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### INTRODUCTION

The Company was ranked seventh among oil well pipe manufacturers in China in terms of output and was also one of the leading oil well pipe manufacturers in China for 2005, according to the China Iron and Steel Association. The Company has experienced strong financial growth since it started to sell oil well pipes (a type of specialized seamless pipes which are characterised by their high quality, durability and safety standards). The profit before income tax for the two years ended 31 December 2005 and the six months ended 30 June 2006 was approximately RMB24.6 million, RMB96.3 million and RMB81.1 million respectively. The Directors believe that the strong growth in profit is attributable to the Company's focus on the production and sales of oil well pipes. The Directors also believe that continued specialisation in the production and sales of oil well pipes will underpin the Company's development in the future.

The Company classifies its products into two main categories: (i) specialized seamless pipes for the oil and natural gas industry, including oil well pipes (mainly oil transfer pipes and casing pipes etc.) and petrochemical pipes; and (ii) other specialized seamless pipes which include vessel pipes and boiler pipes, etc. Oil well pipes represented 1.7%, 51.8% and 56.8% of the Company's revenue for the two financial years ended 31 December 2005 and the six months ended 30 June 2006. Other products accounted for 98.3%, 48.2% and 43.2% of the Company's sales for the two financial years ended 31 December 2005 and the six months ended 30 June 2006.

A majority of the Company's revenue for the financial year ended 31 December 2005 and the six months ended 30 June 2006 came from the sales of specialized seamless pipes to the oil and natural gas industry. For the two financial years ended 31 December 2005 and the six months ended 30 June 2006, sales to the oil and natural gas industry accounted for approximately 22.5%, 60.3% and 63.7% of the Company's sales. It is expected that the Company's revenue contribution from oil well pipes will grow significantly going forward when the Company's utilisation of its oil well pipe production capacity continues to increase and its oil well pipe heat processing and threading value-added production lines commence operation. Additional value-added service, such as threading, is required for all oil well pipes before being used on site at oil wells. Upon commencement of such additional value-added service, the Company expects that it will then be able to deliver finished products for direct use by oil fields.

The Company has more than 13 years of experience in the manufacture, sourcing and distribution of specialized seamless pipes. Although oil well pipes became the Company's principal product in 2005, the Company's first involvement in the oil well pipes business commenced in 2000 when it first conducted feasibility studies involving technological support for and market research in the production and sale of oil well pipes. Between 2002 and 2004, the Company focused on the planning for the establishment of hot-rolled oil well pipe production lines. The Company's hot-rolled oil well pipe production line in Chuzhou was established at the end of 2004 and it then began production of oil well pipes in January 2005 when the hot-rolled oil well pipe production line was put into commercial production and the Company has since then established its reputation in the oil and natural gas industry in China for its ability to manufacture high quality oil well pipes. The award of the Product

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Inspection Waiver received at the end of 2005 (and valid until December 2008) as well as its API certification obtained are testaments to the high quality of the Company's products and production processes.

The Company has also devoted resources to maintaining the quality of its other specialized seamless pipe products in line with international standards by adopting advanced production techniques and equipment, as well as strict control of testing and inspection. Throughout the years, the Company has obtained various recognitions for the production of other specialized seamless pipes including vessel pipes and boiler pipes etc., and received plant certifications from shipping classification societies of various countries, various production licences as well as certifications from international standards organisations such as ISO9001 and certifications by other overseas institutions.

The Company's business model involves two segments, namely sales of self-produced oil well pipes and other specialized seamless pipes, and sourcing and distributing specialized seamless pipes. The Company strives to provide an integrated service to its customers by purchasing specialized seamless pipes that it does not manufacture by sourcing and purchasing for customers to fulfill the customers' requirements in their purchase orders.

### COMPETITIVE ADVANTAGES

The Directors consider that the success of the Company is primarily attributable to the following principal factors:

#### **1. Focused line of business**

The specialized seamless pipe industry, especially for the oil well pipe segment, is a fast growing and technically specialized industry. A focused line of business strategy is the Company's key advantage over its major competitors who are all state-owned enterprises. These state-owned enterprises have a wide range of products and the Directors believe that specialized seamless pipes only account for a small portion of their product portfolio. Compared with these enterprises, the Company has focused on the production and development of specialized seamless pipes for over 13 years, and achieved a leading position in the PRC's high growth specialized seamless pipe industry, whilst continuing to increase its market share in the oil well pipe sector. The Directors believe that a focused line of business has enabled the Company to concentrate its resources on product and service development as well as established the Company as a specialist on quality specialized seamless pipe products.

#### **2. Successful market oriented business strategy**

The successful launch of oil well pipes in 2005 was the result of the Company's direct sales strategy to develop its customer base. With the support of 29 dedicated sales and marketing team members, the Company maintains close relationships with its customers and has a better understanding of its customers' requirements as well as better market awareness. It also leveraged its technical expertise and market awareness in developing specialized seamless pipes to produce higher margin oil well pipe

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products that serve the rapidly expanding oil and gas exploration industry, thereby making inroads to supplying leading petrochemical companies in China, including the PetroChina and Sinopec group of companies.

### **3. Strong sourcing and distribution capabilities to provide one-stop shop service**

The Company provides a one-stop shop service to its customers by not only selling self-produced pipes but also helping customers to source and distribute other specialized seamless pipe. The Company continues to develop its operational expertise in maintaining and servicing an extensive logistic and sourcing network. As at 30 June 2006, the Company had 10 personnel dedicated to sourcing and distribution and acquired premises of approximately 258,507 sq.m. and a warehouse of approximately 31,522 sq.m. from which it has set up its distribution and logistics centre. This one-stop shop service has not only enhanced the strong relationships with its clients, improved the Company's profitability and enlarged the Company's product range, but it has also enabled the Company to get the most up-to-date market information in specialized seamless pipe industry by way of better communication with its clients. By closely monitoring the market trends and industrial developments, the Company can further expand its client base, timely adjust its product portfolios, and seek suitable merger and acquisition targets for further growth.

### **4. Corporate branding and quality products**

The oil well pipe industry requires high quality, durability and safety standards, hence the quality of products and the branding reputation are important in this industry.

The Company was ranked seventh among oil well pipe manufacturers in China in terms of output and was also one of the leading oil well pipe manufacturers in China for 2005. The Directors believe that corporate reputation and goodwill are essential factors for success in this industry which in turn are driven by customer acknowledgement and acceptance of the quality of its products and timely delivery. The Directors believe that the fact the Company was awarded the Product Inspection Waiver in December 2005 made it a preferred supplier of many large petrochemical companies in the PRC and also enabled the Company to increase its exports. Internationally, the Company has also obtained API certification from the American Petroleum Institute which is only granted to companies which are recognised as quality producers with regard to their equipment, products and services relating to the oil and gas industry. Further, the Company's production plants have been recognized by national shipping registers such as the China Classification Society in the PRC, Det Norske Veritas in Norway, Lloyd's Register in the United Kingdom, Germanischer Lloyd in Germany, American Bureau of Shipping, Bureau Veritas in France and similar certifications in South Korea. The Company is in the process of applying for similar certification in Japan. To reinforce its corporate branding in the market, the Company's logo is printed on each of its self-produced products. The Directors believe that its brand enhances customer loyalty and provides the Company with a solid platform for a further expansion of its sales network, product range and services.

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### **5. Experienced senior management team together with strong technology know-how and technical expertise**

The senior management team of the Company has demonstrated experience in, and market knowledge of, the PRC specialized seamless pipe industry. The Company's senior management team has over 13 years of experience in the production of specialized seamless pipe, bringing with them in-depth product knowledge and strong technical know-how. In addition, they possess extensive knowledge in the production, quality control, marketing and distribution of the Company's products.

The making of specialized seamless pipe requires advanced technology and technical know-how which are entry barriers to the industry for new competitors. Therefore, the Company's technical expertise reinforces its market position and competitive edge.

In addition to the above, the Company's ability to design its own production lines, coupled with its efforts in increasing production efficiency through such production expertise, has enabled it to modify, improve and enhance the design of its products to cater for different needs of its customers and the general market at relatively lower costs.

### **6. Competitive cost structure**

Besides product quality, the Company believes that price is another key competitive factor in the oil well pipe industry. Its low cost structure, attributable to its production and technical know-how and its strategic location, enables it to have more flexibility in pricing its products.

The Company's production equipment are domestically sourced, assembled and upgraded by itself through utilising its production know-how. Under the premise of adequate quality assurance, a substantial amount of investment cost is saved when compared with imported equipment. The Company's new production facilities are strategically located at Chuzhou, Anhui Province, where natural gas, an important production factor to the Company, is relatively cheaper. Further, the Company's production facilities are situated on the bank of Changjiang river near a rail station of the Jinghu railway (Beijing-Shanghai Railway) as well as two highways through which the Company may obtain its raw materials and deliver its products conveniently throughout the PRC. The Directors believe that the Company's unique strategic location in Chuzhou provides it with logistical advantages over its competitors. In addition, the Company adopts a set of strict control mechanisms over costs. The Company has adopted JIT purchasing procedures, which saves inventory costs to a significant extent.

### **7. Participation in an industry which is a sector encouraged by the PRC Government**

The Company's business has benefited from the policies of the PRC Government. In July 2005, the National Development and Reform Commission of the PRC published its future policy in relation to the development of the steel industries in the PRC. The

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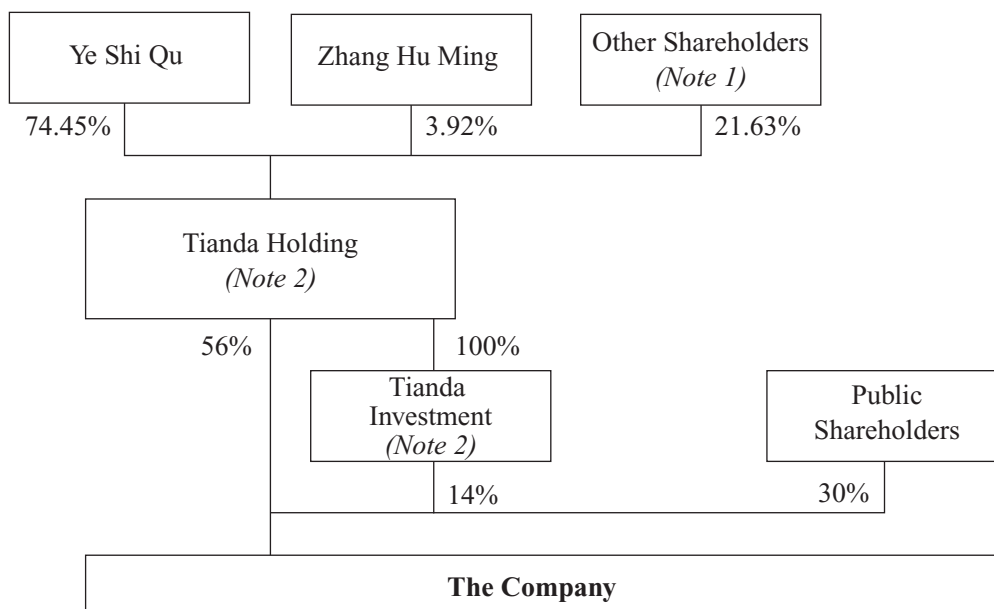
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production of oil well pipes for use in the oil and natural gas industry as well as boiler pipes are specifically highlighted by the National Development and Reform Commission of the PRC as an encouraged production industry. The State Council of the PRC has also, in 2006, indicated its intention to strengthen exploration efforts of natural resources in the central part of the PRC, with particular emphasis on steel and petrochemical resources, amongst other things. Further, the State Council of the PRC also intends to increase its support to the research and development of PRC enterprises in mid-west China via investments in research and development, procurement of machinery and taxation policies. The Company's high value-added oil well pipes and petrochemical pipes expansion project has also been designated as part of the 861 Action Plan promoted and supported by the Anhui Provincial Government. Details of the 861 Action Plan are set out in the "Industry Overview" section.

### SHAREHOLDING AND COMPANY STRUCTURE

The shareholding structure of the Company immediately after the completion of the International Placing (assuming that the Over-allotment Option is not exercised) is as follows:



*Note 1:* Apart from Mr. Ye Shi Qu and Mr. Zhang Hu Ming, there are 47 other individual shareholders in Tianda Holding (who are all Tianda Holding's employees) holding an aggregate of 21.63% of Tianda Holding. The names for each of the 47 other individual shareholders and their respective equity interests in the Company after listing are set out in the section headed "Shareholding and Company Structure" in Appendix VIII to this prospectus.

*Note 2:* Tianda Holding and Tianda Investment undertook to the Company and the Stock Exchange that for a period commencing on the date of this prospectus and ending on the date which is 12 months from the Listing Date, it will not (i) dispose of (nor enter into any agreement to dispose of) or permit the registered holder to dispose of (or to enter into any agreement to dispose of) any of its direct or indirect interest in the Company; or (ii) otherwise create (nor enter into any agreement to create) or permit the registered holder to create (or to enter into any agreement to create) any options, rights, interests or encumbrances in respect of any such interest.

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### AWARDS AND CERTIFICATES

The Company obtained various certificates and approvals throughout its history of operations, details of which are as follows:

Country	Authority granting the certificate/approval	Description and Significance	Current validity period
PRC	Certificate of Works Approval certified by China Classification Society Nanjing Branch	Certification covers specialized seamless pipes to be used for construction of ships or installations classed with China Classification Society	April 2006–April 2010
	Product Inspection Waiver	The specialized seamless pipes produced by the Company passed the strict review by the State General Administration of Quality Supervision, Inspection and Quarantine and are exempted from the sampling inspection on production by the State General Administration of Quality Supervision, Inspection and Quarantine	December 2005–December 2008
	Production Licence for High Pressure Steel Tube issued by the State General Administration of the PRC for Quality Supervision, Inspection and Quarantine	Obtained qualification for the production of high pressure boiler and pressure vessel	November 2004–February 2009
	Production Licence for Low and Medium Pressure Boiler Tube Issued by the State General Administration of the PRC for Quality Supervision and Inspection and Quarantine	Obtained qualification for the production of low and medium pressure boiler and pressure vessel	November 2004–February 2009
	New product evaluated and certified by National Boiler and Pressure Vessels Technology Standardisation Committee	Obtained qualification for the production of 07Cr2AlMo, 09CrMoAL and passed the review by vessel standard quality assurance committee.	December 2003–December 2008

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Country	Authority granting the certificate/approval	Description and Significance	Current validity period
	Quality System Certification certified by China Quality Certification Centre ISO9001	A milestone on the management standard of the Company ranking top among enterprises in the PRC	August 2006–August 2009
	Production licence for stainless steel pipe issued by the General Administration of Quality Supervision, Inspection and Quarantine of the PRC	Obtained qualification for the production of stainless steel pipes	April 2003–April 2008
United States	Certification of Authority to use the Official API Monogram	Qualification of producing products using API Monogram was obtained after review according to the API quality system. Products can be widely applied in various oil fields within and outside the PRC	February 2006–February 2009
	Plant Certification certified by American Bureau of Shipping	Certification covers specialized seamless pipes to be used for construction of ships classed with American Bureau of Shipping	December 2002–December 2007
France	Approval Certificate on the factory certified by Bureau Veritas	Certification covers specified seamless pipes and fittings to be used for construction of ships classed with Bureau Veritas	January 2004–January 2009
Germany	Approval of Material Manufacturers	Certification covers specialized seamless pipe to be used for construction of ships classed with Germanischer Lloyd	April 2006–January 2009

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<b>Country</b>	<b>Authority granting the certificate/approval</b>	<b>Description and Significance</b>	<b>Current validity period</b>
Norway	Approved Manufacturer	Certification covers specialized seamless pipes to be used for construction of ships classed with Det Norske Veritas	July 2004–June 2008
South Korea	Plant certification certified by Korean Ship Classification Society	Certification covers specialized seamless pipes to be used for construction of ships or installations classed with Korean Register of Shipping	August 2006–August 2011
UK	Approved manufacturer certified by Lloyd's Register	Certification covers specialized seamless pipes to be used for construction of ships or installations classed with Lloyd's Register	May 2006–December 2008

The Company applied for similar certification in Japan on 21 June 2006 and the Company's products have to undergo examination, evaluation and classification. The Company expects that if the tests go as planned, it should obtain its certification by the end of 2006.

The Company's Chinese and international certifications date back to 2003. It is evident that its long experience in other specialized seamless pipes for vessels, boilers and others laid a solid foundation on which it subsequently obtained the Production Inspection Waiver in 2005 and certification from the American Petroleum Institute in 2006.



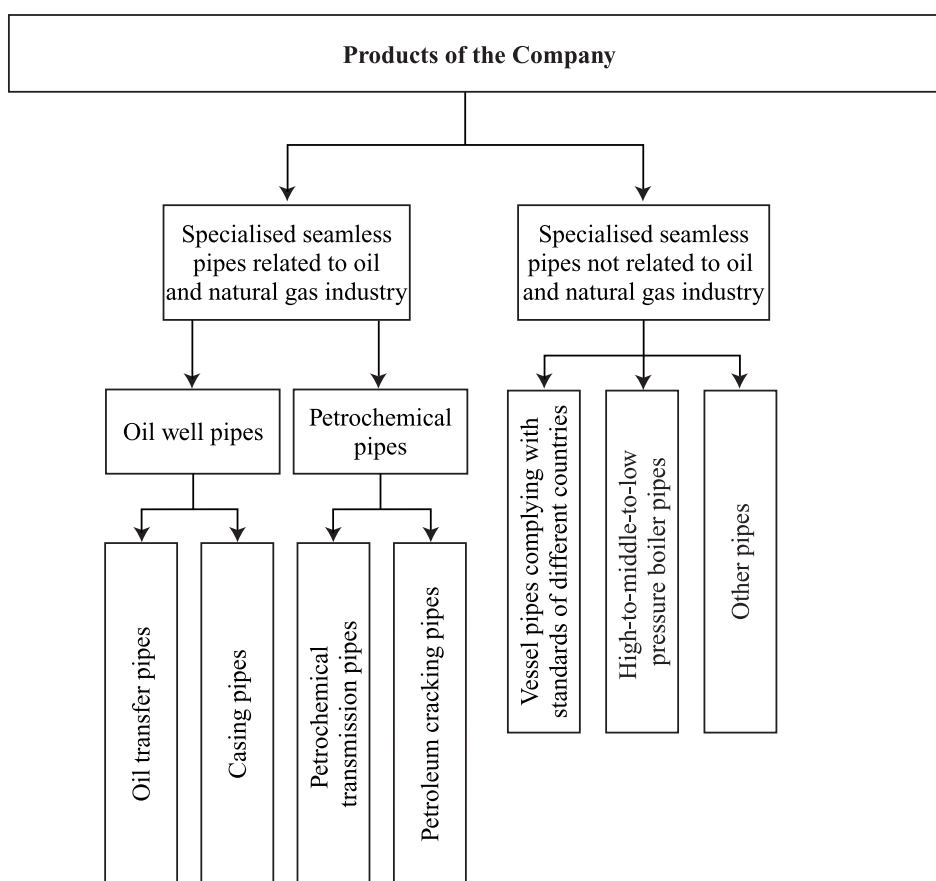
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### PRODUCTS

The Company classifies its products into two main categories: (i) specialized seamless pipes for the oil and natural gas industry, including oil well pipes (mainly oil transfer pipes and casing pipes etc.) and petrochemical pipes; (ii) other specialized seamless pipes which include vessel pipes and boiler pipes etc. The Company's business model involves: (i) selling self-produced oil well pipes and other specialized seamless pipes; and (ii) sourcing and distributing specialized seamless pipes. The Company produces oil well pipes it sells, whereas for other specialized seamless pipes, it either manufactures them or sources from third party suppliers. These products are mainly used in oil and natural gas exploration, transmission and refining enterprises, major vessel and boiler building enterprises. The following chart illustrates, in more detail, the product categories of the Company:



Pipes are used in a number of industries and the Company supplies those referred to above. The Company also provides integrated services to its customers (by sourcing specialized seamless pipes which it does not manufacture for its customers as part of an order) and it is able to deliver products capable of being directly used in the oil field by its customers once commercial production for threading and heat processing is implemented. For further details on threading and heat processing, please see the paragraph headed “Future Plans” in the section headed “Statement of Business Objectives” of this prospectus.

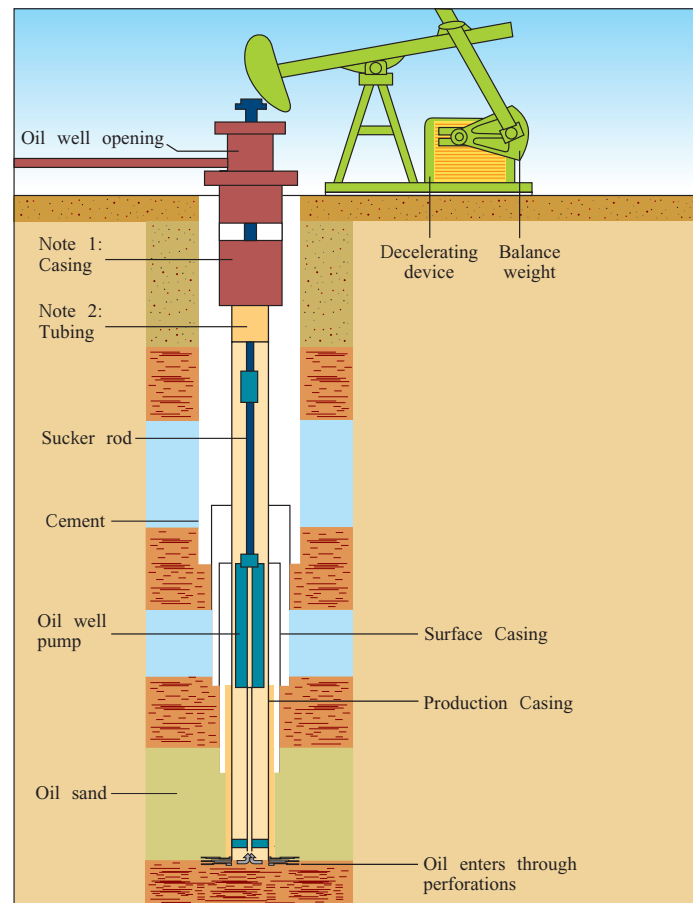
### *Specialized seamless pipes for the oil and gas industry*

The oil well pipes produced and sold by the Company are mainly oil transfer pipes with diameters from 48.3 mm to 114.3 mm and casing pipes with diameters from 114.3 mm to 219 mm.

Casing pipes, oil transfer pipes, drilling pipes, square drilling pipes and drill collars are collectively known as oil well pipes.

- Casing pipes are steel tubes that are used to support the walls of oil and gas wells. They are mainly classified as: (i) surface casing pipes; (ii) technical casing pipes; and (iii) production casing pipes.
- Oil transfer pipes are specialized seamless pipes installed in the production casing pipes that allow the oil and gas to flow to the surface after the formation of oil and gas wells.

The structure of oil well facilities is as follows:



*Notes:*

- (1) Casing is the casing pipes which are one of the principal products of the Company.
- (2) Tubing is the oil transfer pipes which are one of the principal products of the Company.

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Petrochemical pipes are the specialized seamless pipes for the transmission of petroleum and natural gas and for applications in the oil refinery industry.

In February 2006, the API certified that the Company was qualified to use API monogram for API Spec 5CT on oil transfer pipes and casing pipes specification and API Spec 5L on pipes for transmission. These API standards are industry standards set by the American Petroleum Institute to promote the use of safe, interchangeable equipment and operations through the use of proven, sound engineering practices.

*Specialized seamless pipes for vessels, boilers and others*

Vessel pipes are pressure resistant pipes which are used in various types of ship building works. Boiler pipes refer to the specialized seamless pipes for boilers, which are mainly categorized into: (i) specialized seamless pipes for low-to-medium pressure boilers; and (ii) specialized seamless pipes for high pressure boilers. Since 1993 when the Company commenced production of specialized seamless pipes, it has continued to develop new products so as to meet market demand in this sector. The Company's vessel pipes have been certified for use in seven countries and it has also successfully developed pipes for low, medium and high pressure boilers. The Company is also planning to develop vessel pipe products for Japan, a leading ship building country in the world. It is expected that accreditation by the Japanese shipping classification society will be awarded in the second half of 2006.

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The following table sets out the percentages of the Company's total revenue by product types for the two years ended 31 December 2005 and the six months ended 30 June 2005 (unaudited) and 30 June 2006.

	Year ended 31 December					
	2004			2005		
	<i>Tonnes</i>	<i>RMB '000</i>	<i>% of sales</i>	<i>Tonnes</i>	<i>RMB '000</i>	<i>% of sales</i>
<u>Self-produced</u>						
Oil well pipes	255.5	2,255	0.7%	94,063.1	469,529	51.8%
Petrochemical pipes	5,594.7	37,671	11.3%	6,642.7	44,868	4.9%
Other specialized seamless pipes	17,266.1	110,913	33.2%	27,804.6	161,120	17.8%
<b>Sub-total</b>	<u>23,116.3</u>	<u>150,839</u>	<u>45.2%</u>	<u>128,510.4</u>	<u>675,517</u>	<u>74.5%</u>
<u>Sourcing and distribution</u>						
Oil well pipes	607.6	3,240	1.0%	–	–	–
Petrochemical pipes	5,297.5	31,726	9.5%	5,334.1	33,020	3.6%
Other specialized seamless pipes	24,765.7	147,840	44.3%	31,315.3	198,053	21.9%
<b>Sub-total</b>	<u>30,670.8</u>	<u>182,806</u>	<u>54.8%</u>	<u>36,649.4</u>	<u>231,073</u>	<u>25.5%</u>
<b>Total</b>	<u><u>53,787.1</u></u>	<u><u>333,645</u></u>	<u><u>100%</u></u>	<u><u>165,159.8</u></u>	<u><u>906,590</u></u>	<u><u>100%</u></u>
	<b>Six months ended 30 June</b>					
	<b>2005</b>			<b>2006</b>		
	<i>Tonnes</i>	<i>RMB '000</i> <i>(unaudited)</i>	<i>% of sales</i>	<i>Tonnes</i>	<i>RMB '000</i>	<i>% of sales</i>
<u>Self-produced</u>						
Oil well pipes	37,417.4	177,004	45.3%	67,878.4	338,386	56.8%
Petrochemical pipes	3,209.8	20,631	5.3%	4,041.9	25,255	4.2%
Other specialized seamless pipes	14,022.6	81,207	20.8%	17,936.3	99,637	16.7%
<b>Sub-total</b>	<u>54,649.8</u>	<u>278,842</u>	<u>71.4%</u>	<u>89,856.6</u>	<u>463,278</u>	<u>77.7%</u>
<u>Sourcing and distribution</u>						
Oil well pipes	–	–	–	–	–	–
Petrochemical pipes	3,103.8	19,833	5.1%	2,709.4	16,286	2.7%
Other specialized seamless pipes	16,181.7	91,928	23.5%	21,810.4	116,565	19.6%
<b>Sub-total</b>	<u>19,285.5</u>	<u>111,761</u>	<u>28.6%</u>	<u>24,519.8</u>	<u>132,851</u>	<u>22.3%</u>
<b>Total</b>	<u><u>73,935.3</u></u>	<u><u>390,603</u></u>	<u><u>100%</u></u>	<u><u>114,376.4</u></u>	<u><u>596,129</u></u>	<u><u>100%</u></u>

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### PROCUREMENT

The Company's procurement department is responsible primarily for sourcing raw materials for self-produced and sourcing and distribution of specialized seamless pipes for trading purposes. The specialized seamless pipe industry has a highly diversified product range. The Company's self-produced products may not cover all of its customers' needs, but in order to provide quality service, the Company will purchase those pipes which are not produced by it from the market. The Company's purchase orders normally contain a list of pipes which their customers need. This one-stop shop service requires in-depth product knowledge of specialized seamless pipes and insights into the market which can only be gathered through time. The Company's inventory policy for both self produced pipes and merchandise pipes for sourcing and distribution are discussed in the paragraph headed "Inventory Control" below.

#### *Sourcing of raw materials for self-production*

The Company only purchases raw materials, mainly steel billets, for production needs, with the remaining being a small amount of plastic packaging materials. In general, the Company purchases raw materials on a monthly basis based on its customers' orders for the month, thereby deploying a JIT policy for its inventory. The Company has relatively long-standing relationships with its major suppliers for between 4 to 10 years and has not experienced any significant difficulties in sourcing raw materials and components since the supply of these goods to the Company. The Directors consider that the raw materials and components required by the Company can be sourced locally without difficulties. The Company does not hedge against increases in raw materials but when considered appropriate, it makes strategic purchases of steel billets at times when it believes the price is low.

Any decisions relating to the levels of inventory and the related procurement of raw materials is premised on the Company's assessment of market conditions for such raw materials. This is monitored by the Company's procurement team and the procurement manager submits an application for the general manager's review if he considers appropriate. After obtaining the general manager's approval, the application will be subject to further vetting by the managers' office which is responsible for conducting a final market analysis before confirmation is given that the raw material purchase may be proceeded with. For inventory applications which represent over 1.5 times of the normal stock level, the chairman of the Company must also be consulted.

#### *Purchase of specialized seamless pipes for the sourcing and distribution business*

To complement its product offering to customers, the Company also sources and distributes specialized seamless pipes in finished goods form in the market. For its sourcing and distribution procurement, the Company anticipates demand for particular specialized seamless pipes and, depending on market conditions at the time would make purchases in order to build up inventory. The prices at which such specialized seamless pipes are purchased are dictated by market conditions at that time.

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In accordance with the requirements of its customers, the sales manager related the types and specifications of productions not produced by the Company in the customer's order, together with the volume and delivery period in writing to the purchasing department. The purchasing department will categorize whether the products pending purchase are of usual specifications. For those specialized seamless pipes which are not produced by the Company and not of usual specifications, application of purchase has to be submitted to the general manager for approval prior to confirming orders with the sales department. For specialized seamless pipes not produced by the Company but of usual specification, the Company will keep stock in an appropriate volume for satisfying the urgent requirement of its customers. The purchasing department will submit their purchasing application to the general manager for review and then forward to the general manager's office for study before deciding on whether to purchase in bulk or not. The chairman of the Company must be consulted in connection with bulk purchase applications.

### *Suppliers*

When selecting its suppliers, the Company strictly conducts its selection in accordance with its purchasing control procedures. Prior to becoming an approved supplier of the Company, potential suppliers would be assessed by the Company's procurement team based on the following criteria:

- supplier's production capacity and quality control;
- whether the raw materials manufactured by the supplier meet the national and the Company's standard;
- whether the supplier has previously been involved in significant poor product quality issues and whether the product functions stably. The supplier must also be equipped with the ability to undertake contingencies;
- the supplier is equipped with its own research capabilities and has a clear vision for development in the industry; and
- the Company's other major criteria include price, delivery time, service quality, integrity and reputation in the relevant industry.

To ensure the quality of the approved suppliers, the Company will conduct the following control procedures:

- review or monitor the production process of the supplier;
- collect information regarding the supplier on its product development, production facility, management team and any other major developments in the industry;
- maintain control on the level of inventory and accounts payable through financial management; and

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- regularly conduct quality assessment on the supplier's raw materials to ensure that the raw materials meet the Company's standard.

The major raw materials required by the Company are sourced locally and are denominated and settled in RMB. Terms of payment for the raw materials are made on a cash (or cash equivalent) on delivery basis. They are usually settled by bank bills or telegraphic transfers. During the two years ended 31 December 2005 and the six months ended 30 June 2006, the largest five suppliers of the Company accounted for approximately 52.6%, 50.3% and 62.0% respectively of the Company's total purchases. Over the same period, the Company's largest supplier accounted for approximately 14.8%, 26.4% and 30.4% of the Company's total purchases respectively for the same periods. None of the Directors, their respective associates or, so far as the Directors are aware, Shareholders who will be interested in more than 5% of the issued share capital of the Company immediately following completion of the International Placing (but taking no account of any Over-allotment Shares) had any interest in any of the five largest suppliers of the Company during the two years ended 31 December 2005 and the six months ended 30 June 2006. Anhui Plastic Company, a subsidiary of Tianda Holding, has been supplying a kind of raw material, namely, plastic for packaging, to the Company. Please refer to the paragraph headed "Framework Agreement for the Supply of pipe protection casing and packaging materials with Tianda Plastic Company" under the section headed "Relationships with the Controlling Shareholder and Connected Transactions" in this prospectus for further details. The Company's five largest suppliers in the Track Record Period do not include Tianda Plastic Company and are Independent Third Parties.

### INVENTORY CONTROL

As at 30 June 2006, the Company had inventories of approximately RMB198.8 million, comprising raw materials, work-in-progress and finished goods. For the two years ended 31 December 2005 and the six months ended 30 June 2006, the inventory turnover days of the Company were approximately 34 days, 38 days and 61 days respectively. The Directors consider that the normal level of inventories is around 35-40 days which is necessary in order to maintain a smooth production and to ensure timely delivery to customers. However, the Company sometimes strategically bulk purchases a substantial amount of raw materials in anticipation of price increase of raw materials. Leaving aside strategic purchases of raw materials, the Company aims to keep no more than 10 production days of raw materials.

The Company adopts inventory control that allow it to closely monitor the level of inventories of each of the raw materials, work-in-progress and finished goods. The Company adopts a networked inventory control software which records all input and output of inventory from any of the warehouses. In addition, the Company will, based on its estimation, keep about 10 business days of finished goods as inventory although it may, in anticipation of any price increase for a particular product, increase its inventory of finished goods at any one time. Purchases are primarily made after a sales order is confirmed. Once a sales order is received, the engineering department and production department of the Company will determine the nature and quantity of materials necessary for that particular order. After producing and testing the finished products, they will be delivered to the customers of the Company. The Company will review any damaged, slow moving and obsolete inventory on a quarterly basis. The stock provision is made for the differences

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between the costs and the net realizable values of the inventories. The stock provision is assessed on an individual basis. When obsolete items are identified by the Company, they will be written-down to net realizable value and all losses of inventories are recognized as expenses in the period in which such write-downs or losses occur. Inventory would be regarded as obsolete when they are considered not saleable or no longer suitable for production. For each of the two years ended 31 December 2005 and the six months ended 30 June 2006, provision for obsolete inventory amounting to RMBNil, RMB1.8 million and RMB1.8 million respectively.

### **QUALITY CONTROL**

The Company is committed to manufacturing high quality products. The Directors believe that product quality is vital in enhancing the Company's competitiveness, market position and reputation. As at 30 June 2006, the Company employed 62 quality control staff with an average working experience of five years and the majority of whom possess tertiary or college qualification. Staff training for the quality control teams include training in the various product specifications, industry standards, inspection methods, quality assurance and management programmes.

The quality control of the Company's products is divided into three phases:

#### **Purchase control**

The Company has implemented a set of procedures for selecting its major suppliers and only places orders with those qualified suppliers. In addition, all the raw materials are subject to inspections and examinations in accordance with relevant quality standards before acceptance.

#### **Production control**

The production process involves different procedures. The Company carries out its quality control in accordance with ISO9001, API Specifications and the relevant countries' vessel manufacturing standards in accordance with the relevant type of specialized seamless pipe standard. All production procedures are documented and are guided by the instruction manual with appropriate personnel and advanced equipments.

The Company utilises technological advanced quality control machineries such as ultrasonic test machines, hydrostatic pressure test machines, hydraulic universal test machines and various other testing equipment to ensure its specialized seamless pipes are all of the highest quality.

#### **Product control**

All final products will be tested in accordance with the technical standards and only qualified products will be accepted. Furthermore, the Company regularly invites customers to come to the factory and check the quality of the products before delivery. During the Track Record Period, there were no return of goods by the Company's customers.



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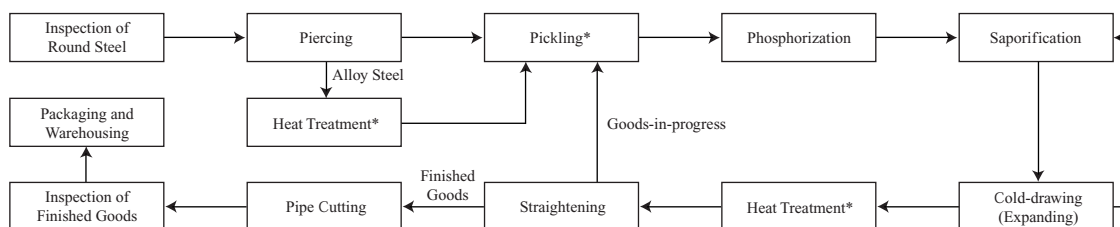
## BUSINESS

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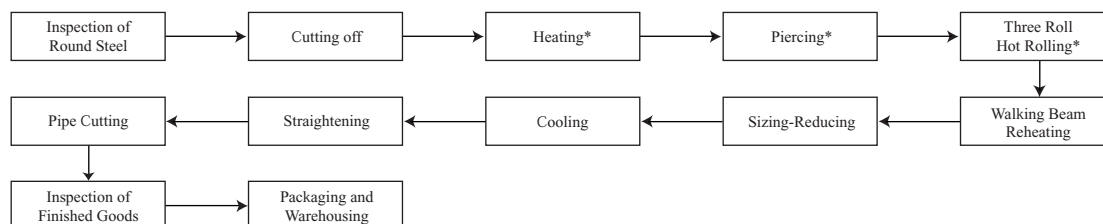
### PRODUCTION PROCESS AND FACILITIES

The Company has established two production bases in Tianchang and Chuzhou, both in Anhui Province. The Company uses two different technologies to shape its specialized seamless pipes, being Cold-drawn Steel Pipe technology which is used in Tianchang, and Hot-rolled Steel Pipe Technology which is used in Chuzhou. Cold-drawn Steel Pipe Technology is a special technology for the production of a large variety of high precision specialized seamless pipes with small diameters like oil transfer pipes, petrochemical pipes and other specialized pipes in the oil well pipes category. Hot-rolled Steel Pipe Technology is a specialized technology for high efficiency mass production of specialized seamless pipe with larger diameters like casing pipes in the oil well pipes category. The following diagrams illustrate their respective production process:

#### The workflow of Cold-drawn Steel Pipe Technology (\* means Quality Control Point)



#### The workflow of Hot-rolled Steel Pipe Technology (\* means Quality Control Point)



#### Production and technology upgrades

Through technology upgrades, the Company has increased the standard and upgraded the value of its products. The Company has commenced (but has not yet completed) its technology upgrade projects for heat processing of 100,000 tonnes of oil casing pipes and threading finish for oil casing pipes for up to 100,000 tonnes per annum from 2006. The trial production phase is expected to commence at the end of this year, gradually transitioning to commercial production in the early first half of 2007. Once in commercial production, the oil well pipes can, after threading, be used directly in the oil fields without further processing, thereby improving the Company's product. Oil well pipes which have been subject to heat processing can be used in harsher geological conditions, thereby expanding the Company's product offering.

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### Production facilities and sourcing and production packaging/logistics

The Company's production bases in Tianchang and Chuzhou are approximately 125 km apart. The gross floor area of the plant in Tianchang is approximately 52,000 sq.m and it houses three sets of cold drawing production lines for specialized seamless pipes, including energy saving tilted heater and two-roll tilted hole puncher. The gross floor area of the plant in Chuzhou is approximately 43,840 sq.m. and houses three hot-rolled machines sets, including automatic circular heater, conical hole puncher, ASSEL three rolled pipe machine, incremental heater, micro tension diameter fixing machine and a series of sophisticated one-stop inspection equipment. There is also a warehouse of approximately 31,522 sq.m. in Chuzhou from which the Company has set up its distribution and logistics centre.



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The total production capacity of the Company for 2006 is 300,000 tonnes and 200,000 tonnes and 25,000 tonnes for 2005 and 2004 respectively. As a general indication only, such production capacity can be translated into:

Period	Oil well pipes (tonnes)	Other specialized seamless pipes including petrochemical pipes (tonnes)	Total production capacity (tonnes)
2004	5,000	20,000	25,000
2005	150,000	50,000	200,000
2006	250,000	50,000	300,000

The production utilisation rates during the Track Record Period for each of the production facilities in Tianchang and Chuzhou were as follows:

	Year ended 31 December						Six months ended 30 June 2006 (half year statistics)		
	2004			2005			Production Capacity (tonnes)	Actual Production (tonnes)	Utilisation Rate
	Production Capacity (tonnes)	Actual Production (tonnes)	Utilisation Rate	Production Capacity (tonnes)	Actual Production (tonnes)	Utilisation Rate			
Tianchang Facility	25,000	25,300	>100%	50,000	27,700	55.40%	50,000	25,600	51.20%
Chuzhou Facility	-	-	-	150,000	107,300	71.53%	100,000	66,700	66.70%

*Note:* The production capacities for the six months ended 30 June 2006 is calculated by reference to the annual production capacity divided by two. In 2006 the annual production capacity of the Tianchang Facility increased to 100,000 tonnes as a result of the installation of a new oil well pipe production line. For the Chuzhou Facility, the production capacity increased to 200,000 tonnes as a result of technological upgrade of the production equipment.

The Company's production facilities can be modified to manufacture different types of specialized seamless pipes with minimal costs.

### ENVIRONMENTAL PROTECTION

The Company complies with the national, provincial and local environmental laws and regulations, including the Environmental Protection Law of the PRC and laws regarding the evaluation on the impact to the environment, including the Environmental Protection Law of the People's Republic of China as promulgated and implemented by the Standing Committee of the Seventh National People's Congress on 26 December 1989, the Law on Environmental Impact Assessment of the People's Republic of China as promulgated by the Standing Committee of the Ninth National People's Congress on 28 October 2002 and implemented on 1 September 2003 and the Regulation on Environmental Management for Construction Projects promulgated and implemented by the State Council on 29 November 1998. The Company has passed the environmental test conducted by the Anhui Environmental Protection Bureau in May 2006. The Company has not committed any breaches and has not been penalized for any violation of PRC environmental protection laws

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since its date of incorporation. The Company has obtained all the necessary permits and licences as required under the applicable PRC environmental protection laws for it to conduct its current business.

In order to enhance environment management, the Company formed an environment protection unit, which established a system of working standards, rewards and penalties for environment protection. Pursuant to PRC law, the Company implemented environmental impact assessment system in new projects as well as modification and expansion projects. For example, the environmental protection and treatment facilities in each project should be designed, constructed and commenced with the core structure at the same time. The industrial solid waste generated by the Company were all safely disposed of and deployed for various purposes. The cooling water used in the production processes of the Company is recycled after treatment without discharging any pollutants.

With the increase in awareness of civic duties and environment protection, as well as ongoing improvement in environment protection standard required by the PRC government, the Company will use clean energy such as natural gas as much as practicable and arrange relevant staff to learn and promote environmental laws and regulations. The Company will follow up with the PRC legal requirements and devote more efforts and resources to environment protection, so as to fulfill the need of the government and the society.

The Company conducted certain research and development activities to adopt new technologies for reducing impact on the environment:

- (i) Dust removing devices were installed at all boiler equipment so as to reduce the pollution to the atmosphere;
- (ii) Water recycling technologies were applied to construction facilities so as to reduce the pollution to water resources;
- (iii) The technical staff under the environment protection unit of the Company's research and development department continued to implement new technologies and application of new technologies.

The design, repair and maintenance of the Company's existing facilities were featured with environmental protection elements, such as recycling water facilities for existing equipment and gradually deployment of clean energy such as natural gas.

The Company invested an aggregate of approximately RMB6.8 million during the Track Record Period in controlling its environmental pollution and treatment with related depreciation charges of about RMB0.6 million per annum. The Company's investment in controlling its environmental pollution and treatment for the two years ended 31 December 2005 and the six months ended 30 June 2006 was approximately RMB6,632,000, RMB168,000 and RMBnil respectively. The Company's investment in environmental protection continues to increase and approximately RMB2,600,000 is expected to be spent for the full year ending 31 December 2006. For the two years ended 31 December 2005, the contamination disposal fee paid by the Company is approximately RMB18,000 and RMB22,000 respectively. According to the "Administration Provisions on the Collection and

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Use of the Contamination Disposal Fee” issued by the State Council, the environmental protection authority in the PRC, after taking into consideration the type of pollutant emission and the amount thereto, determines the appropriate contamination disposal fee.

The Company intends to expand its production facilities through technology upgrades for the threading production line of 100,000 tonnes per annum and for the heat processing of oil transfer pipes of 100,000 tonnes per annum. The environmental impact assessment documents for the above two projects have been approved by Chuzhou Environmental Protection Bureau. After the completion of the above two projects, the Company shall apply to the environmental protection competent authorities for the inspection and acceptance of the environmental protection standard of the projects completed. These projects shall only officially commence production or operation after inspection and acceptance by the environmental protection competent authorities.

### SALES AND MARKETING

#### Sales

The Company had a sales force of 19, 22 and 29 as at 31 December 2004, 31 December 2005 and 30 June 2006 respectively. The Company deploys a direct sales strategy to develop its customer base. The sales team’s main responsibility is to closely monitor market development, provide after-sales services and other advertising work. The sales team is divided into three groups based on their geographical locations, with a regional sales manager responsible for that region’s sales team, sales and marketing activities and after-sales services. Three teams cover the following regions in China:

Southwestern and Northwestern China areas	Chongqing, Sichuan, Yunnan, Guizhou, Xizang, Xinjiang, Gansu, Qinghai, Shaanxi, Ningxia
Northern, Central and Southern China areas	Beijing, Tianjin, Hebei, Inner Mongolia, Shanxi, Hubei, Hunan, Henan, Guangdong, Guangxi, Hainan
Eastern and Northeastern China areas	Shanghai, Shandong, Anhui, Zhejiang, Fujian, Jiangsu, Jiangxi, Heilongjiang, Jilin, Liaoning

Such regional sales manager reports to the general sales manager of the Company who is also responsible for the Company’s overall sales and marketing strategy. Of these, the sales force is primarily incentivized by commissions and their performance by reference to pre-set annual sales targets. As at 30 June 2006, the sales force responsible for domestic sales in China comprised 24 people and the remaining five people were primarily responsible for exports. For each of the two years ended 31 December 2005 and the six months ended 30 June 2006, the export sales accounted for approximately less than 1%, 2.7% and 3.4% of the Company’s total sales respectively. The Company is capable of producing specialized seamless pipes for the oil and natural gas industry, including oil well pipes (mainly oil transfer pipes and casing pipes etc.) and petrochemical pipes, and enjoys a good reputation in the oil well pipes industry in the PRC.

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### Top five customers of the Company for the six months ended 30 June 2006

	Sales amount <i>RMB'000</i>	% of sales	Product sold	Business scope	Location of oil field
1) Shengli Oilfield Highland Petroleum Equipment Co., Ltd. 勝利油田高原石油裝備有限責任公司	57,649	9.7%	Oil well pipe	Manufactures and operates in oil equipment products	Shandong, Xinjiang, Shaanxi, Harbin
2) Tianjin Tiangang Special Petroleum Pipe Manufacture Co., Ltd. 天津天鋼石油專用管製造有限公司	39,295	6.6%	Oil well pipe	Manufactures oil transfer pipes, casing pipes and connectors of casing pipes	Harbin, Henan
3) Tianjin Tubular Goods Machining Co., Ltd. 天津市石油管材加工有限公司	32,584	5.5%	Oil well pipe	Manufactures casing pipes, oil transfer pipes and pipe joints	Harbin, Xinjiang and Shaanxi
4) Dagang Oilfield Group New Century Machinery Manufacturing Co., Ltd. 大港油田集團新世紀機械製造有限公司	27,142	4.6%	Oil well pipe	Manufactures oil exploration equipment	Tianjing and Shaanxi
5) Dalipal Pipe Company Ltd. 達力普石油專用管有限公司	16,607	2.8%	Oil well pipe	Manufactures casing pipes and oil transfer pipes	Harbin, Cangzhou, Xinjiang, Shaanxi
Total	<u>173,277</u>	<u>29.2%</u>			

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### Top five customers of the Company for the six months ended 30 June 2005

	Sales amount <i>RMB'000</i>	% of sales	Product sold	Business scope	Location of oil field
1) Wuxi Seamless Oil Pipes Co., Ltd. 無錫西姆萊斯石油專用管 製造有限公司	78,864	20.2%	Oil well pipe	Manufactures casing pipes and oil transfer pipes	Harbin, Tianjing, Cangzhou, Xinjiang and Shaanxi
2) Cangzhou OCTG Co., Ltd. of Huabei Oilfield 滄州華北石油專用管材有限公司	22,929	5.9%	Oil well pipe	Manufactures various types of casing pipes	Harbin, Cangzhou, Xinjiang and Shaanxi
3) Lusheng Shihua Trading (Beijing) Co., Ltd. 魯勝實華貿易(北京)有限公司	17,415	4.5%	Oil well pipe	Operates in oil well pipes	Shandong
4) Tianjin Tubular Goods Machining Co., Ltd. 天津市石油管材加工有限公司	11,993	3.1%	Oil well pipe	Manufactures casing pipes, oil transfer pipes and pipe joints	Harbin, Xinjiang and Shaanxi
5) Shanghai Kangzong Enterprise Development Co., Ltd. 上海康宗企業發展有限公司	5,824	1.5%	Oil well pipe	Operates in oil well pipes	Yanchang oil field in Yanan, Shaanxi
Total	<u>137,025</u>	<u>35.2%</u>			

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### Top five customers of the Company for the year ended 31 December 2005

	Sales amount <i>RMB'000</i> <i>(unaudited)</i>	% of sales	Product sold	Business scope	Location of oil field
1) Wuxi Seamless Oil Pipes Co., Ltd. 無錫西姆萊斯石油專用管製造有限公司	112,970	12.5%	Oil well pipe	Manufactures casing pipes and oil transfer pipes	Harbin, Tianjing, Cangzhou, Xinjiang and Shaanxi
2) Shengli Oilfield Highland Petroleum Equipment Co., Ltd. 勝利油田高原石油裝備有限責任公司	35,359	3.9%	Oil well pipe	Manufactures and operates in oil exploration equipment	Shandong, Xinjiang, Shaanxi and Harbin
3) Cangzhou OCTG Co., Ltd. of Huabei Oilfield 滄州華北石油專用管材有限公司	34,926	3.9%	Oil well pipe	Manufactures various types of casing pipes	Harbin, Cangzhou, Xinjiang and Shaanxi
4) Shanghai Naili Shiye Co., Ltd 上海耐利實業有限公司	25,569	2.8%	Oil well pipe	Operates in oil well pipes	Harbin, Cangzhou, Xinjiang and Shaanxi
5) Tianjin Baosteel Industry and Trade Co., Ltd. 天津寶鋼工貿有限公司	22,324	2.5%	Oil well pipe	Operates in oil well pipes	Harbin and Henan
<b>Total</b>	<b><u>231,148</u></b>	<b><u>25.6%</u></b>			



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### Top five customers of the Company for the year ended 31 December 2004

	Sales amount <i>RMB'000</i>	% of sales	Product sold	Business scope
1) NanJing JinLing Shipyard 南京市金陵船廠	7,241	2.2%	Other specialized seamless pipes	Vessel construction
2) Hubei Changjiang Petrochemical Equipment Co., Ltd. 湖北省長江石化設備有限公司	6,552	2.0%	Petrochemical pipe	Manufactures oil refining machinery and relevant accessories
3) Jiangsu Hengsheng Chemical Fertilizer Co., Ltd. 江蘇省新沂市恒盛化肥有限公司	5,535	1.7%	Petrochemical pipe	Manufactures chemical raw materials
4) China National Shipbuilding Equipment & Materials Corporation 中國船舶工業物資總公司	4,963	1.5%	Other specialized seamless pipes	Operates in materials for vessel construction and relevant industry
5) Jiangsu Taixing Ningxing Machinery Co., Ltd. 江蘇省泰興寧興機械有限公司	4,866	1.5%	Petrochemical pipe	Operates in pressure containers
Total	<u>29,157</u>	<u>8.9%</u>		

For each of the two years ended 31 December 2005 and the six months ended 30 June 2005 (unaudited) and 2006, the five largest customers of the Company accounted for approximately 8.9%, 25.6%, 35.2% and 29.2% respectively of the Company's total sales. For the two years ended 31 December 2005 and the six months ended 30 June 2005 (unaudited) and 2006, sales to the largest customer of the Company accounted for approximately 2.2%, 12.5%, 20.2% and 9.7% respectively of the Company's total sales.

For the two years ended 31 December 2005 and the six months ended 30 June 2006, the Company had active customers\* of approximately 2,000, 1,400, 1,000 respectively. For the respective periods in the two years ended 31 December 2005 and the six months ended 30 June 2006, about 440, 410, and 280 active customers were oil fields or their designated processing factories and about 80, 70 and 40 active customers were ship-builders.

The Company's sales were settled in Renminbi for transactions completed in the PRC while sales generated from export were settled in US dollars. For the two years ended 31 December 2005 and the six months ended 30 June 2006, 99.3%, 97.3% and 96.6% of the Company's sales was settled in Renminbi while 0.7%, 2.7% and 3.4% was settled in US dollars.

Regardless of whether the products are self produced or purchased as part of its sourcing and distribution business, the Company remains liable for any product liability claims. The agreements between the Company and customers include product warranties of

\* active customers are those which had made at least one purchase from the Company during the relevant period.

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six or 12 months after product delivery. The Company has obtained product liability insurance from PICC. The Company has not received any product liability claims during the Track Record Period and has insured itself for such matters. However, there is no assurance that any and all claims in respect of product liability will be covered by such insurance.

None of the Directors, their respective associates or, so far as the Directors are aware, Shareholders who will be interested in more than 5% of the issued share capital of the Company immediately following completion of the International Placing (but taking no account of any Over-allotment Shares) had any interest in any of the five largest customers of the Company during the two years ended 31 December 2005 and the six months ended 30 June 2006. The Company's five largest suppliers in the Track Record Period were Independent Third Parties.

### Marketing and branding

The Company aims to:

- *Establish a sales and marketing team with innovative sales and marketing business models to strengthen sales and marketing services*

The Company's sales and marketing team has been expanding over the years. As at 31 December 2004, the sales and marketing team comprised 19 staff and as at 30 June 2006, this increased to 29 staff. The Company has devoted efforts to the training of staff, improving the sales and marketing standard of its staff and its corporate image in major oil field markets. The Company has also adopted a direct sales model to reduce intermediaries, so as to provide pre-sales, sales and after-sales services to the fullest extent. As part of the brand promotion scheme, the Company embosses its corporate logo on the products they manufacture and sell.

- *Promotion through various channels of communication*

The Company places emphasis on the circulation of promotional materials within the industry's network and has, since 1993, been collecting market data. The Company has advertised extensively in approximately 50 publications of the industry, such as China Petrochemical (《中國石油化工》), Steel Pipes (《鋼管》) and China Special Equipment Safety (《中國特種設備安全》). At the same time, the Company has also leveraged on the advantages of the internet and maintained its own domain name and created its own website at <http://www.td-gg.com>. It is also a member of certain professional websites in the industry, namely Alibaba and My Steel Network (我的鋼鐵網絡).

- *Participation in trade exhibitions to increase promotional efforts and raise its profile*

The Company's marketing efforts include participation in various international and national professional pipe materials exhibitions. The Company participated in the Second Shanghai International Steel Pipes Trade Exhibition held at Shanghai Expo Exhibition Centre in May 2006. During the exhibition, the Company entered into

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product contracts with certain customers from within and outside the PRC and achieved good results. The Company participated in the Second All-China International Tube & Pipe Industry Trade Fair 2006 held at Shanghai Expo Exhibition Centre in September 2006. Through the participation in these trade exhibitions, the Company has further understood the requirements of and obtained feedback from its customers. Such requirements and feedback also provide the Company with useful information for improving its products, enabling it to better monitor and work towards meeting expectations of its current and potential customers. Such trade exhibitions provide the Company with the opportunity of promoting its corporate image and products.

### **Pricing of products**

The Company's pricing policies depend on whether the products are self produced or purchased as part of its sourcing and distribution business.

#### *Self-produced products*

The Company usually determines the price of its products based on the following steps. The purchase department will generate the pricing trend of raw materials at the relevant time. The production department will generate information on production cost by tonne. Finance department will generate information on the relevant management and administrative expenses per tonne of product produced. The sales department will then collate these information and determine the relevant sales prices at the time. Sales prices are negotiated once a week. The pricing for such products result in an average gross margin of between 14% to 20% depending on the product specifications. Petrochemical pipes tend to command a relatively higher profit margin because it involves a more complex production requirement and are generally produced in small quantities.

#### *Sourcing and distribution*

The Company's sourcing and distribution of specialized seamless pipes is undertaken to provide a one-stop shop service to its customers. When the Company receives a purchase order from its customers, the Company will identify the specialized seamless pipes that is part of the order and which are not produced by the Company. The Company will then source from its suppliers those products and will generally price these products based on a 10% to 15% margin to their costs of sourcing those products and also depending on market conditions and market prices at the relevant time.

### **Payment terms**

Whether it is for self-produced pipes or for sourcing and distribution of pipes, for domestic sales in the PRC, sales contracts are entered into, with prepayments of certain sales amount, usually 30%. Delivery of goods shall be made when the entire sales amount is received by the Company. Settlements are made by the customers usually in telegraphic transfer or bank bills. For overseas customers, sales contracts are entered into, for which the customers issue the letter of credit pursuant to the contract. Upon receipt of the letter of credit, the Company will arrange for production. After production is completed, the Company will arrange for inspection and receipt of goods. Goods will be delivered directly

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to the customers after the inspection is completed. The Company will then submit the entire set of bills to the notifying bank, whereby the notifying bank will transfer the bills to the bank issuing the letter of credit, so that payment shall be made. As most of the products are only sent to customers on receipt of payment, the Company has not experienced any difficulties in recovering its receivables from its customers. As such there was no material provision made for doubtful debts for the two years ended 31 December 2005 and the six months ended 30 June 2006.

### RESEARCH AND DEVELOPMENT

#### Overview

The research and development efforts of the Company focus on development of new products, better production craftsmanship and techniques as well as modifying its product mix. Throughout its history, the Company has engaged research institutions to assist the Company in achieving the production of new petrochemical proprietary specialized seamless pipes such as H<sub>2</sub>S resistant specialized seamless pipes, 09CrMoAL specialized seamless pipes and screwing specialized seamless pipes for high efficiency heat exchange, of which the petrochemical specialized seamless pipe for heat exchange obtained the State Patent for Practical New Model. The success of these research projects significantly enhanced the value of steel in industrial applications. This added value include stress and corrosion resistance, increase of useful life and efficiency as well as reduction of operating and production costs through reduction of use of water resources as well as other technical operational enhancements (such as expansion of heat exchange area for better collection of energy).

The industry in which the Company operates is characterized by rapid technological development and increasing demand for high quality advanced technology products. The Directors understand successful technological development is very important for the Company to stay competitive in the market. Accordingly, the Company places strong emphasis on research and development. The Company intends to further develop its oil well pipe products in the following direction. In 2007, the Company intends to continue the development of high grade steel oil well pipes that are designed to be strong, high pressure resistant and corrosion resistant. At the same time, it will also conduct research and development in the oil well pipe products and thickened oil transfer pipe products with circular thread and ladder thread according to the API standard.

In relation to other specialized seamless pipes, as for the near future, apart from continuing to comply with other international production standards, the Company will develop specialized vessel pipes in compliance with the Japanese standards. By 2009, the Company expects to conduct research and development of high pressure boiler pipes for use at power stations according to ASTM and ASME standards.

#### Divisions and tasks

As at 30 June, 2006, the Company's research and development team consisted of 27 people who, on average, have over eight years of relevant experience. The research and development team consists of employees (including four part time employees) with expertise

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including engineering, production technology and quality assurance. Their education background include 6 employees with bachelor degrees, 20 employees with diplomas and 1 employee with a master's degree. In terms of work experience, 11 employees of the research team has 1 to 5 years of work experience, 9 employees of the research team has 6 to 10 years of work experience, 4 employees of the research team has 11 to 15 years of work experience, 2 employees of the research team has 16 to 20 years of work experience and 1 employee of the research team has 21 to 25 years of work experience. Staff training takes the form of continuous education courses, participations in exhibitions and seminars. The team is focused on two parts, namely product development and production technology research. The product development team is responsible for the development of new products emphasizing on technology level, function, quality and value adding features of products. The production technology research team is involved in the research and design of production craftsmanship. Through upgrades in the equipment and production techniques, production capabilities of the equipment and quality of its products will be further enhanced. Production costs will thereby be saved. The Company spent RMB405,000, RMB526,000 and RMB1,012,200 respectively in the two years ended December 2005 and the six months ended 30 June 2006 on research and development projects.

For a typical research and development project for new products, the sales and research and development departments will consolidate suggestions from the production technology department and sales department of the Company and formulate the proposals in the form of feasibility analysis reports. The chief engineer of the Company assesses the proposed projects and for those that he considers appropriate, they will be submitted to the general manager for approval. Once it is approved by the general manager, the chief engineer will decide on the staff to participate in the project and to monitor and trace the progress of the project. The costs for each project are allocated in a lump sum which is reviewed and examined by the chief engineer before submitting to the general manager for approval. A separate account is maintained for such costs under the control of the research and development department and monitored by the finance department. Such funds will only be used for research and development purpose.

The production technology department of the Company will propose feasibility analysis report for new techniques. The chief engineer of the Company organizes the relevant departments to assess the projects proposed. The projects that pass the assessment will be submitted to the general manager of the Company for approval. After the general manager has approved the project, the chief engineer will be responsible for the research and development of such new production techniques and decide on the staff to participate in the research and development, and to monitor and trace the progress on the research and development of such new products. Key research and development projects will be submitted to the general manager's meeting for approval. The chairman of the board of Directors will also be present in such meeting.

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### Research and development co-operation

The Directors believe that the long-term success of the Company will, to a certain extent, depend upon its ability to work with partners who will be able to provide the Company with assistance to jointly research and develop new technologies, products and markets as well as to transfer product knowledge and expertise to the Company. The following summarises the Company's major agreements or memorandum with partners:

Objective	Responsibilities	Ownership of the intellectual property rights	Date and duration of the agreement	Project investment by the Company (RMB)	Amount invested by the Company as at the Latest Practicable Date (RMB)
Jointly researched in series of oil casing pipes and two stainless steel products that are corrosion resistant, extremely hard, pressure resistant and non-conditioning with Baoshan Iron and Steel Company Limited	<p>Baosteel was responsible for preparing the technical documents and corresponding physical and chemical functional tests for metallurgy, rolling and heat processing of billets for various specialized seamless pipes.</p> <p>The Company was responsible for preparing the documents for rolling, tubing and heat processing of various types of specialized seamless pipes.</p>	<p>Rights regarding the pipes owned by the Company</p> <p>Rights regarding the billets owned by Baoshan Iron and Steel Company Limited</p>	Dated 18 March 2006 and lasts until the research in the new product is successful	6,000,000	1,600,000
Provision of technology services for casing pipes by Tubular Goods Research Center of China National Petroleum Corporation	The Tubular Goods Research Center of China National Petroleum Corporation is responsible for the provision of technology services developed for scientific functional tests and corrosion resistant steel on pipe billets and finished products as well as provision of technology services for the design, inspection and product testing of oil well pipe threading.	Owned by the Company	30 March 2006 to 30 June 2007, to be renewed upon expiry of the agreement	two related projects 5,000,000	two related projects 400,000

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Objective	Responsibilities	Ownership of the intellectual property rights	Date and duration of the agreement	Project investment by the Company (RMB)	Amount invested by the Company as at the Latest Practicable Date (RMB)
07Cr2AlMo and 09CrMoAl jointly developed by Baosteel Group Shanghai No. 5 Steel Co. Ltd. Technical Centre and Hefei General Machinery Research Institute	Baosteel Group Shanghai No. 5 Steel Co. Ltd. Technical Centre was responsible for preparing the technical documents and corresponding physical and chemical functional tests for metallurgy, rolling and heat processing of billets for various specialized seamless pipes.  The Company was responsible for preparing the documents for rolling, tubing and heat processing of various types of specialized seamless pipes.  Hefei General Machinery Research Institute was responsible for conducting the mechanics function, craftsmanship function and non-defective inspection for the Company.	Rights regarding the pipes owned by the Company  Rights regarding the billets owned by Baosteel Group Shanghai No. 5 Steel Co. Ltd.	Dated 11 October 2002 and lasted until the research in the new product is successful	400,000	400,000

As at 30 June 2006, the Company had already incurred the costs of the above projects and these were funded by the Company's internal resources. Pursuant to the relevant alliance agreements or memorandum between the Company and its research and development partners, there is no profit-sharing arrangement between the Company and its research partners. There is no separate confidentiality agreement between the parties. However, in the agreements or memorandum with its research partners, there is a confidentiality clause that the parties to the agreement or memorandum will not disclose research details and other confidential information provided to the other party for the sole use of the project to any other third party.

The Company is not privy to the investments of the other parties to the agreement or memorandum (i.e. costs to the other parties in performing their contractual obligations). The Company can only provide information on its investments as above.

### COMPLIANCE AND INSURANCE

The PRC Legal Advisers have confirmed that the requirements under applicable PRC laws and regulations relevant to the conduct of the Company's business in the PRC have been fully complied with and the Company has obtained all requisite licences, permits, certificates or approvals from the PRC government to conduct its business as set out in its business licence.



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The Company has obtained product liability insurance from PICC. It also has a comprehensive policy for some of the assets of the Company from PICC. As for its staff, it maintains staff social insurance in accordance with the legal requirements. Although the Company has a code for safety at work, it does take precautions by ensuring that such insurance policy covers the Company's employees in respect of pension insurance, medical insurance, unemployment insurance, occupational disability insurance and dormitory reserve fund. As the Company has obtained all insurance policies which are required by the relevant PRC laws, the Directors believe that insurance coverage of the Company is adequate.

### COMPETITION

An overview of the oil well pipe industry in China is set out in the "Industry Overview" section of this prospectus. Consumption of oil well pipes in China grew from approximately 1,449,000 tonnes in 2001 to approximately 2,085,000 tonnes in 2005, representing a CAGR of approximately 9.5%. Output for the same period had grown from 1,265,000 tonnes to 2,400,000 tonnes, representing a CAGR of approximately 17.4%. Since 2003, China has become a net exporter of oil well pipes.

The oil well pipes market is dominated by Tianjin Pipe (Group) Corporation (TPCO) and Bao Steel Group who, together, accounted for approximately 62.7% of total market share in China. In 2005, the Company was ranked seventh in the top 10 oil well pipe manufacturers in China in terms of output and was also one of the leading oil well pipe manufacturers.

The Company believes it is well positioned to face competition. The Company's direct sales model enables it to serve its customers better with diversified requirements, and provide better services to its customers and reduces intermediaries between the Company and its clients. The Directors expect that new entrants into this market segment would not result in significant competition for the Company. Firstly, the oil well pipes industry are capital intensive and an enormous amount of funds is required for the construction of production facilities. Secondly, professional knowledge and profound experience is required for the construction of production lines and the appropriate techniques for the production of oil well pipes in the petroleum industry. Consequently, these pose significant barriers to entry for new entrants who wish to make inroads into and establish a foothold in the oil well pipes supplied to the petroleum industry. Therefore, the Directors consider that technology, market and customer recognition being the major barriers facing the new entry manufacturers in this industry, and it is unlikely that keen competition from a competitor on a similar scale will occur in the oil well pipes market in China in the short term.

Although there are manufacturers of other oil well pipes in the PRC, the Directors consider that the Company enjoys a relatively strong competitive edge in products as compared with other manufacturers in terms of costs, quality, product type, technology level and fulfillment of customer requirements. This is based on a combination of:

- the Company's choice to use domestic and self assembled equipment which is cheaper compared to equivalent imported equipment;



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- the Company being one of the major oil well pipe manufacturers in the PRC which has been granted the Product Inspection Waiver;
- the Company obtained certificate from API and from ship classification societies of various countries;
- in addition to providing self-produced oil well pipes, the Company also provides services to assist customers to procure from the market specialized seamless pipes that are not produced by the Company. Therefore, the Company is able to provide a complete range of products to its customers in terms of specification as part of one-stop shop solutions;
- the Company conducts its own research and development as well as cooperates with research institutions in new product research and development as well as enhancement of the quality of existing products. Its technology level is evidenced by the certificates and patents it has obtained;
- the Company is one of the leading oil well pipe producers in China in 2005. Its unique shareholding structure and effective management system enables it to implement an incentive mechanism for its employees, and thus can adapt faster to market changes to the satisfaction of its customers. The Company's customer service standard is reflected in its timely delivery irrespective of order size, regular on site technical support, product quality warranty and satisfying after-sales service, etc.

The Company has advanced production technologies and equipment, and has established good cooperative relationships with leading scientific research and development institute in the PRC. Quality and technology sophistication of its products is relatively higher than before.

The Company operates primarily in the PRC market with less than 3% of its sales in 2005 being attributable to exports. The Company commenced its export to the US in 2006 and for the six months ended 30 June 2006, exports to the US accounted for approximately 0.7% of the Company's sales. As these overseas sales agents will have representatives in China to check the Company's products before they are exported and there is transportation insurance which covers the relevant deliveries, the Company will not in practice accept returns of goods if they passed inspection before export. Title of the products can pass at different times during the shipment. In some cases, title will pass to the customers when the products are placed onboard the export ship and in other cases, title will pass when the documents representing title to the products, such as bills of lading, are taken up by the purchaser. When exactly title of the products passes depends on the terms of the individual sale contracts and the trade term on which the sales is based. The Company would, however, follow up any issues with customers as part of its after-sales service. The Company did not have any products returned from these agents during the Track Record Period. As China's exports to the rest of the world increase, Chinese manufacturers' competitiveness in the global market will increase. At present, the Company does not expect to pose any significant competition in the global market.

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The Company believes that foreign companies avoid segments of the market where they believe will be costly for them. This usually means they will concentrate on much higher price segment as foreigners' costs are generally higher than those in the PRC. The market for higher quality products are usually concentrated on products for harsher drilling environments (like offshore drilling and exploration for oil and drilling at more than 4,000 metres). Whilst the Company intends to increase their product mix to include these higher grade quality products, the Company does not consider itself to be in the same competitive market segment of such foreign companies.

The Company has limited means to finance its business expansion as compared to state-owned enterprises. Currently, the Company's cash flow comprises a combination of internally generated cash from sales, bank financing and equity financing. It probably does not enjoy the same degree of access to bank financing which state-owned enterprises enjoy.

Crude oil plays a fundamental role in the industrial development of developing countries. From 2001 to 2005, total world demand for oil grew by approximately 8%. For that period, the global demand for crude oil increased from 77.7 million barrels per day in 2001 to 83.8 million barrels per day in 2005, representing a CAGR of approximately 1.9%. From 2001 to 2005, China's demand for oil grew at a much faster rate of 40.2% from 4.9 million barrels per day in 2001 to 6.9 million barrels per day in 2005, representing a CAGR of approximately 8.8%.

From the demand side, investment by various countries in the exploration for oil in the short term is expected to increase by over 10% per annum. Consumption of oil well pipes is therefore also expected to increase significantly. From the supply side, industrially developed countries, such as Europe, US and Japan did not record increases in production capabilities during these years, and only had new products developed. Additional production capabilities of oil well pipes for petroleum industry in the world mainly came from the PRC. Global additional demand mainly met by the additional production capabilities from the PRC. The oil well pipe market in China is characterized by faster demand growth than supply growth. Therefore, the Directors have confidence in the future prospects for oil well pipe producers for the petroleum industry in China.