is a risk that securities traded on GEM may be more susceptible to high market volatility than securities traded on the Main Board and no assurance is given that there will be a liquid market in the securities traded on GEM.

The principal means of information dissemination on GEM is publication on the internet website operated by the Stock Exchange. Listed companies are not generally required to issue paid announcements in gazetted newspapers. Accordingly, prospective investors should note that they need to have access to the GEM website in order to obtain up-to-date information on GEM-listed issuers.

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DEFINITIONS

In this circular, the following expressions have the following meanings unless the context requires otherwise:

“associate(s)”	has the meaning given to it by the Main Board Listing Rules
“Board”	the board of Directors
“Business Day”	a day on which licensed banks are open for business in Hong Kong and the Stock Exchange is open for business of dealing in securities
“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 amended by a supplemental agreement dated 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
“Class Meetings”	the separate class meetings of the holders of H Shares and holders of Domestic Shares to be held at 10:00 a.m. and 11:00 a.m., respectively, on 5 December 2006 or any adjournment thereof
“Company”	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 PRC with limited liability and whose H Shares are listed on GEM
“CSRC”	China Securities Regulatory Commission
“Director(s)”	the director(s) of the Company
“Domestic Share(s)”	the ordinary domestic share(s) with a nominal value of RMB0.10 each in the registered share capital of the Company which are subscribed for in RMB
“Effective Date”	expected to be on 10 January 2007, the date on which the Proposed Withdrawal and the Proposed Introduction become effective
“EGM”	an extraordinary general meeting of the Company to be held at No. 99 Beihai Road, Shouguang City, Shandong Province, the People’s Republic of China on 5 December 2006 at 9:00 a.m. or any adjournment thereof

DEFINITIONS

“EGM Notice”	the notice convening the EGM, which is set out on pages 37 to 44 of this circular
“Existing Articles”	the existing articles of association of the Company as amended from time to time
“Existing General Mandate”	the general mandate to issue Shares granted to the Directors pursuant to the relevant resolution passed at the annual general meeting of the Company held on 12 May 2006
“GEM”	the Growth Enterprise Market of the Stock Exchange
“GEM Listing Rules”	the Rules Governing the Listing of Securities on GEM, as amended from time to time
“GEM Sponsor”	Deloitte & Touche Corporate Finance Limited
“Group”	the Company and its subsidiaries (as defined in the GEM Listing Rules)
“Hong Kong”	the Hong Kong Special Administrative Region of the PRC
“H Share(s)”	the overseas listed foreign invested shares with a nominal value of RMB0.10 each in the registered share capital of the Company, which are subscribed for and traded in Hong Kong dollar
“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
“Latest Practicable Date”	16 October 2006, being the latest practicable date prior to the printing of this circular for the purpose of ascertaining certain information contained in this circular
“Listing Document”	the listing document dated 19 October 2006 to be issued by the Company in connection with the Proposed Introduction
“Main Board Listing Committee”	the listing committee of the Stock Exchange

DEFINITIONS

“Main Board Listing Rules”	the Rules Governing the Listing of Securities on the Stock Exchange, as amended, supplemented or otherwise modified from time to time, and any applicable practice notes, supplementary guidance or other regulations issued by the Stock Exchange
“Main Board”	the stock market operated by the Stock Exchange prior to the establishment of GEM (excluding the options market) which stock market continues to be operated by the Stock Exchange in parallel with GEM. For the avoidance of doubt, the Main Board excludes GEM
“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 on 1 August 2000 with a registered capital of RMB12,380,000
“Molong Equipment”	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
“Mr. Fang”	方亨超 (Luke Fang), one of the shareholders of Molong Equipment, who is not connected with any of the Directors, Supervisors, chief executive and substantial shareholders of the Company or its subsidiaries or any of their respective associates (as defined under GEM Listing Rules)
“PRC”	the People’s Republic of China, which for the purposes of this circular, excludes Hong Kong, the Macau Special Administrative Region of the PRC and Taiwan
“Proposed Introduction”	the proposed listing of the H Shares on the Main Board by way of introduction pursuant to the Main Board Listing Rules
“Proposed Withdrawal”	the proposed voluntary withdrawal of the listing of the H Shares on GEM
“RMB”	Renminbi, the lawful currency for the time being of the PRC
“SFO”	Securities and Futures Ordinance (Chapter 571 of the Laws of Hong Kong)
“Share(s)”	Domestic Share(s) and/or H Share(s), as the case may be
“Shareholder(s)”	holder(s) of the Shares

DEFINITIONS

“Share Issue Mandate”	a general mandate proposed to be granted to the Directors to allot, issue and otherwise deal with Shares not exceeding 20% of the aggregate amount of Domestic Shares in issue and 20% of the aggregate nominal amount of the H Shares in issue as at the date of the passing of the relevant special resolution as set out in the EGM Notice
“Sponsor” or “Guotai Junan”	Guotai Junan Capital Limited
“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 provide for the Casting Annual Caps
“Supervisor(s)”	members of the supervisory committee of the Company
“Weihai Baolong”	威海寶隆石油專材有限公司 (Weihai Baolong Special Petroleum Materials Co., Ltd.), which is owned as to 95% by Maolong Machinery and as to 5% by Molong Equipment
“HK\$”	Hong Kong dollars, the lawful currency of Hong Kong
“US\$”	United States dollars, the lawful currency of the United States of America
“%”	per cent.

RESPONSIBILITY STATEMENT

This circular includes particulars given in compliance with the GEM Listing Rules for the purpose of giving information with regard to the Company. The Directors collectively and individually accept full responsibility for the accuracy of the information contained in this circular and confirm, having made all reasonable enquiries, that to the best of their knowledge and belief:

- (i) the information contained in this circular is accurate and complete in all material aspects and not misleading;
- (ii) there are no other matters the omission of which would make any statement herein misleading; and
- (iii) all opinions expressed in this circular have been arrived at after due and careful consideration and are founded on bases and assumptions that are fair and reasonable.

EXPECTED TIMETABLE

The expected timetable for the Proposed Withdrawal and the Proposed Introduction is set out below:

Despatch of this circular, the notices convening the EGM and the separate Class Meetings and the related forms of proxy and reply slips to the Shareholders	Thursday, 19 October 2006
Despatch of the Listing Document to the Shareholders	Thursday, 19 October 2006
Latest time for lodgement with the instrument of transfer accompanied by the relevant share certificate in order to qualify for the interim dividend and attending the EGM and/or the Separate Class Meetings	4:00 p.m. on Friday, 3 November 2006
Closure of register of members (both days inclusive)	
from	Sunday, 5 November 2006
to	Tuesday, 5 December 2006
Latest time for return of related reply slips for the EGM and the separate Class Meetings	Tuesday, 14 November 2006
Latest time for lodgement of related forms of proxy for the EGM and the separate Class Meetings	9:00 a.m. on Monday, 4 December 2006
EGM	9:00 a.m. on Tuesday, 5 December 2006
Class meeting of holders of H Shares	10:00 a.m. on Tuesday, 5 December 2006
Class meeting of holders of Domestic Shares	11:00 a.m. on Tuesday, 5 December 2006
Date of the announcement of results of the EGM and the separate Class Meetings which are to be published in The Standard (in English), Hong Kong Economic Times (in Chinese) and on the GEM website	Wednesday, 6 December 2006
Notice of the Proposed Withdrawal on or before	Wednesday, 6 December 2006
The CSRC granting approval for the listing of the H Shares on the Main Board on or before	Tuesday, 2 January 2007
Date of the announcement in respect of the CSRC granting approval for the listing of the H Shares on or before	Tuesday, 2 January 2007
Last day of dealing in the H Shares on GEM	4:00 p.m. on Tuesday, 9 January 2007
Withdrawal of listing of the H Shares on GEM effective from	9:30 a.m. on Wednesday, 10 January 2007
Dealings in the H Shares on the Main Board to commence on	9:30 a.m. on Wednesday, 10 January 2007

Notes:

1. All times and dates refer to Hong Kong local times and dates.
2. Shareholders will be informed by public announcement of any changes in the above expected timetable.



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)

Executive Directors:

Zhang En Rong
Lin Fu Long
Zhang Yun San
Xie Xin Cang

Registered Office:

No. 99 Beihai Road
Shouguang City
Shandong Province
The People's Republic of China

Non-executive Directors:

Chen Jian Xiong
Wang Ping

*Principal place of business
in Hong Kong:*

Suite A, 11th Floor
Ho Lee Commercial Building
38-44 D'Aguilar Street
Central, Hong Kong

Independent Non-Executive Directors:

Qin Xue Chang
Yan Yi Zhuang
Loke Yu

19 October 2006

To the Shareholders

Dear Sir or Madam,

**PROPOSED VOLUNTARY WITHDRAWAL OF LISTING
ON THE GROWTH ENTERPRISE MARKET OF
THE STOCK EXCHANGE OF HONG KONG LIMITED,
PROPOSED LISTING ON THE MAIN BOARD OF
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BY WAY OF INTRODUCTION,
PROPOSED REDUCTION OF THE MINIMUM NOTICE PERIOD
IN RESPECT OF THE PROPOSED WITHDRAWAL,
PROPOSED GRANT OF NEW GENERAL MANDATE
AND PROPOSED REVOCATION OF EXISTING GENERAL MANDATE,
PROPOSED AMENDMENTS TO THE ARTICLES
OF ASSOCIATION OF THE COMPANY,
CONTINUING CONNECTED TRANSACTION,
PROPOSED DECLARATION OF INTERIM DIVIDEND AND
CLOSURE OF REGISTER OF MEMBERS**

INTRODUCTION

On 11 July 2006, the Board announced that the Sponsor had on behalf of the Company submitted an application to the Stock Exchange for the Proposed Introduction and informed the Stock Exchange

* For identification purpose only

LETTER FROM THE BOARD

of the intention of the Company to implement the Proposed Withdrawal, conditional upon the conditions set out in the paragraph headed “Conditions of the Proposed Withdrawal and the Proposed Introduction” below.

In connection with the Proposed Introduction, the Directors propose to the Shareholders to amend the Existing Articles, and grant the Share Issue Mandate and to revoke the Existing General Mandate in order to comply with the requirements under the Main Board Listing Rules.

On 25 September 2006, the Board announced that the Company and Molong Equipment entered into the Supplemental Agreement for the purpose of extending the term of the Casting Supply Agreement to 31 December 2007 and providing for the Casting Annual Caps. 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 requires the approval of the independent Shareholders under GEM Listing Rule 20.48.

Subject to the approval of the Shareholders at the EGM, the Board proposes to declare and pay an interim dividend of RMB1.5 cents per share in respect of the six months ended 30 June 2006 to the Shareholders whose names appear on the register of members of the Company on 4 December 2006, which will be payable on or before 29 December 2006.

The purpose of this circular is to give you further information on, *inter alia*, the Proposed Withdrawal, the Proposed Introduction, the proposed amendments to the Existing Articles, the proposed grant of the Share Issue Mandate, the proposed revocation of the Existing General Mandate, the CCT Transaction, the Casting Annual Caps, the proposed declaration of interim dividend and to seek Shareholders’ approval (save and except for CCT Transaction and the Casting Annual Caps which require the independent Shareholders’ approval) of the resolutions in respect of the aforesaid at the EGM and the separate Class Meetings as described in the paragraph headed “The EGM and Class Meetings” below. The notices convening the EGM and the separate Class Meetings are set out in pages 45 to 50 of this circular.

THE PROPOSED WITHDRAWAL AND THE PROPOSED INTRODUCTION

On 11 July 2006, the Sponsor had on behalf of the Company submitted an advance booking form to the Stock Exchange for the listing of, and permission to deal in, on the Main Board 246,276,000 H Shares in issue.

The Stock Exchange informed the Sponsor on 17 October 2006 that the Main Board Listing Committee had granted an approval in principle of the listing of, and permission to deal in, the H Shares on the Main Board. Immediately following the Proposed Withdrawal, the listing of the H Shares on the GEM will be withdrawn and the H Shares as mentioned in the immediately preceding paragraph will be listed on the Main Board.

LETTER FROM THE BOARD

WAIVER FROM STRICT COMPLIANCE WITH THE MINIMUM NOTICE PERIOD IN RESPECT OF THE PROPOSED WITHDRAWAL

Pursuant to Rule 9.19 of the GEM Listing Rules, an issuer that has an alternative listing on another regulated, regularly operating, open stock exchange or securities market recognised for this purpose by the Stock Exchange, may not voluntarily withdraw its listing on GEM unless:

- (i) the prior approval of the shareholders of the issuer has been obtained by way of an ordinary resolution passed at a duly convened meeting of the shareholders of the issuer;
- (ii) the prior approval of holders of H Shares and Domestic Shares has been obtained at the separate Class Meetings; and
- (iii) the issuer has given its shareholders and holders of H Shares and Domestic Shares at least three months' notice of the proposed withdrawal of listing.

In connection with the Proposed Withdrawal, the Company has applied to, and the Stock Exchange has granted, a waiver from strict compliance with the minimum three months' notice required under Rule 9.19 of the GEM Listing Rules, subject to the fulfillment of the following conditions:

- (i) the prior approval of the Shareholders for the reduction in the notice period for the Proposed Withdrawal to at least five clear Business Days shall have been obtained;
- (ii) in respect of the H Shares, there is no change in the board lot size, the share certificates, the share registrar and the trading currency in connection with the proposal to transfer its listing status; and
- (iii) there is no other fact that leads the Stock Exchange to believe that the reduced notice period is not feasible.

Accordingly, the EGM and the separate Class Meetings are respectively convened to seek the approval of the Shareholders for, amongst other things, the Proposed Withdrawal and the proposed reduction in the notice period for the Proposed Withdrawal. After Shareholders' approval shall have been obtained, a notice of the Proposed Withdrawal will be published at least five clear Business Days from the date on which the Shareholders shall have approved the Proposed Withdrawal at the EGM and separate Class Meetings.

The Directors consider that it is in the best interests of the Shareholders and the Company as a whole that the notice period for the Proposed Withdrawal be reduced so that the Proposed Withdrawal and the Proposed Introduction can be carried out as soon as practicable after obtaining the relevant approvals from the Shareholders at the EGM and the Class Meetings as well as from the CSRC.

LETTER FROM THE BOARD

CONDITIONS OF THE PROPOSED WITHDRAWAL AND THE PROPOSED INTRODUCTION

The implementation of the Proposed Withdrawal and the Proposed Introduction are conditional upon, amongst other things:

- (i) the Main Board Listing Committee granting approval for the listing of, and permission to deal in, the H Shares on the Main Board as mentioned under the paragraph headed “The Proposed Withdrawal and the Proposed Introduction” above;
- (ii) the CSRC granting approval for the listing of the H Shares on the Main Board;
- (iii) the passing of special resolutions at the EGM and the separate Class Meetings to approve, amongst other things, the Proposed Withdrawal, the Proposed Introduction and the proposed reduction in the notice period for the Proposed Withdrawal;
- (iv) the publication of a notice of the Proposed Withdrawal after obtaining the approval of Shareholders referred to in condition (iii) above not less than five clear Business Days after the approval of the Shareholders for the Proposed Withdrawal;
- (v) the GEM Listing Committee granting a waiver for the reduction of the notice period for the Proposed Withdrawal from a minimum of three months under Rule 9.19(3) of GEM Listing Rules to at least five clear business days from the date on which the Shareholders shall have approved the Proposed Withdrawal at the EGM and the separate Class Meetings and the fulfillment of such waiver by the Company; and
- (vi) the obtaining of all other relevant consents (if any) which are required in connection with the implementation of the Proposed Withdrawal and the Proposed Introduction and fulfillment of all conditions which may be attached to such consents.

EFFECTS OF THE PROPOSED WITHDRAWAL AND THE PROPOSED INTRODUCTION

Subject to the fulfillment of the conditions set out in the immediately preceding paragraph, it is expected that dealings in the H Shares on GEM will cease at 9:30 a.m. on the Effective Date and dealings in the H Shares on the Main Board will commence at 9:30 a.m. on the Effective Date. The Company will make an announcement after the EGM and the respective Class Meetings to publish the results of the EGM and the respective Class Meetings and other information on the Proposed Withdrawal and the trading arrangements of the H Shares with respect to the Proposed Withdrawal and the Proposed Introduction. The Company will also issue a notice of the Proposed Withdrawal from the date on which the Shareholders shall have approved the Proposed Withdrawal at the EGM and the respective Class Meetings.

LETTER FROM THE BOARD

The Proposed Withdrawal and the Proposed Introduction will have no effect on the existing share certificates in respect of the H Shares which will continue to be good evidence of legal title and will not involve any transfer or exchange of the existing share certificates. The Directors propose no change to be made to the board lot size, trading currency of the H Shares and the share registrar of the H Shares in connection with the Proposed Withdrawal and the Proposed Introduction. The H Shares will continue to be traded in board lots of 4,000 H Shares. **Please note that if and when the H Shares are listed on the Main Board, you may be required to sign a new client agreement with your stockbrokers.**

Please also note that the continuing obligations of listed issuers under the Main Board Listing Rules and the GEM Listing Rules are not the same. Under the GEM Listing Rules, the Company is required to publish its quarterly results on the internet website operated by the Stock Exchange. Upon the listing of the H Shares on the Main Board, the Company will cease the practice of quarterly reporting and will follow the relevant requirements of the Main Board Listing Rules which include, amongst other things, through paid announcements in newspapers generally circulated in Hong Kong, publish its interim results and annual results within three months and four months from the end of the relevant period or financial year-end respectively. The Directors are of the view that following the reporting requirements under the Main Board Listing Rules will provide investors and the Shareholders with a high degree of transparency and a more complete picture of the performance of the Group during the relevant period. The Directors also believe that the cessation of quarterly reporting would save significant publishing costs and other related expenses, and enable management to devote greater management time to other key aspects of the operation of the Company's business.

REASONS FOR THE PROPOSED WITHDRAWAL AND THE PROPOSED INTRODUCTION

The Group is principally engaged in the design, manufacture and sales of petroleum drilling and extracting machinery and related accessories. Since the listing of the H Shares on GEM in April 2004, the Group has experienced significant growth and has established strong market positions in each of its primary business segments. Nevertheless, the Directors believe that the listing of the H Shares on the Main Board will help to enhance the profile of the Group and increase the trading liquidity of the H Shares. The Directors consider that the listing of the H Shares on the Main Board will be beneficial to the future growth, financing flexibility and business development of the Company. No change in the business of the Group is contemplated by the Directors following the Proposed Introduction.

The Proposed Introduction will not involve any issue of new H Shares by the Company.

WAIVERS FROM STRICT COMPLIANCE WITH RULES 10.07(1)(a) AND 10.08 OF THE MAIN BOARD LISTING RULES

In connection with the Proposed Introduction, the Company has applied to the Stock Exchange for, and the Stock Exchange has granted, a waiver from strict compliance with the restrictions on further issues of securities within six months of listing on the Main Board as required by Rule 10.08

LETTER FROM THE BOARD

of the Main Board Listing Rules and a consequential waiver from strict compliance with the restrictions under Rule 10.07(1)(a) of the Main Board Listing Rules in respect of the deemed disposal of H Shares by the controlling shareholders upon the issue of securities by the Company within six months of listing on the Main Board subject to the following conditions:

- (i) any issue of H Shares (or convertible securities) during the first six months after listing on the Main Board must be either for cash to fund a specific acquisition or as part or full consideration for an acquisition;
- (ii) the acquisition must be for assets or business(es) that will contribute to the growth of the operations of the Group; and
- (iii) Zhang En Rong, the controlling shareholder of the Company, should not cease to be a controlling shareholder of the Company upon the issue of securities by the Company within six months of the listing on the Main Board.

The Company has applied to the Stock Exchange for waivers from strict compliance with Rules 10.07(1)(a) and 10.08 of the Main Board Listing Rules for the following reasons:

- (i) the Company will not raise any new funds pursuant to the Proposed Introduction. Therefore, the Shareholders would not suffer any dilution of their interests as a result of the Company's listing on the Main Board;
- (ii) Mr. Zhang En Rong, the controlling shareholder of the Company, has not disposed of any H Shares since the Company was established and intends not to dispose of any Shares owned by him within six months after the H Shares are listed on the Main Board; and
- (iii) the interests of the Shareholders are protected since any further issue of H Shares by the Company would be subject to Shareholders' approval as required under Rule 19A.38 of the Main Board Listing Rules.

FINANCIAL INFORMATION ON THE GROUP

Liquidity and capital resources

The Company has historically met its working capital and other capital requirements principally from cash provided by operations, while raising the remainder of its requirements primarily through bank borrowings and equity market.

LETTER FROM THE BOARD

The following table presents selected cash flow data of the Company for the three years ended 31 December 2003, 2004 and 2005 and the four months ended 30 April 2006.

Cash flows

	Years ended 31 December			Four months ended 30 April	
	2003	2004	2005	2005	2006
	<i>RMB'000</i>	<i>RMB'000</i>	<i>RMB'000</i>	<i>RMB'000</i>	<i>RMB'000</i>
				<i>(Unaudited)</i>	
Net cash inflow from operating activities	41,388	35,434	302,623	73,454	(25,783)
Net cash outflow from investing activities	(49,871)	(44,660)	(273,851)	(102,838)	(113,463)
Net cash inflow from financing activities	7,831	3,667	99,394	31,900	50,808
Cash and cash equivalents at the end of the year/period	63,087	57,528	185,694	60,044	97,256

The Company has cash and cash equivalents of approximately RMB97.26 million as at 30 April 2006, and reported a net cash outflow from operating activities of approximately RMB25.78 million during the four months ended 30 April 2006. The capital commitments as at 30 April 2006 related primarily to the construction of the new casing production line. The construction of the new casing production line was financed by the proceeds from the placing of additional H Shares in May 2005, internal resources and bank borrowings. The Company continuously manages its liquidity situation to ensure that it is adequate to meet its expansion plans.

Capital commitments

	Group and Company			
	As at 31 December			As at 30 April
	2003	2004	2005	2006
	<i>RMB'000</i>	<i>RMB'000</i>	<i>RMB'000</i>	<i>RMB'000</i>
Contracted, but not provided for:				
Land and buildings	—	37,144	25,549	7,695
Plant and machinery	1,923	90,640	120,790	62,748
Intangible assets	—	186	—	—
	1,923	127,970	146,339	70,443
Authorized, but not contracted for:				
Plant and machinery	—	43,750	—	—
	1,923	171,720	146,339	70,443

LETTER FROM THE BOARD

Indebtedness

Borrowings

As at the close of business on 31 July 2006, being the latest practicable date for the indebtedness statement prior to the printing of this circular, the used and unused banking facilities of the Group are RMB158 million and RMB367 million, respectively.

Commitments

As at 30 April 2006, the Group's operating lease commitment was approximately RMB3,138,000. On the same date, the Group had capital expenditure commitments of approximately RMB70,443,000.

Except as described above, the Group did not have any outstanding loan capital, mortgages, charges, bank overdrafts, finance leases or hire purchase commitments, guarantee indemnities or other material contingent liabilities at the close of business on 30 April 2006.

Working capital

The Directors after due and careful enquiry are of the opinion that, taking into consideration the financial resources available to the Company including its internally generated funds, the Company has sufficient working capital in the next 12 months commencing from the date of the Listing Document.

Net tangible assets

The following statement shows the Group's net tangible assets as at 30 April 2006 which has been prepared based on the audited consolidated net assets of the Group as at 30 April 2006, shown in the accountants' report of the Group set out in Appendix I to the Listing Document.

Audited net tangible assets of the Group as at 30 April 2006 (<i>Note 1</i>)	<u>RMB450,727,000</u>
Audited net tangible asset value per share (<i>Note 2</i>)	<u>RMB0.696</u>

Notes:

1. The audited net tangible assets of the Group as at 30 April 2006 is arrived at based on the audited consolidated net assets of the Group from the Accountants' Report set out in the section headed "Accountants' Report" in Appendix I to the Listing Document.
2. The net tangible asset value per Share has been arrived at based on the 647,998,000 Shares in issue at the date of the Listing Document as if such Shares were outstanding through the financial period ended 30 April 2006.

LETTER FROM THE BOARD

AMENDMENTS TO THE EXISTING ARTICLES

In connection with the Proposed Introduction, to remove references to GEM, to comply with various provisions of the Main Board Listing Rules and to make other immaterial consequential changes to the Existing Articles, the Board proposes to seek the approval of the Shareholders for the amendments to the Existing Articles at the EGM. The provisions of the amended Existing Articles will comply with the relevant requirements of the Main Board Listing Rules. Set out below are the details of the principal amendments to be effected:

1. the consequential amendments to the Existing Articles as a result of the Proposed Introduction;
2. the amendments to the Existing Articles in order to comply with the code provisions of the Code on Corporate Governance Practices contained in Appendix 14 to the Main Board Listing Rules;
3. the amendments to the Existing Articles in order to comply with Rule 13.39(3) of the Main Board Listing Rules; and
4. any consequential amendments to the Existing Articles as the Board may consider necessary.

The coming into effect of the above amendments to the Existing Articles are conditional upon:

- (i) the passing of a special resolution by the Shareholders at the EGM to approve the amendments to the Existing Articles;
- (ii) the approval from the Ministry of Commerce on the amendments to the Existing Articles; and
- (iii) the commencement of dealings in the H Shares on the Main Board.

GENERAL MANDATE

The Directors are of the view that as the Existing General Mandate makes specific references to GEM, in connection with the Proposed Introduction on the Main Board, special resolution will be proposed at the EGM to revoke the Existing General Mandate and to grant to the Directors the Share Issue Mandate. The Share Issue Mandate will expire upon the earlier of (i) the conclusion of the next annual general meeting of the Company; or (ii) the passing of a special resolution by the Shareholders in general meeting revoking or varying the authority given to the Directors by the relevant resolutions. The relevant resolutions relating to the Share Issue Mandate are set out as resolution number 2 in the EGM Notice.

LETTER FROM THE BOARD

The Directors confirm that they have not exercised the Existing General Mandate to issue Shares after they were granted to the Directors pursuant to resolutions passed at the annual general meeting of the Company held on 12 May 2006 and that they have no present intention to exercise the Existing General Mandates prior to the Proposed Introduction.

SUPPLEMENTAL AGREEMENT

Reference is made to the prospectus of the Company dated 30 March 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 for a term from 15 April 2004 to 31 December 2006 and providing for the Casting Annual Caps.

As the term of the Casting Supply Agreement will expire on 31 December 2006, the Company and Molong Equipment entered into the Supplemental Agreement 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 Cap

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 in 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 ended 31 December 2006 is determined on the basis that the actual 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 purchase 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 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.

LETTER FROM THE BOARD

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

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.

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.

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 requires 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.

Financial effects of the CCT Transaction

The Directors confirm that there would be no material adverse effects on the assets, liabilities and earnings of the Group as a result of entering into the Supplemental Agreement.

LETTER FROM THE BOARD

PROPOSED DECLARATION OF INTERIM DIVIDEND AND CLOSURE OF REGISTER OF MEMBERS

Subject to the approval of the Shareholders at the EGM, the Board proposes to declare and pay an interim dividend of RMB1.5 cents per share in respect of the six months ended 30 June 2006 to the Shareholders whose names appear on the register of members of the Company on 4 December 2006. The interim dividend will be payable on or before 29 December 2006. The register of members of the Company will be closed from 5 November 2006 to 5 December 2006, both days inclusive, during which period no share transfer shall be effected. The interim dividend as declared should not be taken as an indication of the level of profit or dividend for the full year. In order to qualify for the interim dividend and attending the EGM, all instruments of transfer accompanied by the relevant share certificates must be lodged with the Company's H Share Registrar, Tricor Investor Services Limited, at 26th Floor, Tesbury Centre, No. 28 Queen's Road East, Hong Kong for registration no later than 4:00 p.m. on 3 November 2006

An ordinary resolution in relation to the proposed declaration of interim dividend will be put forth for consideration by the Shareholders.

THE EGM AND CLASS MEETINGS

The notices convening the EGM and the separate Class Meetings are set out on pages 37 to 50 of this circular.

Special resolutions will be proposed at the EGM to consider and, if thought fit, approve, amongst other things, the following:

- (i) the Proposed Withdrawal;
- (ii) the Proposed Introduction;
- (iii) the proposed reduction in the notice period for the Proposed Withdrawal;
- (iv) the proposed revocation of the Existing General Mandate;
- (v) the proposed granting of the Share Issue Mandate to the Directors; and
- (vi) the proposed amendments to the Existing Articles.

Ordinary resolution will also be proposed at the EGM for the purpose of seeking the approval of the Independent Shareholders of 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 in 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

LETTER FROM THE BOARD

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 the Maolong Machinery; and (3) Molong Equipment is a subsidiary of Maolong Machinery.

Ordinary resolution will also be proposed at the EGM for the proposed declaration of the interim dividend.

In addition, special resolution will be proposed at each of the Class Meetings to consider and, if thought fit, approve, amongst other things, the Proposed Introduction and Proposed Withdrawal.

The votes to be taken at the EGM and the separate Class Meetings will be taken by poll.

For the purposes of the EGM and the separate Class Meetings, the register of members of the Company will be closed from 5 November 2006 to 5 December 2006 (both dates inclusive), during which no transfer of Shares will be registered. Accordingly, holders of H Shares and holders of Domestic Shares whose names appear on the register of members of the Company at the close of business on 3 November 2006 shall have the right to attend the EGM and the separate Class Meetings.

Whether or not you are able to attend the meetings, you are reminded to complete the forms of proxy enclosed with this circular, in accordance with the instructions printed thereon and send the relevant forms of proxy to the registered office of the Company at No. 99 Beihai Road, Shouguang City, Shandong Province, the People's Republic of China (for holders of Domestic Shares), or to the office of the Company's H Share Registrar, Tricor Investor Services Limited, on the 26th Floor, Tesbury Centre, 28 Queen's Road East, Hong Kong (for holders of H Shares) as soon as practicable and in any event not later than 24 hours before the respective time appointed for the holding of the separate Class Meetings of holders of H Shares and holders of Domestic Shares and the EGM. Completion and return of the relevant forms of proxy will not preclude you from attending and voting in person at the meetings or at any adjourned meetings should you so wish.

Reply slips for each of the EGM and the separate Class Meetings have also been enclosed. You are reminded to complete and sign the relevant reply slips (if you are entitled to attend the relevant meetings) and return the signed slips to the Company's registered office (for holders of Domestic Shares), or to the office of the Company's H Share Registrar, Tricor Investor Services Limited, on the 26th Floor, Tesbury Centre, 28 Queen's Road East, Hong Kong (for holders of H Shares) on or before 14 November 2006 in accordance with the instructions printed thereon.

RIGHT TO DEMAND A POLL

Pursuant to the Existing Articles, at any general meeting of the Company a resolution put to the vote of the meeting shall be decided on a show of hand unless a poll is taken as may from time to time be required under the GEM Listing Rules or any other applicable laws, rules or regulations or unless (before or on the declaration of the result of the show of hands or on the withdrawal of any other demand for a poll) a poll is duly demanded. A poll may be demanded by:

- (i) the chairman of the meeting;

LETTER FROM THE BOARD

- (ii) at least five members of the Company present in person or by proxy and entitled to vote or who represent in the aggregate not less than one-tenth of the total voting rights of all members having the right to attend and vote at the meeting; or
- (iii) any member or members present in person or by proxy and holding shares conferring a right to attend and vote at the meeting on which there have been paid up sums in the aggregate equal to not less than one-tenth of the total sum paid up on all shares conferring that right.

RECOMMENDATION

The Board considers that the Proposed Introduction, the Proposed Withdrawal, the proposed reduction in the notice period for the Proposed Withdrawal, the proposed revocation of the Existing General Mandate, the proposed grant of the Share Issue Mandate, the proposed amendments to the Existing Articles, the proposed declaration of interim dividend, the CCT Transaction and the Casting Annual Caps to be in the interests of the Company and the Shareholders as a whole. Accordingly, the Board recommends the Shareholders to vote in favour of all the resolutions to be proposed at the EGM and the separate Class Meetings, and in particular, the independent Shareholders to vote in favour of the resolutions in relation to the CCT Transaction and the Casting Annual Caps and vote in favour of the relevant ordinary resolution set out in the notice of the EGM for the approval of the CCT Transaction and the Casting Annual Caps.

ADDITIONAL INFORMATION

Your attention is drawn to the appendices to this circular.

Yours faithfully,
By Order of the Board
Shandong Molong Petroleum Machinery Company Limited
Zhang En Rong
Chairman



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)

19 October 2006

To the Independent Shareholders

Dear Sir or Madam,

Continuing Connected Transaction

We have been appointed as the Independent Board Committee to advise the independent Shareholders on whether the terms of the CCT Transaction and the Casting Annual Caps are fair and reasonable. Details of the CCT Transaction and the Casting Annual Caps are set out in the letter from the Board contained in the circular to the Shareholders dated 19 October 2006 (the “Circular”), of which this letter forms part. Terms defined in the Circular shall have the same meanings when used herein unless the context otherwise requires.

Having considered, among other matters, the factors and reasons considered by, and the opinions of Independent Financial Adviser as stated in its letter of advice set out on pages 22 to 27 of the Circular, we are of the opinion that the terms of the CCT Transaction and the Casting Annual Caps are fair and reasonable and the CCT Transaction and the Casting Annual Caps are in the interests of the Company and the Shareholders as a whole. We therefore recommend the independent Shareholders to vote in favour of the ordinary resolution to be proposed at the EGM to approve the CCT Transaction and the Casting Annual Caps.

Yours faithfully,

Mr. Qin Xue Chang

Independent

non-executive Director

Mr. Yan Yi Zhuang

Independent

non-executive Director

Mr. Loke Yu

Independent

non-executive Director

* For identification purpose only

The following is the text of a letter of advice from China Everbright Capital Limited to the Independent Board Committee and the Independent Shareholders in respect of the Supplemental Agreement and the New Annual Caps, which has been prepared for the purpose of inclusion in this circular:



China Everbright Capital Limited

40/F., Far East Finance Centre

16 Harcourt Road

Hong Kong

19 October 2006

To: the Independent Board Committee and
the Independent Shareholders

Dear Sirs,

CONTINUING CONNECTED TRANSACTION

We refer to our appointment as the independent financial adviser to advise the Independent Board Committee and the Independent Shareholders in connection with the Supplemental Agreement and the new annual caps under the Supplemental Agreement for the two years ending 31 December 2007 (“New Annual Caps”), particulars of which are set out in a circular to the Shareholders dated 19 October 2006 (the “Circular”) and in which this letter is reproduced. Unless the context requires otherwise, terms used in this letter shall have the same meanings as given to them in the Circular.

As (i) the Casting Supply Agreement dated 20 March 2004 will expire on 31 December 2006; and (ii) the aggregate purchase of casting products from Molong Equipment by the Company under the Casting Supply Agreement for the year ending 31 December 2006 is expected to exceed the existing annual cap for the year ending 31 December 2006 (“Existing 2006 Annual Cap”) stated in the Casting Supply Agreement, the Board announced that the Company entered into the Supplemental Agreement with Molong Equipment on 22 September 2006. Pursuant to the Supplemental Agreement, Molong Equipment and the Company agreed to extend the term of the Casting Supply Agreement to 31 December 2007 and to increase the Existing 2006 Annual Cap.

Given that Molong Equipment is regarded as the connected person of the Company within the meanings of the GEM Listing Rules, the entering into the Supplemental Agreement and the New Annual Caps, will be subject to, *inter alia*, the Independent Shareholders’ approval at the EGM.

As mentioned in the letter from the Board, Zhang En Rong, Lin Fu Long, Zhang Yun San, Xie Xin Cang, Liu Yun Long and their respective associates (as the case may be) will abstain from voting with respect to the resolution to be passed at the EGM as mentioned above.

China Everbright is independent from and not connected with the Company or the directors, chief executive and substantial shareholders of the Company or any of its subsidiaries or their respective associates, and is qualified to give independent advice to the Independent Board Committee and Independent Shareholders.

In formulating our opinion, we have relied on the accuracy of the information and representations provided to us by the Company and contained in the Circular, and have assumed that all information and representations made or referred to in the Circular were true at the time they were made and continue to be true as at the date of the Circular. We have also assumed that all statements of belief, opinion and intention made by the Directors in the Circular were reasonably made after due inquiry. We consider that we have reviewed sufficient information to reach an informed view, to justify relying on the accuracy of the information contained in the Circular and to provide a reasonable basis for our opinion. We have no reason to suspect that any material facts have been omitted or withheld from the information contained or opinion expressed in the Circular nor to doubt the truth, accuracy and completeness of the information and representations provided to us by the Directors.

We have not, however, carried out any independent verification of the information and representations provided by the Company, nor have we conducted an independent in-depth investigation into the business and affairs of the Group (including the Company, Molong Equipment and their respective associates).

PRINCIPAL REASONS AND FACTORS CONSIDERED

In arriving at our recommendation to the Independent Board Committee and the Independent Shareholders in respect of the Supplemental Agreement and the New Annual Caps, we have considered the following principal reasons and factors:

(i) Background to and reasons for the Supplemental Agreement and the New Annual Caps

The Group is principally engaged in the design, manufacture and sale of petroleum drilling and extracting machinery and related accessories. Molong Equipment, which is a connected person to the Company, is principally engaged in the production and sales of tip thickened oil well pipes, electrical equipment set and castings, and the casting products are used by the Group as raw material during production process.

Since the listing of the shares of the Company on GEM on 15 April 2004, the purchase of casting products from Molong Equipment has been conducted in accordance with the terms of the Casting Supply Agreement dated 20 March 2004. The Company has obtained waivers in respect of the continuing connected transactions in 2004 pursuant to the then GEM Listing Rules and the waivers shall expire on 31 December 2006.

According to the Casting Supply Agreement, the existing annual caps for the purchase of casting products by the Company from Molong Equipment for the three years ending 31 December 2006 would not exceed RMB36 million, RMB47 million and RMB61 million respectively. During the nine months ended 30 September 2006, the actual purchase amount of casting products from Molong Equipment was approximately RMB50.18 million, accounting for 82.3% of the Existing 2006 Annual

Cap. In view of the recent surge of the purchase volume and the estimated purchase in the fourth quarter of 2006, the Directors proposed to increase the Existing 2006 Annual Cap. Based on the above and the Casting Supply Agreement will expire on 31 December 2006, the Company entered into the Supplemental Agreement with Molong Equipment to extend the term of the Casting Supply Agreement to 31 December 2007 and to increase the Existing 2006 Annual Cap from RMB61 million to RMB70 million.

Shareholders should note that, save for the increase in the Existing 2006 Annual Cap and extension of the terms of the Casting Supply Agreement to 31 December 2007, all other terms of Casting Supply Agreement remain substantially the same. Under the Casting Supply Agreement, transactions will be conducted in accordance with the terms of the relevant agreement governing such transaction or on terms that are no less favourable than terms available from independent third parties.

(ii) **The rationale for determining the New Annual Caps**

The following sets out (i) actual purchase amount of casting products from Molong Equipment during the three years ended 31 December 2005; (ii) the existing annual caps for the three years ending 31 December 2006 under the Casting Supply Agreement; and (iii) the New Annual Caps.

	<i>RMB million</i>	Increase as compared to the previous year
Actual purchase amounts of casting products from Molong Equipment		
1 January 2003 — 31 December 2003	18.63	—
1 January 2004 — 31 December 2004	30.41	63%
1 January 2005 — 31 December 2005	40.76	34%
Average growth rate:		49%
The existing annual caps under the Casting Supply Agreement		
1 January 2004 — 31 December 2004	36.00	—
1 January 2005 — 31 December 2005	47.00	31%
1 January 2006 — 31 December 2006	61.00	30%
The New Annual Caps		
1 January 2006 — 31 December 2006	70.00	—
1 January 2007 — 31 December 2007	105.00	50%

As illustrated above, the Directors expect that the New Annual Caps will not exceed RMB70 million and RMB105 million respectively for each of the two years ending 31 December 2007.

The basis for the New Annual Caps

- (1) *The new annual cap for the year ending 31 December 2006 (the “New 2006 Annual Cap”)*

As mentioned before, the New 2006 Annual Cap will be increased to RMB70 million from the Existing 2006 Annual Cap of RMB61 million. Based on our discussions with the Directors, we understand that the New 2006 Annual Cap is determined with reference to historical transaction amounts during the nine months ended 30 September 2006 and the projected purchase of casting products from Molong Equipment in the fourth quarter of 2006.

To assess the reasonableness of the New 2006 Annual Cap, we have discussed with the management of the Company and we have been informed that (i) the purchase of casting products from Molong Equipment has surged significantly during the nine months ended 30 September 2006, compared with the same period in 2005; and (ii) the projected purchase from Molong Equipment in the fourth quarter of 2006 is expected to maintain a strong growth similar to the first three quarters of 2006.

Set out below is the historical transaction amount during the nine months ended 30 September 2005 and 2006, which is based on the internal management accounts provided by the Company:

	The historical transaction amount	Increase as compared to the previous period
	<i>RMB million</i>	
The nine months ended 30 September 2005	27.43	—
The nine months ended 30 September 2006	50.18	83%

As disclosed in the prospectus of the Company dated 30 April 2004, the existing annual caps for the three years ending 31 December 2006 was determined by, among others, the Directors' expectation of approximately 30% increase in the purchase of casting products from Molong Equipment for each of the three years ending 31 December 2006. Therefore, the actual growth rate of purchase from Molong Equipment during the nine months ended 30 September 2006 significantly exceeds the assumption under the Casting Supply Agreement.

As advised by the management, the basis of determining the New 2006 Annual Cap is summarized as below:

	(A)	(B)	(C)	(D)=(A)+(B)+(C)
	Actual purchase amount for the nine months ended 30 September 2006 (unaudited)	Estimated purchase amount for the three months ending 31 December 2006 (Note)	Estimated buffer	New 2006 Annual Cap
	<i>RMB million</i>	<i>RMB million</i>	<i>RMB million</i>	<i>RMB million</i>
Purchase of casting products from Molong Equipment	50.18	16.73	3.09	70.00

Note: The estimated purchase amount is estimated with reference to the average monthly purchase amount during the nine months ended 30 September 2006.

Based on the above, we consider the estimation of the New 2006 Annual Cap is reasonable and justifiable.

(2) *The new annual cap for the year ending 31 December 2007 (“New 2007 Annual Cap”)*

According to the letter from the Board, the New 2007 Annual Cap is determined with reference to (i) the average historical growth of the purchase of casting products by the Company from Molong Equipment by approximately 49% 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.

As set out from the Letter of the Board, the purchase of casting products from Molong Equipment is estimated to reach RMB105 million for the year ending 31 December 2007, representing a 50% growth from the New 2006 Annual Cap. We note that the 50% growth estimation for New 2007 Annual Cap is also in line with the nearly 50% growth rate from the existing 2005 annual cap of RMB47 million to the New 2006 Annual Cap of RMB70 million. Based on our discussion with the Directors, Molong Equipment has increased its production capacity during the nine months ended 30 September 2006 in order to meet the ever-increasing purchase orders from the Group. The Directors envisage that, should the Group place larger order of casting products to Molong Equipment, it will continue to cooperate with the Group in future by increasing its production capacity in casting products.

In addition, we are advised by the Directors that the Group has been dealing with a few new overseas customers and it is essential to obtain a sufficiently large annual cap for the above transactions in order to meet the demand when opportunities arise.

In light of the above, we consider the New 2007 Annual Cap of RMB105 million is reasonable and justifiable.

RECOMMENDATION

Having considered the above factors, in particular,

- (i) the background of and the reasons for the Supplemental Agreement and the New Annual Caps; and
- (ii) the rationale for determining the New Annual Caps,

we consider that the entering into the Supplemental Agreement, including the New Annual Caps, are fair and reasonable so far as the Independent Shareholders are concerned. Accordingly, we recommend the Independent Board Committee to advise the Independent Shareholders to vote in favour of the resolutions approving the Supplemental Agreement (including the New Annual Caps) to be proposed at the EGM.

Yours faithfully,
For and on behalf of
China Everbright Capital Limited
Jacky Ho
Managing Director

1. DISCLOSURE OF INTERESTS

Directors', Supervisors' and Chief Executive's Interests in Shares, Underlying Shares and Debentures

As at the Latest Practicable Date, the interests and positions of the Directors, Supervisors and chief executive of the Company in the shares, debentures or underlying shares of the Company and any of its associated corporations (within the meaning of Part XV of the Securities and Futures Ordinance (“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 5.67 of the GEM Listing Rules, to be notified to the Company and the Stock Exchange, will be as follows:

Long positions in the domestic shares of the Company:

	Type of interest	Number of domestic shares <i>(Note)</i>	Approximate percentage of total issued domestic share capital <i>(%)</i>	Approximate percentage of total issued share capital <i>(%)</i>
Zhang En Rong	Personal	279,517,000	69.58%	43.14%
Lin Fu Long	Personal	34,216,000	8.52%	5.28%
Zhang Yun San	Personal	30,608,000	7.62%	4.72%
Xie Xin Cang	Personal	21,410,000	5.33%	3.30%

Note: Unlisted shares

Save as disclosed above, as at the Latest Practicable Date, none of the Directors, Supervisors or chief executive of the Company nor their associates had any interest and short positions 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) which would have to be notified to the Company and the Stock Exchange under the provisions of Divisions 7 and 8 of Part XV of the SFO or pursuant to section 352 of the SFO, to be entered in the register referred to therein or which were required to be notified to the Company and the Stock Exchange pursuant to rules 5.46 to 5.67 of the GEM Listing Rules.

GEM Sponsor's Interests

Neither the GEM Sponsor nor any of its directors, employees or associates (as referred to in Note 3 to GEM Listing Rule 6.35) had any interests in the securities of the Company or any right to subscribe for or to nominate persons to subscribe for the securities of the Company or any member of the Group. The Company was also informed by the Sponsor that none of the Sponsor or its directors, employees, associates (as referred to in GEM Listing Rule 6.36) has any competing interest.

Pursuant to the sponsorship agreement dated 29 March 2004 and entered into between the Company and the GEM Sponsor, the GEM Sponsor has been appointed as the sponsor of the Company for the remainder of the year ended 31 December 2004 and for the period of two years thereafter until 31 December 2006 and the GEM Sponsor is entitled to receive an agreed amount of fee for its provision of services.

Directors' and Supervisors' Interest in Any Asset Acquired, Disposed or Leased

None of the Directors and Supervisors has any material interest, direct or indirect, in any asset which, since 30 April 2006, being the date to which the latest audited consolidated financial statements of the Group have been made up, had been acquired or disposed of by or leased to any member of the Group or was proposed to be acquired or disposed of by or leased to any member of the Group.

Directors' and Supervisors' Service Contract

Each of the Directors and Supervisors has entered into a service contract with the Company. Particulars of these contracts, except as indicated, are in all material respects identical and set out below:

- (i) each service contract is for an initial term of three years commencing from the date of the signing of the service contract and may be renewed thereunder subject to the approval of the Shareholders' meeting of the Company;

- (ii) the annual salary and/or allowance (subject to actual adjustments) for each of the Directors and Supervisors during their initial term of three years are as follows:

	Annual salary and/or allowance (RMB)
Executive Director	
Zhang En Rong	220,000
Lin Fu Long	160,000
Zhang Yun San	150,000
Xie Xin Cang	120,000
Non-executive Director	
Chen Jian Xiong	0
Wang Ping	0
Independent Non-executive Director	
Qin Xue Chang	30,000
Yan Yi Zhuang	62,400
Loke Yu alias Loke Hoi Lam	62,400
Supervisor	
Li Bao Hui	70,000
Liu Wan Fu	20,000
Fan Ren Yi	10,000

- (iii) subject to resolution passed at the Shareholders' meeting of the Company, the remuneration of each of the Directors and Supervisors may be changed;
- (iv) each of the Directors and Supervisors is entitled to out-of-pocket expenses reasonably incurred during his/her term of office;
- (v) the actual salary payable to each of the executive Directors is subject to adjustment dependent upon the results of the internal review of the executive Directors concerned; and
- (vi) each of the executive Directors is entitled to such bonus as decided by the Board, calculated by reference to the operating results of the Company as a whole and the performance of the executive Directors.

Save as disclosed above, none of the Directors has or is proposed to have a service contract with the Company or any of its subsidiaries in the capacity of a director which is not determinable by the Group within one (1) year without the payment of compensation other than statutory compensation.

Directors' and Supervisors' Interest in Contracts

No contracts of significance to which the Company, any of its holding companies, fellow subsidiaries or subsidiaries was a party and in which a Director or a Supervisor has a material interest and which is significant to the Group's business, whether directly or indirectly, subsisted at the date of this circular. None of the Directors or their respective associates has any competing interest (as would be required to be disclosed under Rule 11.04 of the GEM Listing Rules if each of them were a controlling shareholder of the Company for the purpose of the GEM Listing Rules).

Competing interests

None of the management Shareholders, the Directors nor their respective associates has any business or interest which competes or may compete with the Group.

Substantial Shareholders

As at the Latest Practicable Date, so far as is known to any Directors, Supervisors or chief executive of the Company, the following persons (other than a Director, Supervisor or chief executive of the Company) had, or were deemed or taken to have interests or short positions in the shares or underlying shares and debentures of the Company which would fall to be disclosed to the Company and the Stock Exchange under the provisions of Divisions 2 and 3 of Part XV of the SFO and required to be entered in the register maintained by the Company pursuant to section 336 of the SFO:

Name	Type of interests	Number of shares	Percentage of domestic shares	Percentage of H shares	Percentage of total registered capital
Zhang Xiu Lan (<i>Note 1</i>)	Interests of spouse	279,517,000	69.58%	—	43.14%
Li Xiu Fen (<i>Note 2</i>)	Interests of spouse	34,216,000	8.52%	—	5.28%
Zhang Xin Lan (<i>Note 3</i>)	Interests of spouse	30,608,000	7.62%	—	4.72%
Li Bao Hui (<i>Note 4</i>)	Interests of spouse	21,410,000	5.33%	—	3.30%
Paul G. Desmarais (<i>Notes 5 and 6</i>)	Interest of controlled corporation	69,000,000	—	28.02%	10.65%
Nordex Inc. (<i>Notes 5 and 6</i>)	Interest of controlled corporation	69,000,000	—	28.02%	10.65%

Name	Type of interests	Number of shares	Percentage		Percentage of total registered capital
			of domestic shares	Percentage of H shares	
Gelco Enterprises Ltd. (Notes 5 and 6)	Interest of controlled corporation	69,000,000	—	28.02%	10.65%
Power Corporation of Canada (Notes 5 and 6)	Interest of controlled corporation	69,000,000	—	28.02%	10.65%
Power Financial Corporation (Notes 5 and 6)	Interest of controlled corporation	69,000,000	—	28.02%	10.65%
IGM Financial Inc. (Notes 5 and 6)	Interest of controlled corporation	69,000,000	—	28.02%	10.65%
RAB Energy Fund Limited (Notes 5 and 7)	Investment manager	33,832,000	—	13.74%	5.22%
Commonwealth Bank of Australia (Note 5)	Interest of controlled corporation	19,718,000	—	8.01%	3.04%
Martin Currie Investment Management Limited (Note 5)	Interest of controlled corporation	12,400,000	—	5.04%	1.91%
China Development Capital Partnership LP (Note 5)	Beneficial owner	12,400,000	—	5.04%	1.91%

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.

Note 6: Mackenzie Cundill Investment Management Ltd. is a wholly-owned subsidiary of Mackenzie Financial Corporation, which in turn is a wholly-owned subsidiary of Mackenzie Inc.. Mackenzie Inc. is a wholly-owned subsidiary of IGM Financial Inc. which in turn is owned as to 55.99% by Power Financial Corporation. Power Financial Corporation is owned as to 66.4% by 171263 Canada Inc. which in turn is a wholly-owned subsidiary of 2795957 Canada Inc. 2795957 Canada Inc. is a wholly-owned subsidiary of Power Corporation of Canada which in turn is owned as to 54.18% by Gelco Enterprises Ltd. Gelco Enterprises Ltd. is owned as to 94.95% by Nordex Inc., which in turn is owned as to 68% by Paul G. Desmarais.

Mackenzie Cundill Investment Management (Bermuda) Ltd. is a wholly-owned subsidiary of Mackenzie (Rockies) Corp., which in turn is a wholly-owned subsidiary of Mackenzie Financial Corporation.

By virtue of the SFO, Mackenzie Financial Corporation, Mackenzie Inc., IGM Financial Inc., Power Financial Corporation, 171263 Canada Inc., 2795957 Canada Inc., Power Corporation of Canada, Gelco Enterprises Ltd., Nordex Inc. and Paul G. Desmarais are deemed to be interested in the 60,000,000 H Shares held by Mackenzie Cundill Investment Management Ltd. and 9,000,000 H Shares held by Mackenzie Cundill Investment Management (Bermuda) Ltd.

Note 7: According to its Form 2 filed on 27 May 2005, RAB Energy Fund Limited derives all or part of its interest in the 33,832,000 H Shares from certain cash settled equity derivatives which are listed on a stock exchange or traded on a futures exchange.

Save as disclosed above, so far as is known to the Directors, Supervisors or chief executive of the Company, no other person (not being a Director, Supervisors or chief executive of the Company) had any interests or short positions in shares or underlying shares of the Company which would fall to be disclosed to the Company and the Stock Exchange, under the provisions of Divisions 2 and 3 of Part XV of the SFO and required to be entered in the register maintained by the Company pursuant to section 336 of the SFO.

2. MATERIAL ADVERSE CHANGE

The Directors are not aware of any material adverse change in the financial position or trading prospects of the Group since 30 April 2006, the date to which the latest audited financial statements of the Group were made up.

3. LITIGATION

As at the Latest Practicable Date, neither the Company nor any of its subsidiaries was engaged in any litigation or arbitration of material importance and no litigation, arbitration or claim of material importance was known to the Directors to be pending or threatened by or against the Company or any of its subsidiaries.

4. CONSENT AND EXPERT

The following is the qualification of the professional adviser who has given opinion or advice, which is contained in this circular:

Name	Qualification
China Everbright Capital Limited	Licensed under the SFO for type 1 (dealing in securities) and type 6 (advising on corporate finance) as defined under the SFO

China Everbright Capital Limited has given and has not withdrawn its written consent to the issue of this circular with the inclusion of its letter and the references to its name in the form and context in which it appears.

As at the Latest Practicable Date, (i) China Everbright Capital Limited did not have any interest, either direct or indirect, in any assets which have been, since the date to which the latest published audited financial statements of the Company were made up, acquired or disposed of by, or leased to any member of the Group or are proposed to be acquired or disposed of by, or leased to, any member of the Group and (ii) China Everbright Capital Limited did not have any shareholding interests, beneficially or non-beneficially, in any member of the Group and it did not have any right, whether legally enforceable or not, to subscribe for or nominate any persons to subscribe for securities of any members of the Group.

5. DOCUMENTS FOR INSPECTION

Copies of the following documents will be available for inspection at the office of Coudert Brothers in association with Orrick, Herrington & Sutcliffe LLP on the 39th Floor, Gloucester Tower, The Landmark, 11 Pedder Street, Central, Hong Kong during normal business hours on any weekday (except public holidays) from the date of this circular up to and including 3 November 2006:

- (a) the letter of recommendation from the Independent Board Committee, the text of which is set out on page 21 of this circular;
- (b) the letter issued by China Everbright Capital Limited, the text of which is set out on pages 22 to 27 of the circular;
- (c) the service contracts of the Directors and Supervisors referred to in paragraph headed "Directors and Supervisors' Service Contracts" of this appendix;
- (d) the Supplemental Agreement;
- (e) the articles of association of the Company;
- (f) the Casting Supply Agreement; and
- (g) the Listing Document.

6. GENERAL

- (i) The legal address and head office of the Company is No. 99 Beihai Road, Shouguang City, Shandong Province, the People's Republic of China.
- (ii) The principal place of business of the Company in Hong Kong is Suite A, 11th Floor, Ho Lee Commercial Building.
- (iii) The Company's H share registrar and transfer office in Hong Kong is Tricor Investor Services Limited, at 26th Floor, Tesbury Centre, 28 Queen's Road East, Hong Kong.
- (iv) The qualified accountant and company secretary of the Company is Mr. Chan Wing Nang, Billy.

Mr. Chan Wing Nang, Billy (陳永能先生), aged 45, is the qualified accountant and company secretary of the Company. Mr. Chan graduated from the University of Newcastle upon Tyne, United Kingdom with a bachelor degree in Civil Engineering in 1986. He also read a master degree in business administration at the University of Warwick, United Kingdom. Mr. Chan is a member of the Hong Kong Institute of Certified Public Accountants and The Institute of Chartered Accountants in England and Wales. Mr. Chan has over 10 years of experience in the accounting and consulting field. Prior to joining the Group, Mr. Chan was a director in a consulting company. Mr. Chan joined the Group 13 December 2004.

- (v) The compliance officer of the Company is Mr. Xie Xincang.
- (vi) The Company has established an audit committee of the Board with written terms of reference in compliance with GEM Listing Rules 5.23 to 5.25. The primary duties of the audit committee are to review the Company's annual reports and accounts, half-year reports and quarterly reports and to provide advice and comments thereon to the Board. The audit committee will also be responsible for reviewing the financial reporting process and internal control systems of the Company.

The audit committee presently has three members, who are the three independent non-executive Directors, namely Mr. Qin Xue Chang, Mr. Yan Yi Zhuang and Mr. Loke Yu. The background of the audit committee members are as follows:

Mr. Qin Xue Chang (秦學昌先生), aged 41, is an independent non-executive Director and the Chairman of the Audit Committee. Mr. Qin has over 10 years of experience in accounting and auditing industry. He received his bachelor degree in economics from Shanxi University of Finance and Economics and is a practicing certified public accountant in the PRC. Mr. Qin is a director and deputy chief accountant of Beijing Yongtuo Certified Public Accountants Co., Ltd., and general manager of Shandong Branch Office, Beijing Yongtuo Certified Public Accountants Co., Ltd. He is also the Chairman of Shandong Hengchang Auction Co., Ltd. He was appointed as an independent non-executive Director on 29 March 2003 and was re-appointed as an independent non-executive Director on 12 May 2006.

Mr. Yan Yi Zhuang (閻翊莊先生), aged 49, is an independent non-executive Director and the Chairman of the Nomination Committee. He is also a operation manager of Shougang Concord Technology Holdings Ltd., a company listed on the Main Board of the Stock Exchange. Mr. Yan has over 10 years of management experience in electronics technology and graduated from the University of Western Sydney, Australia. Mr. Yan was appointed as an independent non-executive Director on 29 March 2003 and was re-appointed as an independent non-executive Director on 12 May 2006.

Mr. Loke Yu alias Loke Hoi Lam (陸海林先生), aged 57, is an independent non-executive Director and a chairman of the Remuneration committee of the Company. Mr. Loke has over 30 years' of experience in accounting and auditing for private and public companies, financial consultancy and corporate management. He holds a Master of Business Administration Degree from Universiti Teknologi Malaysia and a Doctor of Business Administration Degree from University of South Australia. He is a Fellow of The Institute of Chartered Accountants in England and Wales; a Fellow of Hong Kong Institute of Certified Public Accountants; and a Fellow of The Hong Kong Institute of Directors. He is also an Associate member of The Hong Kong Institute of Chartered Secretaries and a member of the Malaysian Institute of Accountants. He is an independent non-executive director of United Metals Holdings Limited (a Main Board listed issuer), New Chinese Medicine Holdings Limited (a GEM Board listed issuer), Matrix Holdings Limited (a Main Board listed issuer), China Fire Safety Enterprise Group Holdings Limited (a GEM Board Listed issuer), Yanion International Holdings Limited (a Main Board listed issuer) and Wealthmark International (Holdings) Limited (a Main Board listed issuer), companies listed on the Stock Exchange.



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)

NOTICE IS HEREBY GIVEN THAT an extraordinary general meeting of Shandong Molong Petroleum Machinery Company Limited (the “**Company**”) will be held at No. 99 Beihai Road, Shouguang City, Shandong Province, the People's Republic of China on 5 December 2006 at 9:00 a.m. for the purposes of considering and, if thought fit, with or without modification, passing the following resolutions each as an ordinary or special resolution (as the case may be) of the Company:

SPECIAL RESOLUTIONS

1. “**THAT** conditional upon (1) the Listing Committee of The Stock Exchange of Hong Kong Limited (the “**Stock Exchange**”) granting approval of the listing of, and permission to deal in, on the main board (the “**Main Board**”) of the Stock Exchange the 246,276,000 H Shares of RMB0.10 each in the issued share capital of the Company (the “**H Shares**”) (the “**Proposed Introduction**”); (2) the China Securities Regulatory Commission granting approval of the listing of the H Shares in issue on the Main Board; (3) the publication by the Company of a notice in respect of the proposed withdrawal of listing of the H Shares on the Growth Enterprise Market of the Stock Exchange (“**GEM**”) (the “**Proposed Withdrawal**”) which shall be published at least five clear business days from the date on which the shareholders of the Company shall have approved the Proposed Withdrawal; (4) the GEM Listing Committee of the Stock Exchange granting a waiver for the reduction of the notice period required under Rule 9.19(3) to at least five clear business days from the date on which the shareholders of the Company shall have approved the Proposed Withdrawal and the fulfillment of such waiver by the Company; and (5) the obtaining of all other relevant consents (if any) which are required in connection with the implementation of the Proposed Withdrawal and the Proposed Introduction and the fulfillment of all conditions which may be attached to such consents, the Proposed Introduction be and is hereby approved and confirmed; the listing of the H Shares on GEM shall cease with effect from such date and time as the directors of the Company (the “**Directors**”) may designate and any Director or the company secretary of the Company be and is hereby authorised generally to do all such acts for and on behalf of the Company as he/she may deem necessary, desirable or expedient to effect and implement the foregoing; and the notice period required under Rule 9.19(3) of the Rules Governing the Listing of Securities on The Growth Enterprise Market of the Stock Exchange in connection with the Proposed Withdrawal be reduced to at least five clear business days from the date on which the shareholders of the Company shall have approved the Proposed Withdrawal.”

* For identification purpose only

NOTICE OF EGM

2. “**THAT** conditional upon the listing of the H Shares (as defined in resolution No. 1 set out in this notice) on the Main Board of the Stock Exchange:

(1) there be granted to the board of directors of the Company (“**Board**”) an unconditional general mandate (“**General Mandate**”) to issue, allot and deal with additional shares in the capital of the Company and to make or grant offers or agreements in respect thereof, subject to the following conditions:

(a) such mandate shall not extend beyond the Relevant Period save that the Board may during the Relevant Period make or grant offers or agreements which might require the exercise of such powers after the end of the Relevant Period;

(b) the aggregate nominal amount of shares allotted or agreed conditionally or unconditionally to be allotted (whether pursuant to an option or otherwise) by the Board otherwise than pursuant to any scrip dividends or similar arrangement providing for the allotment of such shares in lieu of the whole or part of a dividend on such shares or any share option scheme adopted by the Company and in accordance with the articles of association of the Company (“**Articles of Association**”), shall not exceed:

(i) 20 per cent of the aggregate nominal amount of Domestic Shares of the Company in issue; and

(ii) 20 per cent of the aggregate nominal amount of H Shares of the Company in issue, in each case as at the date of passing of this resolution; and

(c) the Board will only exercise its power under such mandate in accordance with the Company Law of the People’s Republic of China (the “**PRC**”) and the Listing Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (as the same may be amended from time to time) and only if all necessary approvals from the China Securities Regulatory Commission and/or other relevant PRC government authorities are obtained;

For the purposes of this resolution:

“Domestic Share(s)” mean the ordinary domestic share(s) with a nominal value of RMB0.10 each in the registered share capital of the Company which are subscribed for in RMB;

“H Shares” mean the overseas listed foreign invested shares with a nominal value of RMB0.10 each in the registered share capital of the Company, which are listed on The Stock Exchange of Hong Kong Limited and subscribed for and traded in Hong Kong dollars;

NOTICE OF EGM

“Relevant Period” means the period from the date of passing this resolution until the earlier of:

- (a) the conclusion of the next annual general meeting of the Company following the passing of this resolution; or
- (b) the passing of a special resolution of the Company in a general meeting revoking or varying the authority set out in this resolution.

(2) contingent on the Board resolving to issue shares pursuant to paragraph (1) of this resolution, the Board be authorised:

- (a) to approve, execute and do, or procure to be executed and done all such documents and matters which it may consider necessary in connection with the issue of such new shares, including but not limited to the time, quantity and place for such issue, to make all necessary applications to the relevant authorities, and to enter into underwriting agreement(s) or any other agreement(s);
- (b) to determine the use of proceeds and to make necessary filings and registration with the relevant authorities in the PRC, and/or Hong Kong and any other places and jurisdictions (as appropriate);
- (c) to increase the registered capital of the Company and make any amendments to the Articles of Association in accordance with such increase and to register the increased capital with the relevant authorities in the PRC and/or Hong Kong and any other places and jurisdictions (as appropriate) so as to reflect the new capital and/or share capital structure of the Company resulting from the intended allotment and issue of the shares of the Company pursuant to paragraph (1) of this resolution.

(3) the general mandate to issue H Shares granted to the Directors as set out in the notice of the annual general meeting of the Company held on 12 May 2006 be and is hereby revoked.”

3. **“THAT** conditional upon the listing of the H Shares (as defined in resolution No. 1 set out in this notice) on the Main Board of the Stock Exchange, amendments shall be made to the existing articles of association of the Company (the **“Existing Articles”**), with effect from the date on which dealings in the H Shares on the Main Board of the Stock Exchange commences and the amendments to the Existing Articles are approved by the Ministry of Commerce (whichever is later). The details of the amendments are as follows:

(i) the first paragraph of Article 6 of the Existing Articles shall be deleted in its entirety and replaced by the following:

“The Articles will take effect upon obtaining the approval from the shareholders’ meeting and the relevant state authority in charge.”;

NOTICE OF EGM

- (ii) Articles 44(1) and (2) of the Existing Articles shall be deleted in their entirety and replaced by the following:

“(1) payment of a fee of HK\$2.50 (per transfer document), or such amount as may from time to time be requested by the board of directors which does not exceed the maximum amount as required under the Listing Rules of The Stock Exchange of Hong Kong Limited from time to time, to the Company for the registration of any transfer document(s) and other document(s) relating to or affecting the ownership of the shares in question;

(2) the transfer document relates only to overseas listed foreign shares listed in the Main Board of The Stock Exchange of Hong Kong Limited;”;

- (iii) Paragraph 2 of Article 48 of the Existing Articles shall be deleted in its entirety and replaced by the following:

“Where holders of domestic shares have lost their share certificates and apply for their replacement, the matter shall be dealt with under the provisions of Article 144 of the Company Law.”;

- (iv) Article 77(4) shall be inserted after Article 77(3) of the Existing Articles as follows:

“(4) the Directors and/or Chairman of the Meeting who, individually or collectively, hold proxies in respect of shares representing 5% or more of the total voting rights at a particular meeting (and if on a show of hands a meeting votes in the opposite manner to that instructed in those proxies).”;

- (v) the words “next annual general meeting” in the sixth paragraph of Article 101 of the Existing Articles shall be deleted and replaced with the words “next general meeting”;

- (vi) Paragraphs 1 and 2 of Article 106 of the Existing Articles shall be deleted in its entirety and replaced by the following:

“Regular meetings of the Board of Directors shall be convened at least four times every year. Such meetings shall be convened by the chairman of the Board of Directors by giving notice to all the Directors fourteen (14) days before the meeting date.

Under any of the following circumstances, the chairman of the Board of Directors shall convene the extraordinary board meetings within fourteen (14) days:”;

- (vii) the words “ten (10) days” in each of Articles 107(2) and (3) of the Existing Articles shall be deleted and replaced with the words “fourteen (14) days”;

NOTICE OF EGM

(viii) the words “social economic order” in Article 132(2) of the Existing Articles shall be deleted and replaced with the words “Socialist market economic order”;

(ix) the words “Article 54” in Article 139 shall be deleted and replaced with the words “Article 55”;

(x) Article 143(1) of the Existing Articles shall be deleted in its entirety and replaced by the following:

“the provision of a loan or a guarantee for a loan by the Company to a company which is a subsidiary of the Company;”;

(xi) Article 143(2) of the Existing Articles shall be deleted in its entirety;

(xii) Articles 148(1) and (2) of the Existing Articles shall be deleted in their entirety and replaced by the following:

“(1) emoluments in respect of his service as a Director, Supervisor, or senior officer of the Company;

(2) emoluments in respect of his service as a Director, Supervisor or senior officer of any subsidiary of the Company;”;

(xiii) the words “Article 55” in Article 149(2) of the Existing Articles shall be deleted and replaced with the words “Article 56”;

(xiv) Article 156 shall be deleted in its entirety and replaced by the following:

“The Company shall despatch the directors’ report and its annual accounts and the auditors’ report for the purpose of its annual accounts to the shareholders of the Company at least twenty-one (21) days before the date of the annual general meeting and within one hundred and twenty (120) days after the end of the accounting year.

The Company shall prepare its interim report for the first six months of the accounting year which at least complies with the required information set out in the Main Board Listing Rules and despatch the same within sixty (60) days after the end of the first six (6) months of the accounting year.”;

(xv) the words “five (5) days later” in Article 208 of the Existing Articles shall be deleted and replaced with the words “on that date”;

NOTICE OF EGM

(xvi) the consequential amendments to the margin notes to the effect that all references to “Appendix 11C to the Listing Rules” in the Existing Articles shall be deleted and replaced with “Appendix 13D to the Listing Rules”; and

THAT the Directors be and are hereby authorized to do such other acts and things, enter into all such transactions and arrangements, execute such other documents and/or deeds and/or take all such steps, which in their opinion may be necessary, desirable or expedient to amend the Existing Articles further, as the Directors may deem appropriate and necessary, and file or register the amended Existing Articles (subject to further amendments (if any) being made to the same by the Directors) with the relevant authorities of the PRC and Hong Kong, if required.”

ORDINARY RESOLUTIONS

4. **“THAT** a conditional agreement (the **“Supplemental Agreement”**) entered into between the Company and 壽光墨龍機電設備有限公司 (Shouguang Molong Electromechanical Equipment Company Limited) on 22 September 2006 in relation to the extension of the term of the agreement dated 20 March 2004 between the same parties, to 31 December 2007, the continuing connected transactions contemplated thereunder and the proposed annual caps for the continuing connected transactions contemplated thereunder, be and are hereby approved, confirmed and ratified; and any director of the Company be and is hereby authorized to execute the Supplemental Agreement and do such other acts and things and execute such other documents which in his opinion may be necessary or desirable to implement the Supplemental Agreement for and on behalf of the Company.”
5. **“THAT** the board of directors of the Company be and is hereby authorised to declare and pay an interim dividend of RMB1.5 cents per share in respect of the six months ended 30 June 2006, to shareholders whose names appear on the register of members of the Company on 4 December 2006 (the **“Dividend Declaration and Payment”**); and

THAT the directors of the Company be and are hereby authorized to do such other acts and things, enter into all such transactions and arrangements, execute such other documents and/or deeds and/or take all such steps, which in their opinion may be necessary, desirable or expedient to implement the Dividend Declaration and Payment.”

By Order of the Board
Shandong Molong Petroleum Machinery Company Limited
Zhang En Rong
Chairman

Shandong, 19 October 2006
The People's Republic of China

NOTICE OF EGM

Notes:

- (A) The H Share register of the Company will be closed from 5 November 2006 to 5 December 2006 (both days inclusive), during which no transfer of H Shares will be effected. Any holders of H Shares of the Company, whose names appear on the Company's H Share register at the close of business on 3 November 2006, are entitled to attend and vote at the EGM after completing the registration procedures for attending the meeting. In order to be entitled to attend and vote at the EGM, share transfer documents should be lodged with the Company's H Share registrar not later than 4:00 p.m. on 3 November 2006.

The address of the Company's H Share registrar, Tricor Investor Services Limited, is as follows:

26th Floor
Tesbury Centre
28 Queen's Road East
Hong Kong

- (B) Holders of H Shares and Domestic Shares, who intend to attend the EGM, must complete the reply slips for attending the EGM and return them to the registered office of the Company (for holders of Domestic Shares), or to the Company's H Share registrar, Tricor Investor Services Limited (for holders of H Shares) not later than 20 days before the date of the EGM, i.e. no later than 14 November 2006.

Details of the registered office of the Company are as follows:

No.99 Beihai Road
Shouguang City
Shandong Province
The People's Republic of China

- (C) Each holder of H Shares who has the right to attend and vote at the EGM is entitled to appoint in writing one or more proxies, whether a shareholder or not, to attend and vote on his behalf at the EGM. A proxy of a shareholder who has appointed more than one proxy may only vote on a poll.
- (D) The instrument appointing a proxy must be in writing under the hand of the appointor or his attorney duly authorised in writing. If that instrument is signed by an attorney of the appointor, the power of attorney authorising that attorney to sign, or other documents of authorisation, must be notarially certified.
- (E) To be valid, the form of proxy, and if the form of proxy is signed by a person under a power of attorney or other authority on behalf of the appointor, a notarially certified copy of that power of attorney or other authority, must be delivered to the Company's H Share registrar, Tricor Investor Services Limited, on the 26th Floor, Tesbury Centre, 28 Queen's Road East, Hong Kong, not less than 24 hours before the time for holding the EGM or any adjournment thereof in order for such documents to be valid.

NOTICE OF EGM

- (F) Each holder of Domestic Shares is entitled to appoint in writing one or more proxies, whether a shareholder or not, to attend and vote on its behalf at the EGM. Notes (C) to (D) also apply to holders of Domestic Shares, except that the proxy form or other documents of authority must be delivered to the Office of the Secretary to the Board of Directors, the address of which is set out in Note (B) above, not less than 24 hours before the time for holding the EGM or any adjournment thereof in order for such documents to be valid.

- (G) If a proxy attends the EGM on behalf of a shareholder, he should produce his ID card and the instrument signed by the proxy or his legal representative, which specifies the date of its issuance. If the legal representative of a legal person shareholder attends the EGM, such legal representative should produce his/her ID card and valid documents evidencing his capacity as such legal representative. If a legal person shareholder appoints a representative of a company other than its legal representative to attend the EGM, such representative should produce his ID card and an authorization instrument affixed with the seal of the legal person shareholder and duly signed by its legal representative.

- (H) The EGM is expected to last for half a day. Shareholders attending the EGM are responsible for their own transportation and accommodation expenses.



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)

H Shares Class Meeting

NOTICE IS HEREBY GIVEN THAT a class meeting (the “**Class Meeting**”) of the holders of the H Shares of Shandong Molong Petroleum Machinery Company Limited (the “**Company**”) will be held at No. 99 Beihai Road, Shouguang City, Shandong Province, the People's Republic of China on 5 December 2006 at 10:00 a.m. for the purposes of considering and, if thought fit, with or without modification, passing the following special resolution:

SPECIAL RESOLUTION

“**THAT** conditional upon (1) the Listing Committee of The Stock Exchange of Hong Kong Limited (the “**Stock Exchange**”) granting approval of the listing of, and permission to deal in, on the main board (the “**Main Board**”) of the Stock Exchange the 246,276,000 H Shares of RMB0.10 each in the issued share capital of the Company (the “**H Shares**”) (the “**Proposed Introduction**”); (2) the China Securities Regulatory Commission granting approval of the listing of the H Shares on the Main Board; (3) the publication by the Company of a notice in respect of the proposed withdrawal of listing of the H Shares on the Growth Enterprise Market of the Stock Exchange (“**GEM**”) (the “**Proposed Withdrawal**”) which shall be published at least five clear business days from the date on which the shareholders of the Company shall have approved the Proposed Withdrawal; (4) the GEM Listing Committee of the Stock Exchange granting a waiver for the reduction of the notice period required under Rule 9.19(3) to at least five clear business days from the date on which the shareholders of the Company shall have approved the Proposed Withdrawal and the fulfillment of such waiver by the Company; and (5) the obtaining of all other relevant consents (if any) which are required in connection with the implementation of the Proposed Withdrawal and the Proposed Introduction and the fulfillment of all conditions which may be attached to such consents, the Proposed Introduction be and is hereby approved and confirmed; the listing of the H Shares on GEM shall cease with effect from such date and time as the directors of the Company (“**Directors**”) may designate and any Director or the company secretary of the Company be and is hereby authorised generally to do all such acts for and on behalf of the Company as he/she may deem necessary, desirable or expedient to effect and implement the foregoing; and the notice period required under Rule 9.19(3) of the Rules

* For identification purpose only

NOTICE OF CLASS MEETING OF THE HOLDERS OF H SHARES

Governing the Listing of Securities on The Growth Enterprise Market of the Stock Exchange in connection with the Proposed Withdrawal be reduced to at least five clear business days from the date on which the shareholders of the Company shall have approved the Proposed Withdrawal.”

By Order of the Board
Shandong Molong Petroleum Machinery Company Limited
Zhang En Rong
Chairman

Shandong, 19 October 2006
The People's Republic of China

Notes:

- (A) The H Share register of the Company will be closed from 5 November 2006 to 5 December 2006 (both days inclusive), during which no transfer of H Shares will be effected. Any holders of H Shares of the Company, whose names appear on the Company's H Share Register at the close of business on 3 November 2006, are entitled to attend and vote at the Class Meeting after completing the registration procedures for attending the meeting. In order to be entitled to attend and vote at the Class Meeting, share transfer documents should be lodged with the Company's H Share registrar not later than 4:00 p.m. on 3 November 2006.

The address of the Company's H Share registrar, Tricor Investor Services Limited, is as follows:

26th Floor
Tesbury Centre
28 Queen's Road East
Hong Kong

- (B) Holders of H Shares, who intend to attend the Class Meeting, must complete the reply slips for attending the Class Meeting and return them to the Company's H Share registrar, Tricor Investor Services Limited not later than 20 days before the date of the Class Meeting, i.e. no later than 14 November 2006.
- (C) Each holder of H Shares who has the right to attend and vote at the Class Meeting is entitled to appoint in writing one or more proxies, whether a shareholder or not, to attend and vote on his behalf at the Class Meeting. A proxy of a shareholder who has appointed more than one proxy may only vote on a poll.
- (D) The instrument appointing a proxy must be in writing under the hand of the appointor or his attorney duly authorised in writing. If that instrument is signed by an attorney of the appointor, the power of attorney authorising that attorney to sign, or other documents of authorisation, must be notarially certified.

NOTICE OF CLASS MEETING OF THE HOLDERS OF H SHARES

- (E) To be valid, the form of proxy, and if the form of proxy is signed by a person under a power of attorney or other authority on behalf of the appointor, a notarially certified copy of that power of attorney or other authority, must be delivered to the Company's H Share registrar, Tricor Investor Services Limited, on the 26th Floor, Tesbury Centre, 28 Queen's Road East, Hong Kong, not less than 24 hours before the time for holding the Class Meeting or any adjournment thereof in order for such documents to be valid.
- (F) If a proxy attends the Class Meeting on behalf of a shareholder, he should produce his ID card and the instrument signed by the proxy or his legal representative, which specifies the date of its issuance. If the legal representative of a legal person shareholder attends the Class Meeting, such legal representative should produce his/her ID card and valid documents evidencing his capacity as such legal representative. If a legal person shareholder appoints a representative of a company other than its legal representative to attend the Class Meeting, such representative should produce his ID card and an authorization instrument affixed with the seal of the legal person shareholder and duly signed by its legal representative.
- (G) The Class Meeting is expected to last for half a day. Shareholders attending the Class Meeting are responsible for their own transportation and accommodation expenses.



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)

Domestic Shares Class Meeting

NOTICE IS HEREBY GIVEN THAT an class meeting (the “**Class Meeting**”) of the holders of domestic shares of Shandong Molong Petroleum Machinery Company Limited (the “**Company**”) will be held at No. 99 Beihai Road, Shouguang City, Shandong Province, the People’s Republic of China on 5 December 2006 at 11:00 a.m. for the purposes of considering and, if thought fit, with or without modification, passing the following special resolution:

SPECIAL RESOLUTION

“**THAT** conditional upon (1) the Listing Committee of The Stock Exchange of Hong Kong Limited (the “**Stock Exchange**”) granting approval of the listing of, and permission to deal in, on the main board (the “**Main Board**”) of the Stock Exchange the 246,276,000 H Shares of RMB0.10 each in the issued share capital of the Company (the “**H Shares**”) (the “**Proposed Introduction**”); (2) the China Securities Regulatory Commission granting approval of the listing of the H Shares on the Main Board; (3) the publication by the Company of a notice in respect of the proposed withdrawal of listing of the H Shares on the Growth Enterprise Market of the Stock Exchange (“**GEM**”) (the “**Proposed Withdrawal**”) which shall be published at least five clear business days from the date on which the shareholders of the Company shall have approved the Proposed Withdrawal; (4) the GEM Listing Committee of the Stock Exchange granting a waiver for the reduction of the notice period required under Rule 9.19(3) to at least five clear business days from the date on which the shareholders of the Company shall have approved the Proposed Withdrawal and the fulfillment of such waiver by the Company; and (5) the obtaining of all other relevant consents which are required in connection with the implementation of the Proposed Withdrawal and the Proposed Introduction and the fulfillment of all conditions which may be attached to such consents, the Proposed Introduction be and is hereby approved and confirmed; the listing of the H Shares on GEM shall cease with effect from such date and time as the directors of the Company (“**Directors**”) may designate and any Director or the company secretary of the Company be and is hereby authorised generally to do all such acts for and on behalf of the Company as he/she may deem necessary, desirable or expedient to effect and implement the foregoing; and the notice period required under Rule 9.19(3) of the Rules

* For identification purpose only

NOTICE OF CLASS MEETING OF THE HOLDERS OF DOMESTIC SHARES

Governing the Listing of Securities on The Growth Enterprise Market of the Stock Exchange in connection with the Proposed Withdrawal be reduced to at least five clear business days from the date on which the shareholders of the Company shall have approved the Proposed Withdrawal.”

By Order of the Board
Shandong Molong Petroleum Machinery Company Limited
Zhang En Rong
Chairman

Shandong, 19 October 2006
The People's Republic of China

Notes:

- (A) The Domestic Shares register of the Company will be closed from 5 November 2006 to 5 December 2006 (both days inclusive), during which no transfer of Domestic Shares will be effected. Any holders of Domestic Shares of the Company, whose names appear on the Company's Domestic Share register at the close of business on 3 November 2006, are entitled to attend and vote at the Class Meeting after completing the registration procedures for attending the Class Meeting.
- (B) Holders of Domestic Shares, who intend to attend the Class Meeting, must complete the reply slips for attending the Class Meeting and return them to the registered office of the Company not later than 20 days before the date of the Class Meeting, i.e. no later than 14 November 2006.

Details of the registered office of the Company are as follows:

No.99 Beihai Road
Shouguang City
Shandong Province
The People's Republic of China

- (C) Each holder of Domestic Shares who has the right to attend and vote at the Class Meeting is entitled to appoint in writing one or more proxies, whether a shareholder or not, to attend and vote on his behalf at the Class Meeting. A proxy of a shareholder who has appointed more than one proxy may only vote on a poll.
- (D) The instrument appointing a proxy must be in writing under the hand of the appointor or his attorney duly authorised in writing. If that instrument is signed by an attorney of the appointor, the power of attorney authorising that attorney to sign, or other documents of authorisation, must be notarially certified.

NOTICE OF CLASS MEETING OF THE HOLDERS OF DOMESTIC SHARES

- (E) To be valid, the form of proxy, and if the form of proxy is signed by a person under a power of attorney or other authority on behalf of the appointor, a notarially certified copy of that power of attorney or other authority, must be delivered to the Company's registered office, the address of which is set out in Note (B) above, not less than 24 hours before the time for holding the Class Meeting or any adjournment thereof in order for such documents to be valid.
- (F) If a proxy attends the Class Meeting on behalf of a shareholder, he should produce his ID card and the instrument signed by the proxy or his legal representative, which specifies the date of its issuance. If the legal representative of a legal person shareholder attends the Class Meeting, such legal representative should produce his/her ID card and valid documents evidencing his capacity as such legal representative. If a legal person shareholder appoints a representative of a company other than its legal representative to attend the Class Meeting, such representative should produce his ID card and an authorization instrument affixed with the seal of the legal person shareholder and duly signed by its legal representative.
- (G) The Class Meeting is expected to last for half a day. Shareholders attending the Class Meeting are responsible for their own transportation and accommodation expenses.