LISTING DOCUMENT

The Stock Exchange of Hong Kong Limited takes no responsibility for the contents of this document, makes no representation as to its accuracy or completeness and expressly disclaims any liability whatsoever for any loss howsoever arising from or in reliance upon the whole or any part of the contents of this document.

CNOOC Finance (2003) Limited

(incorporated in the British Virgin Islands with limited liability)

Proposed Listing of

US$200,000,000 4.125% Guaranteed Notes due 2013

US$300,000,000 5.500% Guaranteed Notes due 2033

unconditionally and irrevocably guaranteed by

CNOOC Limited

(incorporated in Hong Kong with limited liability)

on The Stock Exchange of Hong Kong Limited

as

Selectively Marketed Securities

This Listing Document is being issued exclusively in connection with the proposed listing of US$200,000,000 4.125% Guaranteed Notes due 2013 and US$300,000,000 5.500% Guaranteed Notes due 2033 (collectively the "**Notes**") on The Stock Exchange of Hong Kong Limited as Selectively Marketed Securities under Chapter 37 of the Rules Governing the Listing of Securities (the "**Listing Rules**") on The Stock Exchange of Hong Kong Limited (the "**Stock Exchange**"). This Listing Document includes particulars given in compliance with the Listing Rules for the purpose of giving information with regard to the Issuer and the Guarantor. The respective directors of the Issuer and the Guarantor collectively and individually accept full responsibility for the accuracy of the information contained in this Listing Document and confirm, having made all reasonable enquiries, that to the best of their knowledge and belief there are no other facts the omission of which would make any statement herein misleading.

This Listing Document incorporates the offering memorandum dated 14th May, 2003 (the "**Offering Memorandum**") pursuant to which the Notes were offered and sold on a private placement basis. Capitalised terms used in the Offering Memorandum shall have the same meanings when used in this Listing Document unless the context provides otherwise.

The Notes have already been issued and placed to investors pursuant to the Offering Memorandum and are being listed on the Luxembourg Stock Exchange. This Listing Document does not constitute an offer to sell or a solicitation of an offer to buy any of the Notes. Neither the Offering Memorandum nor this Listing Document has been, nor will they be, registered with the Registrar of Companies in Hong Kong.

An application has been made to the Stock Exchange for listing of and permission to deal in the Notes as Selectively Marketed Securities under Chapter 37 of the Listing Rules and such permission to deal in the Notes is expected to become effective on 27th August, 2003. The primary listing of the Notes will continue to be on the Luxembourg Stock Exchange.

FINANCIAL INFORMATION ABOUT THE GUARANTOR

Since 31st December, 2002, the last completed financial year of the Guarantor immediately preceding the date of this Listing Document, the Guarantor has not published any interim financial statement.

INFORMATION ABOUT THE SOLE DIRECTOR OF THE ISSUER

Immediately following the listing of the Notes as Selectively Marketed Securities on the Stock Exchange, the interests and short positions of the sole director of the Issuer in the shares, underlying shares and debentures of the Issuer or any associated corporation (within the meaning of Part XV of the Securities and Futures Ordinance (Cap. 571) ("**SFO**")) which will have to be notified to the Issuer and the Stock Exchange pursuant to Divisions 7 and 8 of Part XV of the SFO (including interests and short positions which he is taken or deemed to have under such provisions of SFO) or which will be required, pursuant to section 352 of the SFO, to be entered in the register referred to therein, will be as follows:

Name of Director	**Type of Interest**	**Number of ordinary shares of US$1.00 each in the share capital of the Issuer**	**Percentage in the registered capital of the Issuer**
CNOOC Limited	Personal	1,000	100%

REMOVAL OF TRUSTEE

Pursuant to the two indentures for the Notes both dated 21st May, 2003, the Trustee may be removed at any time upon the written requests duly signed by and on behalf of the registered holders of a majority of the principal amount of the outstanding Notes, delivered to the Trustee, the Issuer and the Guarantor.

SUBSEQUENT EVENTS

There has been no material adverse change in the financial or trading position of the Issuer and/or the Guarantor since the date of the Offering Memorandum.

Neither the Issuer nor the Guarantor is involved in any litigation or arbitration proceedings relating to claims or amounts which are material in the context of the offering of the Notes and the Guarantees and, so far as the Issuer or the Guarantor are aware, no such litigation or arbitration proceedings are pending or threatened.

The date of this Listing Document is 26th August, 2003.

OFFERING MEMORANDUM

US$500,000,000

CNOOC Finance (2003) Limited

(incorporated in the British Virgin Islands with limited liability)

US$200,000,000 4.125% Guaranteed Notes due 2013
US$300,000,000 5.500% Guaranteed Notes due 2033
unconditionally and irrevocably guaranteed by

CNOOC Limited

(incorporated in Hong Kong with limited liability)

We, CNOOC Limited, through CNOOC Finance (2003) Limited, the "issuer," intend to issue US$200,000,000 principal amount of 4.125% guaranteed notes due 2013, or the "2013 notes," and US$300,000,000 principal amount of 5.500% guaranteed notes due 2033, or the "2033 notes." We refer to the 2013 notes and the 2033 notes collectively as the "notes." The obligations in respect of the notes will be unconditionally and irrevocably guaranteed by us.

The notes will bear interest from May 21, 2003 at the rate set forth above, payable semiannually in arrears on May 21 and November 21 of each year, commencing November 21, 2003. The issuer will not be able to redeem the notes prior to their maturity, except upon the occurrence of certain changes in tax laws of the British Virgin Islands, Hong Kong or the People's Republic of China requiring the payment of Additional Amounts, as described under "Description of the Notes and Guarantees." The notes will be unsecured.

An application has been made to list the notes on the Luxembourg Stock Exchange.

The notes have been rated Baa1 with positive outlook by Moody's Investors Service and "BBB" by Standard & Poor's Ratings Services.

Investing in the notes involves risks that are described in the "Risk Factors" section beginning on page 21 of this offering memorandum.

	Price to Investors(1)	Initial purchasers' discount	Proceeds, before expenses, to the issuer(1)
Per 2013 Note	98.638%	0.500%	98.138%
Total	US$197,276,000	US$1,000,000	US$196,276,000
Per 2033 Note	97.393%	0.750%	96.643%
Total	US$292,179,000	US$2,250,000	US$289,929,000

(1) Plus any accrued interest from May 21, 2003, if settlement occurs after that date.

The notes have not been, and will not be, registered under the United States Securities Act of 1933, as amended, any state securities laws of the United States or the securities laws of any other jurisdiction. Unless they are registered, the notes may be offered only in transactions that are exempt from registration under the U.S. Securities Act, any state securities laws or the securities laws of any other jurisdiction. Accordingly, the notes are only being offered to qualified institutional buyers within the United States and non-residents of the United States outside the United States. For further details about eligible offerees and resale restrictions, see "Transfer Restrictions."

It is expected that the notes will be ready for delivery in book-entry form only through The Depository Trust Company and its participants, including Euroclear and Clearstream, Luxembourg, on or about May 21, 2003, the closing date.

Joint Bookrunners

Credit Suisse First Boston **Merrill Lynch & Co.**

Joint Lead Managers

Credit Suisse First Boston **Merrill Lynch & Co.** **Goldman Sachs (Asia) L.L.C.**

Co-Managers

Cazenove Asia Limited
China Construction Bank
Industrial and Commercial Bank of China (Asia) Limited
ICEA
Daiwa Securities SMBC Hong Kong Limited
HSBC

CITIC Capital Markets Limited
BOCI Capital Limited
Barclays Capital
Nomura International
SG Asia

The date of this offering memorandum is May 14, 2003.

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Except as discussed below, we, CNOOC Limited, and the issuer, CNOOC Finance (2003) Limited, accept responsibility for the information contained in this document. To the best knowledge and belief of us and the issuer (having taken reasonable care to ensure that such is the case), the information contained in this document is in accordance with material facts and does not omit anything likely to affect materially the import of such information.

You should rely only on the information contained in this offering memorandum. We and the issuer have not, and the initial purchasers of the notes have not, authorized any other person to provide investors with different information. If anyone provides you with different or inconsistent information, you should not rely on it. We have published certain information on our website. Such information is not part of this offering memorandum and you should not rely on such information in making any investment decision with respect to the notes. We and the issuer are not, and the initial purchasers are not, making an offer to sell these securities in any jurisdiction where the offer or sale is not permitted. You should assume that the information appearing in this offering memorandum is accurate only as of the date on the front cover of this offering memorandum. Our business, financial condition, results of operations and prospects may have changed since that date.

We and the issuer are relying on an exemption from registration under the U.S. Securities Act for offers and sales of the notes. By purchasing the notes, you will be deemed to have made the acknowledgements, representations, warranties and agreements described under the heading "Transfer Restrictions" in this offering memorandum. You should understand that you will be required to bear the financial risks of your investment for the term of the notes.

This offering memorandum is based on information that we believe is reliable. Some of the information, including the Ernst & Young auditors' report on page F-2, Arthur Andersen & Co auditors' report on page F-3 and the Ryder Scott summary report in Appendix A, as well as certain tables and charts, have been provided by other parties. We only accept responsibility for correctly extracting and reproducing this information. No assurance can be given that this information is accurate or complete. This offering memorandum summarizes certain documents and other information, and you should refer to them for a more complete understanding of what is discussed in this offering memorandum. In making an investment decision, you must rely on your own examination of the issuer and us and the terms of the offering and the notes, including the merits and risks involved.

Neither we nor the issuer make any representation to any purchaser of the notes regarding the legality of an investment in the notes by such purchaser under any investment or similar laws or regulations. You should not consider any information in this offering memorandum to be legal, business or tax advice. You should consult your own attorney, business advisor and tax advisor for legal, business and tax advice regarding an investment in the notes.

Neither the United States Securities and Exchange Commission nor any state securities commission in the United States has approved or disapproved of these securities or determined if this offering memorandum is truthful or complete. Any representation to the contrary is a criminal offense.

The Luxembourg Stock Exchange takes no responsibility for the correctness of any of the statements made, or opinions expressed, in this offering memorandum. Quotation of the notes is not to be taken as an indication of the investment merits of the notes, the guarantees, the issuer or us.

Notwithstanding anything in this offering memorandum or any other document, we, the issuer, the initial purchasers, and any potential investors (and each employee, representative, or other agent thereof) (each a "participant") may disclose to any and all persons, without limitation of any kind, the United States tax treatment and any facts that may be relevant to the tax structure of the offering, provided, however, that no participant shall disclose any other information, the disclosure of which is otherwise limited, that is not relevant to understanding the United States tax treatment or tax structure of the offering (including the identity of any participant and information that could lead another to determine the identity of any participant), or any other information to the extent that such disclosure could result in a violation of any applicable securities law.

NOTICE TO NEW HAMPSHIRE RESIDENTS

Neither the fact that a registration statement or an application for a license has been filed under Chapter 421-B of the New Hampshire Revised Statutes with the state of New Hampshire nor the fact that a security is effectively registered or a person is licensed in the state of New Hampshire constitutes a finding by the Secretary of State that any document filed under Chapter 421-B is true, complete and not misleading. Neither any such fact nor the fact that an exemption or exception is available for a security or a transaction means that the Secretary of State has passed in any way upon the merits or qualifications of, or recommended or given approval to, any person, security, or transaction. It is unlawful to make, or cause to be made, to any prospective purchaser, customer, or client any representation inconsistent with the provisions of this paragraph.

In connection with the offering, Merrill Lynch, Pierce, Fenner & Smith Incorporated, or any of its affiliates, on behalf of the initial purchasers, may over-allot or effect transactions with a view to supporting the market price of the notes at a level higher than that which might otherwise prevail for a limited period. However, there may be no obligation on Merrill Lynch, Pierce, Fenner & Smith Incorporated, or any of its affiliates to do this. Such stabilizing, if commenced, may be discontinued at any time and must be brought to an end after a limited period. Any such transactions must be carried out in accordance with all applicable laws, rules and regulations.

CURRENCY OF PRESENTATION AND CERTAIN DEFINITIONS

We publish our financial statements in Renminbi and in accordance with generally accepted accounting principles in Hong Kong, or Hong Kong GAAP. All references in this offering memorandum to "U.S. dollars" and "US$" are to United States dollars; all references to "H.K. dollars" and "HK$" are to Hong Kong dollars; all references to "JPY" are to Japanese yen; all references to "Rupiah" are to Indonesian Rupiah; and all references to "Rmb" or "Renminbi" are to Renminbi, the official currency of the People's Republic of China, or the PRC. Solely for the convenience of the reader, this offering memorandum contains translations of certain H.K. dollar and Renminbi amounts into U.S. dollars. All such H.K. dollar translations have been made at the rate of HK$7.80 to US$1.00, the linked exchange rate between such currencies under policies of the Hong Kong government in effect as of the date of this offering memorandum. On May 14, 2003, the noon buying rate in The City of New York for cable transfers in H.K. dollars as certified for customs purposes by the Federal Reserve Bank of New York was HK$7.7988 to US$1.00. See "Exchange Rate Information." All Renminbi translations have been made at the rate of Rmb 8.28 to US$1.00, the noon buying rate in The City of New York for cable transfers in Renminbi as certified for customs purposes by the Federal Reserve Bank of New York on December 31, 2002. On May 14, 2003, the noon buying rate for cable transfers in Renminbi was Rmb 8.2769 to US$1.00. No representation is made that the H.K. dollar or Renminbi amounts stated herein could have been, or could be, converted into U.S. dollars at such rates or at any other rate. Totals presented in this offering memorandum may not total correctly due to rounding of numbers.

CONVENTIONS WHICH APPLY TO THIS OFFERING MEMORANDUM

Unless the context otherwise requires, references in this offering memorandum to:

- "CNOOC" are to:
  - — China National Offshore Oil Corporation, and its affiliates, excluding us and our subsidiaries.
- "CNOOC Limited," "we," "our," "us," and the "guarantor" are to:
  - — CNOOC Limited, a company incorporated with limited liability on August 20, 1999 in Hong Kong under the Companies Ordinance (Registration No. 685974) and, where the context so requires, our subsidiaries, including our wholly owned finance subsidiary that will be issuing the notes, CNOOC Finance (2003) Limited.
- "CNOOC Finance (2003) Limited" and the "issuer" are to:
  - — CNOOC Finance (2003) Limited, a company incorporated with limited liability on April 2, 2003 in the British Virgin Islands under the International Business Companies Act (Registration No. 540274) and a wholly owned subsidiary of CNOOC Limited.

References in this offering memorandum to:

- "China" or the "PRC" are to the People's Republic of China, excluding for the purpose of this offering memorandum Hong Kong, Macau and Taiwan; and
- the "Hong Kong Stock Exchange" are to The Stock Exchange of Hong Kong Limited.

This offering memorandum contains references to our "average net realized prices" for oil and gas with respect to certain periods. "Average net realized prices" for each period is derived from a numerator divided by a denominator, where:

- the numerator is equal to the sum of (i) revenues from our oil and gas sales offshore China for the applicable period; (ii) the 30% ownership share of revenues from oil and gas sales for the applicable period from our associated company, Shanghai Petroleum and Natural Gas Company Limited; and (iii) the revenues from oil and gas sales for the applicable period from our overseas interests; while
- the denominator is equal to the sum of (i) the volume of oil and gas sales offshore China for the applicable period; (ii) 30% of the volume of oil and gas sales for the applicable period from our associated company; and (iii) the volume of oil and gas sales for the applicable period from our overseas interests.

This offering memorandum contains references to "net proved reserves." "Net proved reserves" are derived from proved reserves less certain adjustments, where:

- proved reserves is equal to the sum of (i) our 100% interest in our independent oil and gas properties (excluding the proved reserves attributable to our associated company); (ii) our participating interest in the properties covered under our production sharing contracts in the PRC and Indonesia; and (iii) our 30% interest in the proved reserves of our associated company; while
- the adjustments equal the sum of (i) an adjustment for our share of royalties payable to the PRC government and our participating interest in share oil payable to the PRC government under our production sharing contracts in the PRC; (ii) an adjustment for production allocable to foreign partners under our production sharing contracts in the PRC as reimbursement for

exploration expenses attributable to our working interest and (iii) adjustments for share oil payable under our Indonesian production sharing contracts to Pertamina, the Indonesian state-owned oil and gas company, and for a domestic market obligation under which the contractor must sell a specified percentage of its crude oil to the local Indonesian market at a reduced price. In this offering memorandum, we use "share oil" to refer to the portion of production that must be allocated to the relevant government entity or company under our production sharing contracts and technical assistance contracts.

Net proved reserves do not include any deduction for production taxes payable by us, which are included in our operating expenses. Net production is calculated in the same way as net proved reserves. Unless otherwise noted, all information in this offering memorandum relating to oil and natural gas reserves is based upon estimates prepared by us. In calculating barrels-of-oil equivalent, or BOE, amounts, we have assumed that 6,000 cubic feet of natural gas equals one BOE, with the exception of natural gas from certain fields which is converted using the actual heating value of the natural gas.

For other conventions which apply to this offering memorandum, see "Certain Oil and Gas Terms."

ENFORCEMENT OF CIVIL LIABILITIES IN THE UNITED STATES

The issuer is incorporated in the British Virgin Islands, or the BVI, and we are incorporated in Hong Kong. All or substantially all of our assets and that of the issuer are located outside the United States. In addition, most of our directors and officers and those of the issuer and certain of the experts named herein are not residents of the United States, and all or a substantial portion of the assets of such persons may be located outside the United States. As a result, it may not be possible for you to effect service of process within the United States upon such persons, the issuer or us, or to enforce against any of them, judgments obtained in the United States courts. The issuer has been advised by its BVI legal advisors, Conyers Dill & Pearman, that there is no treaty between the British Virgin Islands and the United States providing for reciprocal enforcement of judgments. We have been advised by our Hong Kong counsel, Sidley Austin Brown & Wood, that there is no treaty between Hong Kong and the United States providing for reciprocal enforcement of judgments.

SPECIAL NOTE REGARDING FORWARD-LOOKING STATEMENTS

Certain statements under the captions "Summary," "Risk Factors," "Use of Proceeds," "Management's Discussion and Analysis of Financial Condition and Results of Operations," "Business" and elsewhere in this offering memorandum constitute "forward-looking statements" within the meaning of the United States Private Securities Litigation Reform Act of 1995 (the "Reform Act"). Such forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause our actual results, performance and financial condition, or industry results, to be materially different from any future results, performance or financial condition, expressed or implied by such forward-looking statements. Such factors include, among other things, oil and gas prices, the amount and nature of future exploration, development and other capital expenditures, the economic and political conditions in China and the other regions where we operate, the legal systems in China and the other jurisdictions where we operate, various business and regulatory factors affecting the petroleum industry in China and the other regions where we operate, our holding company structure, controlling shareholders, the lack of an established market for the notes and other factors referenced in this offering memorandum. See "Risk Factors."

AVAILABLE INFORMATION

For so long as the notes remain outstanding and are "restricted securities" within the meaning of Rule 144(a)(3) under the U.S. Securities Act, we will furnish, upon the request of any holder of a note or of a beneficial interest in a note, such information as is specified in paragraph (d)(4) of Rule 144A, to such holder or beneficial owner or to a prospective purchaser of such note or interest therein who is a qualified institutional buyer, in order to permit compliance by such holder or beneficial owner with Rule 144A in connection with the resale of such note or beneficial interest therein in reliance on Rule 144A unless, at the time of such request, we are subject to the reporting requirements of Section 13 or Section 15(d) of the United States Securities Exchange Act of 1934, as amended, or are exempt from reporting pursuant to Rule 12g3-2(b) under the U.S. Exchange Act.

We are currently subject to the reporting requirements of the U.S. Exchange Act and file periodic reports and other information with the U.S. Securities and Exchange Commission. As a foreign private issuer, we are not required to file periodic reports and financial statements with the U.S. Securities and Exchange Commission as frequently or as promptly as U.S. companies whose securities are registered under the U.S. Exchange Act.

For additional information available to holders of the notes, see "General Information."

SUMMARY

Because this is only a summary, it does not contain all the information that may be important to you. You should read the entire offering memorandum, including "Risk Factors," before deciding to invest in the notes. For a discussion of industry terms, including net proved reserves and net production, see "Conventions Which Apply to this Offering Memorandum" on page 5 and "Certain Oil and Gas Terms" on page 163.

The Issuer

The issuer is our wholly owned subsidiary and was incorporated with limited liability on April 2, 2003 in the British Virgin Islands under the International Business Companies Act. The issuer has no material assets and will conduct no business except in connection with the issuance of the notes and the advance of the net proceeds from the issuance of the notes to us. The registered office of the issuer is located at Romasco Place, Wickhams Cay 1, P.O. Box 3140, Road Town, Tortola, British Virgin Islands.

CNOOC Limited

We are an oil and gas company engaged in the exploration, development, production and sale of crude oil and natural gas primarily offshore China. We are the dominant producer of crude oil and natural gas offshore China and the only company permitted to conduct exploration and production activities with international oil and gas companies offshore China. As of December 31, 2002, we had estimated net proved reserves of 2,015.8 million BOE, comprised of 1,424.4 million barrels of crude oil and condensate and 3,547.9 billion cubic feet of natural gas. For the year 2002, our net production averaged 298,625 barrels per day of crude oil, condensate and natural gas liquids and 272.6 million cubic feet per day of natural gas, which together totaled 346,639 BOE per day.

Our net proved reserves increased from 668 million BOE as of December 31, 1995 to 2,015.8 million BOE as of December 31, 2002, which represents a compound annual growth rate of 17.1%. Based on net proved reserves, we are one of the largest independent oil and gas exploration and production companies in the world. In the petroleum industry, an "independent" company owns oil and gas reserves independently of other downstream assets, such as refining and marketing assets, whereas an integrated company owns downstream assets in addition to oil and gas reserves. As of December 31, 2002, approximately 60.6% of our net proved reserves were classified as net proved undeveloped. We plan to spend approximately US$2.7 billion developing our reserves offshore China and approximately US$308 million for independent exploration offshore China from 2003 through 2004.

We conduct exploration, development, production and sale activities through both independent operations and production sharing contracts with foreign partners. We have added to our reserves in recent years primarily through our independent operations. As of December 31, 2002, independent properties accounted for approximately 53.2% of our total net proved reserves and approximately 56.0% of our total net proved undeveloped reserves. We are the operator of all of our independent producing properties. For the year ended December 31, 2002, production from our independent properties accounted for 46.3% of total net production.

Through our parent company, CNOOC, we have the exclusive right to enter into contracts with international oil and gas companies to conduct exploration and production activities offshore China. Under these production sharing contracts, we have the sole right to acquire, at no cost, up to a 51% participating interest in any successful discovery offshore China made by our foreign partners. Our foreign partners can recover their exploration costs under the production sharing contracts only if a commercially viable discovery is made. As of December 31, 2002, we had approximately 28 foreign partners under our production sharing contracts offshore China, all of which are international oil and gas companies, including Agip, BP, Burlington Resources, ChevronTexaco, ConocoPhillips, Devon Energy, Husky, Kerr-McGee, Newfield Exploration and Royal Dutch Shell. We are currently the operator or joint operator of most of the properties developed under our production sharing contracts.

Natural gas is becoming an increasingly important part of our business strategy because of rapidly growing domestic demand. In view of the domestic natural gas supply shortfall forecasted by the Chinese government, we have continued to develop our natural gas reserves and invested in liquefied natural gas related upstream projects outside the PRC. We continue to explore for natural gas and develop natural gas properties. We have acquired interests in gas reserves located in Tangguh, Indonesia and entered into an agreement to acquire interests in gas reserves located in the North West Shelf of Australia. In addition, CNOOC has granted us an option to invest in liquefied natural gas projects or other natural gas related businesses in which CNOOC has invested or proposes to invest in the PRC. Furthermore, in connection with this option, CNOOC will at its own expense procure all necessary PRC government approvals needed for our participation in the related projects or businesses.

On April 19, 2002, we completed the acquisition of Repsol YPF, S.A.'s interest in a portfolio of oil and gas production sharing and technical assistance contracts in areas located offshore and onshore Indonesia.

The PRC government established CNOOC, our parent company, as the state-owned offshore petroleum company of China in 1982, whereby CNOOC assumed overall responsibility for the administration and development of PRC offshore petroleum operations with foreign oil and gas companies. As a result of CNOOC's October 1999 reorganization, we became the only entity through which CNOOC engages in the offshore upstream petroleum business. CNOOC continues to perform administrative functions relating to our business. As of March 31, 2003, CNOOC indirectly owned or controlled an aggregate of approximately 70.6% of our shares.

We listed our ordinary shares on the Hong Kong Stock Exchange under the stock code "883" and our American Depositary Shares, or ADSs, on the New York Stock Exchange under the symbol "CEO" in February 2001. As of May 14, 2003, our equity market capitalization based on our Hong Kong share price was approximately HK$86.7 billion (US$11.1 billion).

Effective July 31, 2001, we were included as one of the 33 companies in the Hang Seng Stock Index in Hong Kong. We were also included in the Morgan Stanley Capital Index and the Hang Seng China-Affiliated Corporations Index in May and June of 2001, respectively. We currently are the only oil and gas company in the Hang Seng Index. On March 3, 2003, Standard & Poor's launched its S&P/HKEx LargeCap Index, which is comprised of 25 stocks on the Hong Kong Stock Exchange and includes our ordinary shares.

Our principal executive office is located at 65th Floor, Bank of China Tower, One Garden Road, Hong Kong, and our telephone number is (852) 2213-2500. We are a limited liability company incorporated in Hong Kong and are subject to the Companies Ordinance (Chapter 32 of the Laws of Hong Kong) and other applicable legislation of Hong Kong. As a company listed on both the Hong Kong Stock Exchange and the New York Stock Exchange, we are subject to their listing rules.

Competitive Strengths

We believe that our historical success and future prospects are directly related to a combination of our strengths, including the following:

Large proved reserve base with significant exploitation opportunities. Based on net proved reserves as of December 31, 2002 and average net daily production for the year ended December 31, 2002, we had a reserve-to-production ratio of approximately 15.9 years. As of December 31, 2002, approximately 60.6% of our net proved reserves were classified as net proved undeveloped. We expect our production to grow significantly as these undeveloped properties begin producing.

Sizable operating area with demonstrated exploration potential. The offshore China exploration area is approximately 1.3 million square kilometers in size, about twice as large as the U.S. Gulf of Mexico exploration area. As of December 31, 2002, a total of 797 exploration wells had been drilled offshore China. Between the beginning of 1999 and December 31, 2002, we made 15 discoveries and foreign parties made 15 discoveries offshore China.

Successful independent exploration and development record. From the inception of CNOOC in 1982 to December 31, 2002, we achieved a success rate of approximately 50% on our 177 offshore China independent wildcat wells, while our foreign partners achieved a success rate of approximately 29% on their 253 offshore China wildcat wells. Reserve additions from independent operations have accounted for approximately 67% of our total reserve additions offshore China since the beginning of 1997. Between late 1995 and the end of 2002, we completed seven of our major independent development projects on time and under budget.

Competitive cost structure. For the year ended December 31, 2002, our total offshore China lifting costs were US$3.92 per BOE. Total lifting costs for independent operations offshore China were US$3.89 per BOE during the same period. Lifting costs consist of operating expenses and production taxes. Our average finding and development cost for the three years ended December 31, 2002 was US$4.59 per BOE, or US$4.54 per BOE as adjusted for the estimated future costs of developing proved undeveloped reserves. We believe that this cost structure allows us to compete effectively even in a low crude oil price environment.

Reduced risks and access to capital and technology through production sharing contracts. Production sharing contracts help us minimize our offshore China finding costs, exploration risks and capital requirements because our foreign partners are responsible for all costs associated with exploration. Our foreign partners recover their exploration costs only if a commercially viable discovery is made.

Strategic position in China's growing natural gas markets. The proximity of our natural gas reserves to the major demand areas in the coastal regions of China provides us with a competitive advantage over other natural gas suppliers in China, whose natural gas reserves are located primarily in northwest and southwest China. We have natural gas fields near many of China's rapidly growing coastal areas, including Hong Kong, Shanghai and Tianjin. We have also acquired interests in gas reserves located in Tangguh, Indonesia and entered into an agreement to acquire interests in gas reserves located in the North West Shelf of Australia. In addition, CNOOC has granted us an option to invest in liquefied natural gas projects or other natural gas related businesses in the PRC in which CNOOC has invested or proposes to invest, which includes an option to acquire CNOOC's interest in a liquefied natural gas terminal in Guangdong Province, China. For further information, see "Business—Natural Gas Business."

Experienced management team. Our senior management team has extensive experience in the oil and gas industry, and most of our executives have been with the CNOOC group since its inception in 1982. We evolved from a company heavily reliant on production sharing contracts with foreign partners to a company with a balance of both independent and production sharing contract operations. Our management team and staff have had the opportunity to work closely with foreign partners both within and outside China. We have implemented international management practices including incentive compensation schemes for our employees. In addition, we have adopted a share option scheme for our employees. See "Management—Share Option Scheme."

Business Strategy

We intend to continue expanding our oil and gas exploration and production activities and, where appropriate, to continue making strategic investments in natural gas businesses. While our expansion strategy will continue to focus primarily on offshore China, we may also consider overseas acquisition opportunities that may be presented to us. The principal components of our strategy are as follows:

- increase production primarily through the development of our net proved undeveloped reserves;
- add to our reserves through independent exploration and production sharing contracts;
- capitalize on the growing demand for natural gas in China;
- selectively pursue acquisitions to ensure long-term production growth, geographical reserves risk diversification, and to further our natural gas strategy;
- maintain operational efficiency and low production costs; and
- maintain financial flexibility through conservative financial practices.

Recent Developments

Development and Production

On February 27, 2003, we announced the drilling of a successful wildcat well in Bozhong 34-1S-1 in southern Bohai Bay. The well was drilled on the Bozhong 34-1S structure located about 3 kilometers southeast of the Bozhong 34-2 producing oilfield.

On December 31, 2002, we began to produce oil from the Penglai 19-3 oilfield in the Bohai Bay. Penglai 19-3 is China's largest offshore oilfield. As of December 31, 2002, our share of net proved reserves in the Penglai 19-3 field was 123 million BOE. The project is a production sharing contract between ConocoPhillips and us. We hold a 51% participating interest in it.

On July 11, 2002, we announced that we commenced commercial production at our Wenchang project located in the Western South China Sea, approximately 400 kilometers southwest of Hong Kong and 140 kilometers east of Hainan Island, China. The Wenchang project consists of the Wenchang 13-1 and 13-2 fields. We are the operator of both fields and hold a 60% working interest in the project. The average net production for 2002 from the Wenchang project was 19,794 BOE per day.

Acquisitions

On March 7, 2003, we announced that we entered into an agreement with a subsidiary of the BG Group to acquire an interest in the North Caspian Sea Project in Kazakhstan, subject to certain conditions including the waiver of certain preemptive rights held by the current partners to the project. On May 9, 2003, some current partners to the project elected to exercise their preemptive rights and, accordingly, we did not acquire any interest in the project.

On January 1, 2003, we acquired BP Muturi Limited, which owns a 44.0% interest in the Muturi production sharing contract, and BP Wiriagar Limited's 42.4% interest in the Wiriagar production sharing contract for a total of approximately US$275 million. The Muturi and Wiriagar production sharing contracts, together with the Berau production sharing contract, make up the Tangguh LNG Project. The Tangguh LNG Project is a greenfield project located offshore Indonesia and represents one of the largest natural gas projects in Asia. Our interests in these two production sharing contracts represent approximately 12.5% of the total reserves and upstream production of the Tangguh LNG Project. The remaining interests in the Tangguh LNG Project are held by BP Berau (34.2%), BP Muturi (0.2%), BP Wiriagar Ltd. (2.7%), MI Berau (16.3%), Nippon (12.2%), BG (10.7%), KG Berau (8.6%), KG Wiriagar (1.4%) and Indonesia Natural Gas Resources Muturi (1.1%).

In October 2002, we entered into a key terms agreement to purchase an aggregate interest of approximately 5.56% in the reserves and upstream production of Australia's North West Shelf Gas Project for approximately US$365.6 million, subject to certain adjustments. Under the terms of this agreement, we would purchase our interest from the six current partners to this project: BHP Billiton, BP, ChevronTexaco, Japan Australia LNG (MIMI), Shell and Woodside Energy. Our estimated share of reserves from this project would be approximately 1.2 trillion cubic feet of natural gas. Our share of natural gas together with associated liquids would be approximately 210 million BOE. Woodside Petroleum is the operator for the project. Under the terms of the agreement, we would also acquire a 25% interest in the China LNG Joint Venture, which is being established by the six current partners to supply liquefied natural gas from the North West Shelf Gas Project to a liquefied natural gas terminal currently being developed by CNOOC and various partners in Guangdong Province, China. We expect to complete our acquisition of the interests in the North West Shelf Gas Project and China LNG Joint Venture in 2003. See "Business—Natural Gas Business—Overseas Activity."

The Offering

The following is a brief summary of the terms of this offering. For a more complete description of the terms of the notes, see "Description of the Notes and Guarantees" in this offering memorandum.

Issuer	CNOOC Finance (2003) Limited, a company incorporated with limited liability on April 2, 2003 in the British Virgin Islands under the International Business Companies Act (Registration No. 540274).
Guarantor	CNOOC Limited, a company incorporated with limited liability on August 20, 1999 in Hong Kong under the Companies Ordinance (Registration No. 685974).
Notes Offered	US$200,000,000 aggregate principal amount of 4.125% guaranteed notes due 2013 ("2013 notes"), and US$300,000,000 aggregate principal amount of 5.500% guaranteed notes due 2033 ("2033 notes").
Guarantees	Payment of principal of, interest and any Additional Amount on, the notes is irrevocably and unconditionally guaranteed by us.
Issue Price	2013 notes: 98.638% of principal amount, plus accrued interest, if any, from May 21, 2003, to the issue date. 2033 notes: 97.393% of principal amount, plus accrued interest, if any, from May 21, 2003, to the issue date.
Maturity Date	2013 notes: May 21, 2013. 2033 notes: May 21, 2033.
Interest Payment Dates	May 21 and November 21, commencing November 21, 2003.
Interest	The 2013 notes will bear interest from May 21, 2003 at the rate of 4.125% per annum, payable semiannually in arrears from May 21, 2003. The 2033 notes will bear interest from May 21, 2003 at the rate of 5.500% per annum, payable semiannually in arrears from May 21, 2003. Interest will be calculated on the basis of a 360-day year, consisting of twelve 30-day months.
Further Issues	The 2013 notes and the 2033 notes will be issued in initial aggregate principal amounts of US$200,000,000 and US$300,000,000, respectively. We and the issuer may, however, from time to time, without the consent of the respective holders of a series of the notes, create and issue, pursuant to the related indenture, additional guaranteed notes, having the same terms and conditions under the indenture as the previously outstanding series of notes in all respects (or in all respects except for the date for, and the amount of, the first payment of interest thereon) so that the same shall be consolidated and form a single series with the previously outstanding series of notes.

Ranking	The notes will constitute direct, unsecured and unsubordinated obligations of the issuer ranking *pari passu*, without any preference or priority of payment among themselves, with all other unsecured and unsubordinated indebtedness of the issuer (except obligations preferred by applicable law). The guarantees will constitute our direct, unsecured and unsubordinated obligations ranking *pari passu* with all our other unsecured and unsubordinated indebtedness (except obligations preferred by applicable law).
Certain Covenants	We have covenanted in the indentures, with certain exceptions, not to incur certain liens or consolidate, merge or sell our assets substantially as an entirety unless certain conditions are satisfied. The notes and the indentures do not otherwise restrict or limit our ability to incur additional indebtedness by ourself or our subsidiaries or our ability to enter into transactions with, or to pay dividends or make other payments to, affiliates. See "Description of the Notes and Guarantees—Limitation on Liens," "—Limitation on Sale and Leaseback Transactions" and "—Consolidation, Merger and Sale of Assets."
Additional Amounts..........................	In the event that British Virgin Islands, Hong Kong or PRC taxes are payable in respect of payments pursuant to the notes or the guarantees, we or the issuer, as the case may be, will, subject to certain exceptions, pay such Additional Amounts under the notes as will result, after deduction or withholding of such taxes, in the payment of the amounts that would have been payable in respect of the notes had no deduction or withholding been required. See "Description of the Notes and Guarantees—Additional Amounts."
Optional Tax Redemption................	Each series of notes may be redeemed at our option or the option of the issuer, in whole but not in part, at the principal amount thereof, plus accrued and unpaid interest, in the event we become or the issuer becomes obligated to pay Additional Amounts in respect of the notes or guarantees of that series. See "Description of the Notes and Guarantees—Optional Tax Redemption."
Transfer Restrictions	The notes have not been registered under the U.S. Securities Act, any state securities laws in the United States or the securities laws of any other jurisdiction. Unless they are registered, the notes may not be sold except pursuant to an exemption from or in a transaction not subject to the registration requirements of the U.S. Securities Act, applicable state securities laws or the applicable securities laws of any other jurisdiction. See "Transfer Restrictions."
Use of Proceeds................................	The aggregate proceeds of this offering of approximately US$486 million will be advanced, after deducting offering related expenses, by the issuer to us and used for general corporate purposes.
Governing Law.................................	The notes, the guarantees and the indentures will be governed by, and construed in accordance with, the laws of the State of New York.

Denomination, Form and Registration	The notes will be issued in denominations of US$1,000 and integral multiples of US$1,000 above that amount. Notes offered in the United States to qualified institutional buyers in reliance on Rule 144A will be represented by one or more permanent global notes in fully registered form without interest coupons deposited with The Bank of New York as custodian for, and registered in the name of, Cede & Co., as nominee of The Depository Trust Company, or DTC. Notes offered to non-U.S. persons outside the United States in reliance on Regulation S will be represented by one or more permanent global notes in fully registered form without interest coupons deposited with The Bank of New York as custodian for, and registered in the name of, Cede & Co., as nominee of DTC for the respective accounts of Euroclear Bank S.A./N.V., as operator of the Euroclear System, or Euroclear, and Clearstream Banking, *société anonyme*, or Clearstream, Luxembourg. Prior to the 40th day after the later of the commencement of the offering and the issue date, beneficial interests in the Regulation S global notes may be held only through Euroclear or Clearstream, Luxembourg. DTC will credit the account of each of its participants, including Euroclear and Clearstream, Luxembourg, with the principal amount of notes being purchased by or through such participant. Beneficial interests in the global notes will be shown on, and transfers thereof will be effected only through, records maintained by DTC and its direct and indirect participants, including Euroclear and Clearstream, Luxembourg.
Ratings	The notes have been rated Baa1 with positive outlook by Moody's Investors Service and "BBB" by Standard & Poor's Ratings Services. Security ratings are not recommendations to buy, sell or hold the notes. Ratings are subject to revision or withdrawal at any time by the rating agencies.
Risk Factors	See "Risk Factors" and the other information in this offering memorandum for a discussion of factors that should be carefully considered before deciding to invest in the notes.
Listing	Application has been made to list the notes on the Luxembourg Stock Exchange.
Trustee	The Bank of New York.

Summary Historical Consolidated Financial Data

The following tables present a summary of our financial information for the periods indicated. The summary income statement data for the years ended December 31, 2000 and 2001 and the summary balance sheet data as of December 31, 2000 and 2001 have been derived from our consolidated financial statements audited by Arthur Andersen & Co, our independent public accountants prior to 2002. The summary income statement data for the year ended December 31, 2002 and the summary balance sheet data as of December 31, 2002 have been derived from our consolidated financial statements audited by Ernst & Young, our current independent public accountants. The summary financial data included in this section should be read in conjunction with our consolidated financial statements beginning on page F-1. For a discussion on the change of our accountants, see "Risk Factors—Risks relating to our Business—You may not be able to assert claims against Arthur Andersen, our independent public accountants for periods prior to December 31, 2001, nor may you be able to assert claims against our current independent public accountants for financial statements previously audited by Arthur Andersen" and "Management's Discussion and Analysis of Financial Condition and Results of Operations—Change of Accountants." Our consolidated financial statements are prepared and presented in accordance with Hong Kong GAAP. For an explanation of the reconciliation of our net income and shareholders' equity to U.S. GAAP, see note 38 to our consolidated financial statements beginning on page F-1.

	Year ended December 31,			
	2000	**2001**	**2002**	**2002**
	Rmb	**Rmb**	**Rmb**	**US$**
		(in millions)		
Income Statement Data:				
Hong Kong GAAP				
Operating revenues:				
Oil and gas sales	18,819	17,561	23,779	2,872
Marketing revenues	5,126	2,537	2,377	287
Other income	279	722	217	26
Total operating revenues	24,224	20,820	26,374	3,185
Expenses:				
Operating expenses	(2,124)	(2,329)	(3,775)	(456)
Production taxes	(1,037)	(884)	(1,023)	(124)
Exploration expenses	(553)	(1,039)	(1,318)	(159)
Depreciation, depletion and amortization	(2,578)	(2,567)	(4,020)	(486)
Dismantlement	(104)	(90)	(126)	(15)
Crude oil and product purchases	(5,098)	(2,453)	(2,326)	(281)
Selling and administrative expenses	(456)	(616)	(1,007)	(122)
Other	(217)	(618)	(31)	(4)
	(12,167)	(10,596)	(13,626)	(1,647)
Interest income	237	318	148	18
Interest expenses	(475)	(117)	(295)	(36)
Exchange gain (loss), net	381	235	(114)	(14)
Investment income	—	221	193	23
Share of profit of an associate	218	90	165	20
Non-operating profit (loss), net	(195)	35	(71)	(9)
Income before tax	12,223	11,006	12,774	1,540
Tax	(1,926)	(3,048)	(3,541)	(428)
Net income	10,297	7,958	9,233	1,112
U.S. GAAP				
Operating revenues:				
Oil and gas sales	18,819	17,561	23,779	2,872
Marketing revenues	5,126	2,537	2,377	287
Other income	279	722	217	26
Total operating revenues	24,224	20,820	26,374	3,185
Net income	10,302	7,920	9,088	1,098

	As of December 31,			
	2000	2001	2002	2002
	Rmb	Rmb	Rmb	US$
		(in millions)		
Balance Sheet Data:				
Hong Kong GAAP				
Cash and cash equivalents	2,797	6,394	7,839	947
Time deposits with maturities over three months	3,425	2,050	4,690	566
Short-term investments	300	8,896	6,531	789
Current assets	9,472	20,030	24,487	2,957
Property, plant and equipment, net	22,654	23,828	36,072	4,357
Investment in an associate	471	462	537	65
Total assets	32,597	44,320	61,096	7,378
Current liabilities	8,768	4,392	7,134	862
Long-term bank loans, net of current portion	4,749	3,256	941	114
US$500 million in 6.375% long-term guaranteed notes due 2012	—	—	4,071	492
Total long-term liabilities	7,707	6,617	13,393	1,618
Total liabilities	16,475	11,009	20,527	2,479
Shareholders' equity	16,122	33,311	40,568	4,900
U.S. GAAP				
Total assets	32,330	44,062	59,984	7,244
Total long-term liabilities	7,707	6,617	13,393	1,618
Shareholders' equity	15,855	33,053	39,884	4,817

	Year ended December 31,			
	2000	2001	2002	2002
	Rmb	Rmb	Rmb	US$
	(in millions, except percentage and ratio information)			
Other Financial Data:				
Hong Kong GAAP				
Capital expenditures paid	4,404	4,343	6,833	825
Cash provided by (used for):(1)				
Operating activities	13,233	11,759	14,597	1,763
Investing activities	(7,861)	(11,366)	(11,724)	(1,416)
Financing activities	(3,454)	3,204	(1,428)	(172)
EBITDE(2)	15,315	14,366	18,499	2,235
EBITDE margin(3)	63.2%	69.0%	70.1%	70.1%
Ratio of EBITDE to gross interest expense(4)	32.2x	45.5x	45.7x	45.7x
Ratio of total debt to EBITDE	0.4x	0.3x	0.3x	0.3x
Ratio of total debt to total capitalization(5)	27.5%	12.3%	11.6%	11.6%
U.S. GAAP				
Cash provided by (used for):				
Operating activities(6)	13,233	11,759	14,597	1,763
Investing activities	(7,861)	(11,366)	(11,724)	(1,416)
Financing activities	(3,454)	3,204	(1,428)	(172)
Ratio of cash provided by operating activities to gross interest expense(4)(6)	27.9x	37.2x	44.6x	44.6x
Ratio of total debt to cash provided by operating activities(6)	0.4x	0.4x	0.4x	0.4x
Net income(7)	10,302	7,920	9,088	1,098
Net income margin(7)(8)	42.5%	38.0%	34.5%	34.5%
Ratio of net income to gross interest expense(4)(7)	21.7x	25.1x	27.8x	27.8x
Ratio of total debt to net income(7)	0.6x	0.6x	0.6x	0.6x
EBITDE(2)	15,315	14,319	18,483	2,232
EBITDE margin(3)	63.2%	68.8%	70.2%	70.1%
Ratio of EBITDE to gross interest expense(4)	32.2x	45.4x	56.6x	56.6x
Ratio of total debt to EBITDE	0.4x	0.3x	0.3x	0.3x
Ratio of total debt to total capitalization(5)	27.9%	12.4%	11.8%	11.8%

(1) In accordance with a new accounting pronouncement, SSAP 15 "Cash Flow Statements," the presentation of cash flows for 2000 and 2001 conforms to the presentation of cash flows for 2002. For further information on HK SSAP 15, see "Management's Discussion and Analysis of Financial Condition and Results of Operations—Recent Accounting Pronouncements."

(2) We have defined EBITDE to mean earnings before interest income, interest expense, income taxes, depreciation, depletion, amortization, dismantlement, exploration expenses, impairment losses related to property, plant and equipment and exchange gains or losses as computed under Hong Kong and U.S. GAAP. EBITDE is not a standard measure under either Hong Kong or U.S. GAAP. You should not consider our definition of EBITDE in isolation or construe it as an alternative to net income, cash provided by operating activities or any other measure of performance or as an indicator of operating performance, liquidity or any other standard measure under either Hong Kong or U.S. GAAP. We believe net income and cash provided by operating activities are the most directly comparable financial measures for EBITDE as an indicator of our operating performance and liquidity, respectively. For our management's explanation of how we define EBITDE and why we use it, see "Management's Discussion and Analysis of Financial Condition and Results of Operations—Overview—Non-GAAP Financial Measures."

(3) EBITDE margin represents EBITDE as a percentage of our total operating revenues, as computed under both Hong Kong and U.S. GAAP. EBITDE margin is used as an indicator of operating performance.

(4) Gross interest expense includes capitalized interest.

(5) Total capitalization excludes current portion of long-term debt.

(6) We have included data relating to cash provided by operating activities in this table because we believe it is the most directly comparable Hong Kong and U.S. GAAP measure to EBITDE as an indicator of liquidity. EBITDE is not a standard measure under either Hong Kong or U.S. GAAP.

(7) We have included net income data in this table because we believe it is the most directly comparable Hong Kong and U.S. GAAP measure to EBITDE as an indicator of operating performance. EBITDE is not a standard measure under either Hong Kong or U.S. GAAP.

(8) Net income margin represents net income as a percentage of our total operating revenues, as computed under U.S. GAAP.

Summary Operating and Reserves Data

The following table sets forth our operating data and our net proved reserves as of and for the periods indicated.

	Year ended December 31,		
	2000	2001	2002
Net Production:			
Oil (daily average bbls/day)	206,347	228,873	298,625
Gas (daily average mmcf/day)	197.9	195.0	272.6
Oil equivalent (BOE/day)	239,335	261,379	346,639
Average net realized prices:			
Oil (per bbl)	US$28.21	US$23.34	US$24.35
Gas (per mcf)	3.09	3.08	2.98
Offshore China lifting costs (per BOE)[(1)]	4.45	4.16	3.92
Overseas lifting costs (per BOE)[(1)(2)]	—	—	9.06
Three-year average finding and development costs (BOE)[(3)]	US$2.77	US$4.86	US$4.59
Adjusted three-year average finding and development costs (per BOE)[(4)]	US$3.82	US$4.15	US$4.54
Net Proved Reserves (end of period):			
Oil (mmbbls)	1,215.8	1,245.9	1,424.4
Gas (bcf)	3,249.7	3,247.6	3,547.9
Total (million BOE)	1,757.4	1,787.1	2,015.8
Proved developed reserves (million BOE)	638.6	710.0	794.3
Annual reserves replacement ratio	104%	131%	281%
Estimated reserves life (years)	20.1	18.7	15.9
Present value of estimated future net revenues before income taxes (discounted at 10%) (million Rmb)	108,423	69,860	140,798
Standardized measure of discounted future net cash flows (million Rmb)	93,391	51,082	100,141

(1) Includes operating expenses and production taxes. During the years ended December 31, 2000 and 2001, our overseas operations were not material and our overseas lifting costs were included in our offshore China lifting costs for those years.

(2) Overseas lifting costs reflect lifting costs associated with our operations in Indonesia and are calculated using the net entitlement method.

(3) The three-year average finding and development costs for each of 2000, 2001 and 2002 are calculated by taking the sum of total costs incurred for exploration and development of oil and gas fields in the immediately preceding three-year period and dividing it by the sum of the reserve additions, extensions and revisions for the same three years.

(4) Because a high percentage of our net proved reserves are classified as proved undeveloped, we also presented the adjusted three-year average finding and development cost to reflect the estimated future costs of developing these proved undeveloped reserves as of December 31, 2000, 2001 and 2002, as estimated by Ryder Scott Company. The actual future costs of developing these reserves may differ from these estimates. See the definition of "adjusted finding and development cost per BOE" in "Certain Oil and Gas Terms."

At our request, Ryder Scott Company, independent petroleum engineering consultants, carried out an independent evaluation of the reserves of selected properties as of December 31, 2000, 2001 and 2002. We have obtained a summary report from Ryder Scott Company describing its procedures and conclusions as of December 31, 2002, and its summary report appears as Appendix A to this offering memorandum. For further information regarding our reserves, see "Risk Factors—Risks relating to our business—The oil and gas reserve estimates in this offering memorandum may require substantial revision as a result of future drilling, testing and production," and "Business—Oil and Natural Gas Reserves."

The following table sets forth summary information with respect to our estimated net proved reserves of oil and natural gas as at the dates indicated.

	Net proved reserves at December 31,		Net proved reserves at December 31, 2002		
	2000	2001	Developed	Undeveloped	Total
Bohai Bay:					
Crude oil (mmbbls)	923.9	961.3	381.1	611.4	992.5
Natural gas (bcf)	591.4	629.1	182.1	416.5	598.6
Total (million BOE):	1,022.4	1,066.2	411.4	680.9	1,092.3
Independent (million BOE)	774.2	689.7	326.8	268.3	595.1
Production sharing contracts (million BOE)	248.2	376.5	84.6	412.6	497.2
Western South China Sea:					
Crude oil (mmbbls)	141.1	131.6	99.0	61.4	160.4
Natural gas (bcf)	2,593.0	2,421.5	499.6	2,011.6	2,511.2
Total (million BOE):	573.3	535.1	182.3	396.6	578.9
Independent (million BOE)	372.0	373.3	50.9	383.3	434.2
Production sharing contracts (million BOE)	201.3	161.8	131.4	13.3	144.7
Eastern South China Sea:					
Crude oil (mmbbls)	136.8	132.2	58.9	61.4	120.3
Natural gas (bcf)	—	—	—	42.8	42.8
Total (million BOE):	136.8	132.2	58.9	68.6	127.5
Independent (million BOE)	—	—	—	—	—
Production sharing contracts (million BOE)	136.8	132.2	58.9	68.6	127.5
East China Sea:					
Crude oil (mmbbls)	4.5	12.4	2.9	9.6	12.5
Natural gas (bcf)	65.3	197.0	42.1	137.3	179.4
Total (million BOE):	15.4	45.2	9.9	32.5	42.4
Independent (million BOE)	15.4	45.2	9.9	32.5	42.4
Production sharing contracts (million BOE)	—	—	—	—	—
Overseas:					
Crude oil (mmbbls)	9.5	8.4	114.8	23.9	138.7
Natural gas (bcf)	—	—	101.5	114.4	215.9
Total (million BOE):	9.5	8.4	131.8	42.9	174.7
Independent (million BOE)	—	—	—	—	—
Production sharing contracts (million BOE)	9.5	8.4	131.8	42.9	174.7
Total:					
Total crude oil (mmbbls)	1,215.8	1,245.9	656.7	767.7	1,424.4
Total natural gas (bcf)	3,249.7	3,247.6	825.2	2,722.7	3,547.9
Total (million BOE):	1,757.4	1,787.1	794.3	1,221.5	2,015.8
Independent (million BOE)	1,161.6	1,108.2	387.6	684.1	1,071.7
Production sharing contracts (million BOE)	595.8	678.9	406.7	537.4	944.1

RISK FACTORS

Before purchasing the notes, you should be aware that there are various risks, including those described below. You should carefully consider these risks, together with all of the other information in this offering memorandum, before you decide to purchase any notes.

Risks relating to our business

Our business, revenues and profits fluctuate with changes in oil and gas prices.

Even relatively modest declines in crude oil prices may adversely affect our business, revenues and profits. Our profitability is determined in large part by the difference between the prices received for the crude oil we produce and the costs of exploring for, developing, producing and selling these products.

Prices for crude oil fluctuate widely in response to relatively minor changes in the supply and demand for oil, market uncertainty and various other factors that are beyond our control, including:

- political developments in petroleum producing regions;
- the ability of the Organization of Petroleum Exporting Countries and other petroleum producing nations to set and maintain production levels and prices;
- the price and availability of other energy sources, such as coal;
- domestic and foreign government regulation;
- weather conditions; and
- overall economic conditions.

Our revenues and net income have fluctuated significantly in the past four years, principally due to the volatility of world oil prices. Over the past year, oil prices rose 62% from US$19.84 per barrel on January 1, 2002 to US$32.20 per barrel on December 31, 2002. In the last half of 2002, worldwide oil prices rose due to increasing political and economic turmoil in Venezuela and the conflict in Iraq. These uncertainties, together with the conflict in Iraq, raised concerns about the security and availability of ample supplies to meet growing demand, although oil prices recently have fallen. The international benchmark crude oil, West Texas Intermediate, was US$29.17 per barrel on May 14, 2003. For a description of oil prices in recent years, see "Business—Sales and Marketing—Sales of Offshore Crude Oil—Pricing" in this offering memorandum. Any future declines in oil and gas prices would adversely affect our revenues and net income.

The prices for the natural gas we sell in the PRC market are determined by negotiations between us and the prospective buyers. Our typical contracts with gas buyers include provisions for annual resets and adjustment formulas that depend on a basket of crude oil prices and inflation as well as various other factors. These resets and adjustment formulas can result in natural gas price fluctuations which may adversely affect our business, results of operations and financial condition.

Lower oil and gas prices may result in the write-off of higher cost reserves and other assets and in decreased earnings or losses. Lower oil and natural gas prices may also reduce the amount of oil and natural gas we can produce economically and render existing contracts that we have entered into uneconomical. For further details regarding the effects of oil and gas price fluctuations on our financial condition and results of operations, see "Management's Discussion and Analysis of Financial Condition and Results of Operations."

The oil and gas reserve estimates in this offering memorandum may require substantial revision as a result of future drilling, testing and production.

The reliability of reserves estimates depends on a number of factors, including:

- the quality and quantity of technical and economic data;
- the prevailing oil and gas prices for our production;
- the production performance of reservoirs;
- extensive engineering judgments; and
- consistency in the PRC government's royalty and share oil policies.

Many of the factors, assumptions and variables involved in estimating reserves are beyond our control and may prove to be incorrect over time. Consequently, the results of drilling, testing and production may require substantial upward or downward revisions in our initial reserves data. For more information on our oil and gas reserves data, see "Business—Oil and Natural Gas Reserves."

Any failure to develop our proved undeveloped reserves and gain access to additional reserves could impair our ability to achieve certain growth objectives.

Our ability to achieve certain growth objectives depends upon our success in finding and acquiring or gaining access to additional reserves. Future drilling, exploration and acquisition activities may not be successful. If our exploration and development activities or acquisition of properties containing proved reserves are unsuccessful, our total proved reserves will decline.

Approximately 60.6% of our proved reserves were undeveloped as of December 31, 2002. Our future success will depend on our ability to develop these reserves in a timely and cost-effective manner. There are various risks in developing reserves, including construction, operational, geophysical, geological and regulatory risks.

Our future prospects largely depend on our capital expenditure plans, which are subject to various risks.

The oil and gas exploration and production business is capital intensive. We currently plan to spend approximately US$2.7 billion to develop our oil and gas properties and approximately US$308 million for independent exploration from 2003 through the end of 2004. In addition to these amounts, we may make additional capital expenditures and investments to implement our business strategy.

The ability to maintain and increase our revenues, net income and cash flows depends upon continued capital spending. We adjust our capital expenditure and investment budget each year. Our capital expenditure plans are subject to a number of contingencies, some of which are beyond our control. These variables include:

- our ability to generate sufficient cash flows from operations to finance our capital expenditures, investments and other requirements;
- the availability and terms of external financing;
- changes in crude oil and natural gas prices, which may affect cash flows from operations and capital expenditure and investment plans;
- the mix of exploration and development activities conducted on an independent basis and under production sharing contracts;

- new investment opportunities that may be presented to us, including international investment opportunities and liquefied and other natural gas projects;

- PRC government approvals required for certain capital expenditures and investments;

- our ability to obtain sufficient foreign currency to finance our capital expenditures; and

- economic, political and other conditions in the PRC and Hong Kong.

Therefore, our actual future capital expenditures and investments may differ significantly from our current planned amounts. There can be no assurance that we will be able to execute our capital expenditure program on schedule or as planned.

Any failure to implement our natural gas business strategy may adversely affect our business and financial position.

As part of our business strategy and to meet increasing market demand in China, we continue to expand our natural gas business. This strategy involves a number of risks and uncertainties including the following:

- we have limited experience in investing in liquefied natural gas facilities, gas transmission and distribution systems, and overseas upstream natural gas properties;

- any additional capital expenditures that are necessary to implement our natural gas strategy could divert resources from our core oil and gas exploration and production business and require us to seek additional financing;

- our new natural gas operations may face additional competition from a number of international and PRC companies. In particular, PetroChina Company Limited, or PetroChina, is constructing natural gas pipelines to link its natural gas fields located in the western part of China to the eastern coastal regions. See "The PRC Petroleum Industry;"

- our new natural gas activities may subject us to additional government regulation in China and overseas;

- our overseas natural gas businesses are subject to economic and political risks, particularly in Indonesia. See "—We may be exposed to certain operating risks in Indonesia and Australia as a result of our acquisition of oil and gas interests located in these regions;"

- we do not have the same preferential rights or access to natural gas businesses or overseas natural gas investments that we enjoy with respect to our upstream natural gas business offshore China; and

- we are evaluating an option to make an investment in CNOOC's liquefied natural gas project in Guangdong Province. However, we have not decided whether to exercise this option. This option is subject to various conditions, including certain governmental approvals.

Due to the above factors or other reasons, we may fail to implement our natural gas strategy successfully.

The infrastructure and demand for natural gas in the PRC may proceed at a slower pace than our planned increase in production.

Our proposed expansion of natural gas production in China is currently constrained by a lack of natural gas transmission and supply infrastructure and an underdeveloped natural gas market. Construction of transmission and supply pipelines and other infrastructure depends on many factors, many of which are beyond our control, such as government funding, costs of land acquisition, national and local government approvals, and timely completion of construction. Development of the natural gas market depends on the establishment of long-term natural gas supply contracts with natural gas utilities or large end-users, such as power and chemical plants. The demand of these buyers for natural gas could be affected by a number of regulatory and market factors, such as regulation of coal prices, government power and utility policies, chemical commodity cycles, electricity pricing and demand, and environmental policies.

CNOOC largely controls us, and we regularly enter into related party transactions with CNOOC and its affiliates.

CNOOC indirectly owns, through CNOOC (BVI) Limited, a wholly owned subsidiary, an aggregate of approximately 70.6% of our shares. As a result, CNOOC is able to control the composition of our board of directors, determine the timing and amount of our dividend payments and otherwise control us. Although CNOOC is required to comply with provisions in the Hong Kong Stock Exchange listing rules relating to protection for minority shareholders, there can be no assurance that CNOOC will act in a manner that benefits all of our shareholders. If CNOOC takes actions that favor its interests over ours, our results of operations and financial position may be adversely affected.

We regularly enter into transactions with CNOOC and its affiliates, including China Oilfield Services Limited and CNOOC Finance Corporation Limited. For the year ended December 31, 2002, sales to CNOOC and its affiliates accounted for approximately 16.5% of our total revenues. For further details, see "Relationship with CNOOC and Certain Related Party Transactions." Our transactions with CNOOC and its affiliates constitute connected transactions under the Hong Kong Stock Exchange listing rules. We must obtain the prior approval of the Hong Kong Stock Exchange to engage in some of these transactions and may also be required to obtain the prior approval of our independent directors and our independent shareholders. If we do not obtain these approvals, we may not be allowed to execute these transactions, and our business operations and financial condition could be adversely affected.

Under current PRC law, CNOOC has the exclusive right to enter into production sharing contracts with international oil and gas companies for petroleum exploration and production offshore China. CNOOC has undertaken to us that it will transfer all of its rights and obligations under any new production sharing contracts to us, except those relating to its administrative functions. PRC law restricts us from contracting directly with foreign enterprises for these purposes without CNOOC. The interests of CNOOC in entering into production sharing contracts with international oil and gas companies may differ from our interest, especially with respect to the criteria for determining whether, and on what terms, to enter into production sharing contracts. Our future business development may be adversely affected if CNOOC does not enter into new production sharing contracts on terms that are acceptable to us.

A substantial drop in sales to any of our three main customers could have a material adverse affect on our results of operations.

We sell a significant proportion of our production to China Petroleum & Chemical Corporation, or Sinopec, PetroChina and the Castle Peak Power Company. For the years ended December 31, 2000, 2001 and 2002, sales to Sinopec accounted for approximately 26.1%, 30.2% and 26.1% respectively, of our total operating revenues, while sales to PetroChina were approximately 6.0%, 6.3% and 4.5% respectively, of our total operating revenues. Both PetroChina and Sinopec are majority owned by the PRC government. We sell a significant portion of our natural gas to Castle Peak Power Company Limited in Hong Kong under a long-term take-or-pay contract. For the years ended December 31, 2000, 2001 and 2002, sales to this customer were approximately 5.0%, 5.8% and 4.7%, respectively, of our total operating revenues.

Both PetroChina and Sinopec have their own oil and gas fields and have the right to import crude oil directly from the international market. We do not have any long-term sales contracts with Sinopec or PetroChina. Our business, results of operations and financial condition would be adversely affected if either Sinopec or PetroChina significantly reduces its purchases of crude oil from us and we cannot find another ready buyer for our crude oil in the international market.

The PRC offshore petroleum and natural gas industries are highly competitive and our success depends on several factors.

We compete in the PRC and international markets for customers, capital financing and business opportunities, including desirable oil and gas prospects. The performance of our competitors may also affect the international market price for comparable crude oil, which in turn would likely affect the price of our crude oil. Our principal competitors in the PRC market are PetroChina and Sinopec. For further details, see "Business—Competition."

We are the dominant player in the oil and gas industry offshore China. We are the only company authorized to engage oil and gas exploration offshore China in cooperation with international oil and gas companies. Any change to PRC law that allows new entrants into the offshore petroleum industry could increase the competition for new oil and gas properties offshore China.

CNOOC has undertaken to us that so long as it retains a controlling interest in us and our securities are listed on the Hong Kong Stock Exchange, the New York Stock Exchange or other securities trading systems in other parts of the world, we will have the exclusive right to exercise CNOOC's rights to engage in offshore oil and gas exploration, development, production and sales in the PRC and that it will not compete with us in this business. However, CNOOC's controlling interest in us may not continue in the future and CNOOC's undertaking may be subject to interpretative challenges. See "Relationship with CNOOC and Certain Related Party Transactions."

Exploration, development and production risks and natural disasters affect our operations and could result in losses that are not covered by insurance.

Our petroleum exploration, development and production operations are subject to various risks, including pipeline ruptures and spills, fires, explosions, encountering formations with abnormal pressures, blowouts, cratering and natural disasters. Any of these results could result in loss of hydrocarbons, environmental pollution and other damage to our properties and the properties of operators under production sharing contracts. In addition, we face the risk that we may not discover any economically productive natural gas or oil reservoirs. The costs of drilling, completing and operating wells also are uncertain and are subject to numerous factors beyond our control, including:

- weather conditions;
- natural disasters;
- equipment shortages and delays; and
- lack of adequate transportation facilities.

We maintain insurance coverage against some, but not all, potential losses. We do not maintain business interruption insurance for all of our oil and gas fields. We may suffer material losses resulting from uninsurable or uninsured risks or insufficient insurance coverage.

For further information on insurance coverage, see "Business—Operating Hazards and Uninsured Risks."

We may be exposed to certain operating risks in Indonesia and Australia as a result of our acquisition of oil and gas interests located in these regions.

We acquired interests in oil and gas properties located offshore Indonesia in April 2002 and January 2003 and recently entered into conditional agreements to acquire interests in Australia's North West Shelf Project. See "Business—Principal Oil and Gas Regions—Overseas Activity," "Business—Natural Gas Business—Overseas Activity" and "Management's Discussion and Analysis of Financial Condition and Results of Operations—Acquisitions and Overseas Activities." These interests are subject to certain operating risks in their respective regions, including economic and political risks. Although these properties historically have not experienced problems from civil unrest or regulatory disputes, the political and economic environment in these regions could impact the financial position, results of operations and prospects of these properties.

Our Indonesian interests are subject to the laws and regulations of Indonesia, including those relating to the development, production, marketing, pricing, transportation and storage of natural gas and crude oil, taxation and environmental and safety matters. In addition, the operations are subject to production sharing arrangements with Pertamina, the Indonesian state-owned oil and gas company, which is currently the sole entity authorized to manage Indonesia's petroleum resources on behalf of the Indonesian government. Our Indonesian interests may be adversely affected by changes in governmental policies or social instability or other political, economic or diplomatic developments in or affecting Indonesia which are not within our control including, among other things, a change in crude oil or natural gas pricing policy, the risks of war and terrorism, expropriation, nationalization, renegotiation or nullification of existing concessions and contracts, taxation policies, foreign exchange and repatriation restrictions, changing political conditions, Rupiah/U.S. dollar exchange rate fluctuations and currency controls. If we successfully acquire the interests in Australia's North West Shelf Project, we could face similar risks in Australia.

The Tangguh LNG Project is a greenfield project and may not be successful.

In January 2003, we paid approximately US$275 million to acquire the equivalent of a 12.5% equity interest in the Tangguh LNG Project in Indonesia. The Tangguh LNG Project is a greenfield project with a limited operational track record, and is subject to risks associated with attaining government approvals, delays in the development of LNG facilities required to process gas, and lower than expected demand for gas reserves from this project. Although the partners in the Tangguh LNG Project have entered into a 25-year supply contract beginning in 2007 to provide up to 2.6 million tons of liquefied natural gas per annum to a liquefied natural gas terminal being developed by CNOOC, our controlling shareholder, in Fujian Province, China, this single contract may not be sufficient to make the project commercially viable. We cannot assure you that the parties to the project will be able to secure sufficient contracts to make the project commercially viable. For further details of our investment in the Tangguh LNG Project, see "Business—Natural Gas Business—Overseas Activity."

We may not be able to obtain external financing that is acceptable to us for business development purposes.

From time to time, we must secure external debt and equity financing to implement our development plans and fund our other business requirements.

Our ability to obtain external financing is subject to various uncertainties, including:

- our results of operations, financial condition and cash flows;
- the amount of capital that other PRC and Hong Kong entities may seek to raise in the international capital markets;
- economic, political and other conditions in the PRC and Hong Kong;
- the PRC government's policies relating to foreign currency borrowings; and
- conditions in the PRC, Hong Kong and international capital markets.

If we are unable to obtain sufficient funding for our operations or development plans, our business, revenues, net income and cash flows could be adversely affected. For additional information on our capital expenditure plans and financing requirements, see "Management's Discussion and Analysis of Financial Condition and Results of Operations—Liquidity and Capital Resources."

Once we issue debt securities or otherwise incur indebtedness, we become subject to risks that impact the underlying principal of such indebtedness. While all our current debt securities are rated investment grade by rating agencies, we cannot assure you that such ratings will not change due to internal or external factors. These factors may be beyond our control. Even if there is no default or event of default on our part, a market perception of an increased likelihood of a default may have a material adverse effect on our outstanding indebtedness as well as to our business operations.

You may not be able to assert claims against Arthur Andersen, our independent public accountants for periods prior to December 31, 2001, nor may you be able to assert claims against our current independent public accountants for financial statements previously audited by Arthur Andersen.

On June 6, 2002, we terminated the engagement of Arthur Andersen & Co as our independent public accountants. Prior to that date, Arthur Andersen had audited our financial statements, including the financial statements for the two year period ended December 31, 2001 included elsewhere in this offering memorandum. Our selected historical financial data for the years ended, and as of, December 31, 1998 and 1999 set forth in "Selected Historical Consolidated Financial and Operating Data" were also based on financial statements audited by Arthur Andersen. On June 15, 2002, Arthur Andersen was convicted of federal obstruction of justice charges in connection with the U.S. government's investigation of Enron Corporation. On August 31, 2002, Arthur Andersen voluntarily relinquished its licenses to practice public accountancy in all states of the United States, thereby effectively ceasing to exist as a global accounting firm. Accordingly, it may be difficult or impossible for you to assert any claims against, or recover any damages from, Arthur Andersen, in respect of this offering memorandum, including in respect of the financial statements previously audited by Arthur Andersen that are included elsewhere in this offering memorandum. Moreover, our current independent public accountants, Ernst & Young, have not reaudited the financial statements previously audited by Arthur Andersen. Therefore, it is highly unlikely that you will be able to assert claims against, or recover any damages from, Ernst & Young, in respect of the financial statements that were previously audited by Arthur Andersen and included elsewhere in this offering memorandum.

Risks relating to the PRC petroleum industry

A change in PRC petroleum industry regulations could have an adverse affect on our operations.

The PRC government exercises control over the PRC petroleum industry, including with respect to licensing, exploration, production, distribution, pricing, exports and allocation of various resources. Recently, the PRC government underwent substantial reform. As of the date of this offering memorandum, we cannot assure you that the legal regime affecting our businesses will remain substantially unchanged. Since the reorganization, the Ministry of Commerce has become the primary coordinator for the petroleum industry and, together with other relevant governmental agencies, provides regulatory supervision over the petroleum industry. Prior to March 2003, the State Economic and Trade Commission had been the prime coordinator for the petroleum industry.

In the past, we have benefited from various favorable PRC government policies, laws and regulations that were enacted to encourage the development of the offshore petroleum industry. See "The PRC Petroleum Industry—Regulatory Framework—Special Policies Applicable to the Offshore Petroleum Industry in China." However, there can be no assurance that the PRC government will continue existing policies or that it will not adopt new policies, laws or regulations.

In addition, existing PRC regulations require us to apply for and obtain various PRC government licenses and other approvals, including in some cases approvals for amendments and extensions of existing licenses and approvals, to conduct exploration and development activities offshore China. If we are unable to obtain any necessary approvals, our reserves and production would be adversely affected. For further information on regulations affecting the PRC petroleum industry, see "The PRC Petroleum Industry."

Certain restrictions on foreign companies will be lifted as a result of China's entry into the World Trade Organization and may adversely affect our business.

Effective December 11, 2001, the PRC became a member of the World Trade Organization, or WTO. China's WTO commitments require it, within five years from the date of China's accession to the WTO, to lift restrictions that prohibit foreign companies from directly selling crude and processed oil in China. The sale of natural and liquefied petroleum gas is not specifically dealt with under China's market-access commitments relating to distribution services (as is the case with crude and processed oil). Accordingly, foreign participation in the sale of such products may be permitted within one year of accession in the form of minority-owned joint ventures and, within two years of accession, through wholly owned subsidiaries without any equity restrictions.

We may be harmed if we fail to comply with existing or future environmental laws and regulations.

Our business is subject to PRC environmental protection laws and regulations which:

- impose fees for the discharge of waste substances;
- require the payment of fines and damages for serious environmental pollution; and
- provide that the government may, at its discretion, close or suspend any facility which fails to comply with orders requiring it to cease or cure operations causing environmental damage.

We believe that all of our facilities and operations are in material compliance with the requirements of the relevant environmental protection laws and regulations. However, amendment of existing laws or regulations may impose additional or more stringent requirements. In addition, our compliance with such laws or regulations may require us to incur significant capital expenditures or other obligations or liabilities, which could create a substantial financial burden on us. For a further discussion of the environmental regulations in the PRC, see "Business—Environmental Regulation."

Risks relating to the PRC

PRC economic and political conditions may adversely affect our operations.

Most of our businesses, assets and operations are located in the PRC. The economic system of the PRC differs from the economies of most developed countries in many respects, including:

- government investment;
- level of development;
- control of capital investment;
- control of foreign exchange; and
- allocation of resources.

The economy of the PRC has been undergoing a transformation from a planned economy to a market-oriented economy. In recent years the PRC government has implemented economic reform measures emphasizing decentralization, utilization of market forces in the development of the PRC economy and a higher level of management autonomy. These economic reform measures have and will continue to subject our businesses to some uncertainty. In the future, our operating results could be adversely affected by changes to the laws and regulations that govern our industry and changes in the PRC political and economic systems.

The PRC economy has experienced significant growth in the past 20 years, but the growth has been uneven both geographically and among various sectors of the economy. Economic growth has also been accompanied by periods of high inflation. The PRC government has implemented various policies from time to time to restrain the rate of such economic growth, control inflation and otherwise regulate economic expansion. In addition, the PRC government has attempted to control inflation by controlling the prices of basic commodities. Severe measures or other actions by the PRC government, such as placing additional controls on prices of petroleum and petroleum products, could restrict our business operations and adversely affect our financial position.

In March 2003, several countries, including China, experienced an outbreak of a new and highly contagious form of atypical pneumonia now known as "severe acute respiratory syndrome" or "SARS." The severity of the outbreak in certain municipalities, such as Beijing, and provinces, such as Guangdong Province, has affected general commercial activity. While the long-term impact of the SARS outbreak is unclear at this time, the prolonged existence of SARS could have a negative impact on the PRC economy and, in turn, have a material adverse effect on our results of operations.

Government control of currency conversion and future movements in exchange rates may adversely affect our operations and financial condition.

A portion of our Renminbi revenue may need to be converted into other currencies by our wholly owned principal operating subsidiary in the PRC to meet our foreign currency obligations. We have substantial requirements for foreign currency, including:

- debt service on foreign currency denominated debt;
- overseas acquisitions of oil and gas properties;
- purchases of imported equipment; and
- payment of dividends declared in respect of shares held by international investors.

Our wholly owned subsidiary in the PRC may undertake current account foreign exchange transactions without prior approval from the State Administration for Foreign Exchange. It has access to current account foreign exchange so long as it can produce commercial documents evidencing such transactions and provided that they are processed through certain banks in China. Foreign exchange transactions under the capital account, including principal payments with respect to foreign currency denominated obligations, will be subject to the registration requirements of the State Administration for Foreign Exchange.

Since 1994, the conversion of Renminbi into Hong Kong and United States dollars has been based on rates set by the People's Bank of China, which are set daily based on the previous day's PRC interbank foreign exchange market rate and current exchange rates on the world financial markets. The PRC government has stated publicly that it intends to make Renminbi freely convertible in the future. However, we cannot predict when the PRC government will allow free conversion of Renminbi into foreign currencies. Renminbi devaluation and fluctuations in exchange rates may adversely affect the value, translated or converted into U.S. dollars or H.K. dollars, of our net assets, earnings and any declared dividends. Renminbi devaluation and exchange rate fluctuations may adversely affect our results of operations and financial condition and may result in foreign exchange losses because of our substantial U.S. dollar and Japanese yen-denominated debts, expenses and other requirements. In addition, we may not be able to increase the Renminbi prices of our domestic sales to offset fully any depreciation of the Renminbi due to political, competitive or social pressures.

We do not hedge exchange rate fluctuations between the Renminbi and foreign currencies and currently have no plans to do so. For further information on foreign exchange risks, foreign exchange rates and hedging activities, see "Exchange Rate Information" and "Management's Discussion and Analysis of Financial Condition and Results of Operations—Market Risks."

The interpretation and enforcement of PRC laws and regulations is subject to some uncertainty.

The PRC legal system is based on statutory law. Under this system, prior court decisions may be cited as persuasive authority but are not binding. Since 1979, the PRC government has been developing a comprehensive system of commercial laws and considerable progress has been made in the promulgation of laws and regulations dealing with economic matters, such as corporate organization and governance, foreign investments, commerce, taxation and trade. In particular, the regulatory framework for the securities industry in China is at an early stage of development. The China Securities Regulatory Commission, or CSRC, is responsible for administering and regulating the national securities markets and drafting regulations for the regulation of the national securities markets. Regulations of the State Council and the relevant implementing measures of CSRC, such as provisions dealing with acquisitions of listed PRC companies and disclosure of information, apply to listed companies in general without being confined to companies listed on any particular stock exchange. Hence these provisions apply to our company. Because these laws, regulations and legal requirements are relatively new, and because of the limited volume of published cases and judicial interpretations and the non-binding nature of prior court decisions, the interpretation and enforcement of these laws, regulations and legal requirements involve some uncertainty.

The PRC government recently underwent substantial reforms after the National People's Congress meeting in March 2003. The PRC government has reiterated its policy of furthering reforms in the socialist market economy. No assurance can be given that these changes will not have an adverse effect on business conditions in China generally or on our business in particular.

Risks relating to the notes

Payments of the notes are structurally subordinated to the liabilities and obligations of our subsidiaries.

We own the entire issued share capital of the issuer and intend for it to serve primarily as a finance subsidiary. The guarantees are solely our obligation. We, as guarantor of the notes, are primarily a holding company and our ability to make payments to the issuer or pursuant to the guarantees in respect of the notes depends largely upon the receipt of dividends, distributions, interest or advances from our subsidiaries. The ability of our subsidiaries to pay dividends may be subject to applicable laws. Payments on the notes are structurally subordinated to all existing and future liabilities and obligations of each of our subsidiaries (other than the issuer) and these subsidiaries had an aggregate of US$641 million of debt outstanding as of December 31, 2002. Claims of creditors of such companies will have priority as to their assets over us and our creditors, including holders of the notes seeking to enforce the guarantees. The indentures pursuant to which the notes will be issued do not contain any restrictions on the ability of the issuer, us or our subsidiaries to incur additional indebtedness.

The notes have limited liquidity.

No public market currently exists for the notes. An application has been made to list the notes only on the Luxembourg Stock Exchange. The initial purchasers intend, but are under no obligation, to make a market in the notes and no assurance can be given as to whether a trading market for the notes will develop or as to the liquidity of any such trading market. If any of the notes are traded after the initial issue, they may trade at a discount or premium from their initial offering price, depending on prevailing interest rates, the market for similar securities and other factors, including general economic conditions and our financial condition, performance and prospects. Neither we nor the initial purchasers can provide any assurance as to the future price level of the notes after their initial issue.

USE OF PROCEEDS

The aggregate proceeds of approximately US$486 million from the sale of the notes will be advanced, after deducting offering related expenses, by the issuer to us. We plan to use these proceeds for general corporate purposes. For a discussion of our capital expenditures program for the next two years, see "Management's Discussion and Analysis of Financial Condition and Results of Operations—Liquidity and Capital Resources—Capital Expenditures and Investments." Pending such uses, the net proceeds will be invested in interest bearing, U.S. dollar-denominated short-term deposits or short-term U.S. government bonds.

EXCHANGE RATE INFORMATION

China

The People's Bank of China sets and publishes daily a base exchange rate with reference primarily to the supply and demand of Renminbi against the U.S. dollar in the market during the prior day. The People's Bank of China also takes into account other factors such as the general conditions existing in the international foreign exchange markets. Although Chinese governmental policies were introduced in 1996 to reduce restrictions on the convertibility of Renminbi into foreign currency for current account items, conversion of Renminbi into foreign currency for capital items, such as foreign direct investment, loans or security, requires the approval of the State Administration for Foreign Exchange.

The following table sets forth the noon buying rate for U.S. dollars in New York City for cable transfers in Renminbi as certified for customs purposes by the Federal Reserve Bank of New York for the periods indicated:

	Noon buying rate			
Period	**Period end**	**Average(1)**	**High**	**Low**
	(Rmb per US$1.00)			
1998	8.3008	8.2991	8.3100	8.2778
1999	8.2795	8.2785	8.2800	8.2770
2000	8.2774	8.2784	8.2799	8.2768
2001	8.2766	8.2772	8.2786	8.2676
2002	8.2800	8.2772	8.2800	8.2669
2003 (through May 14, 2003)	8.2769	8.2774	8.2800	8.2766

(1) Determined by averaging the rates on the last business day of each month during the relevant period, except for 2003, which is determined by averaging the daily rates from January 2, 2003 through May 14, 2003.

For a recent noon buying rate for U.S. dollars in New York City for cable transfers in Renminbi as certified for customs purposes by the Federal Reserve Bank of New York, see "Currency of Presentation and Certain Definitions."

Hong Kong

The H.K. dollar is freely convertible into the U.S. dollar. Since 1983, the H.K. dollar has been linked to the U.S. dollar at the rate of HK$7.80 to US$1.00. Under existing Hong Kong law, (i) there are no foreign exchange controls or other laws, decrees or regulations that affect the remittance of interest or other payments on the notes offered hereby to U.S. residents and (ii) there are no limitations on the rights of nonresidents or foreign owners to hold the notes offered hereby. The Basic Law of the Hong Kong Special Administrative Region of the People's Republic of China, which came into effect on July 1, 1997, provides that no foreign exchange control policies shall be applied in Hong Kong.

The market exchange rate of the H.K. dollar against the U.S. dollar continues to be determined by the forces of supply and demand in the foreign exchange market. However, against the background of the fixed rate system which applies to the issuance and withdrawal of Hong Kong currency in circulation, the market exchange rate has not deviated significantly from the level of HK$7.80 to US$1.00. The Hong Kong government has indicated its intention to maintain the link at that rate. Under the Basic Law, the H.K. dollar will continue to circulate and remain freely convertible. The Hong Kong government has also stated that it has no intention of imposing exchange controls in Hong Kong and that the H.K. dollar will remain freely convertible into other currencies, including the U.S. dollar. However, no assurance can be given that the Hong Kong government will maintain the link at HK$7.80 to US$1.00 or at all.

The following table sets forth the noon buying rate for U.S. dollars in New York City for cable transfers in H.K. dollars as certified for customs purposes by the Federal Reserve Bank of New York for the periods indicated:

	Noon buying rate			
Period	**Period end**	**Average(1)**	**High**	**Low**
	(HK$ per US$1.00)			
1998	7.7476	7.7465	7.7595	7.7355
1999	7.7740	7.7599	7.7814	7.7457
2000	7.7999	7.7936	7.8008	7.7765
2001	7.7980	7.7996	7.8004	7.7970
2002	7.7988	7.7996	7.8095	7.7970
2003 (through May 14, 2003)	7.7988	7.7994	7.8001	7.7987

(1) Determined by averaging the rates on the last business day of each month during the relevant period, except for 2003, which is determined by averaging the daily rates from January 2, 2003 through May 14, 2003.

For a recent noon buying rate for U.S. dollars in New York City for cable transfers in H.K. dollars as certified for customs purposes by the Federal Reserve Bank of New York, see "Currency of Presentation and Certain Definitions."

CAPITALIZATION

The following table sets forth our short-term debt and capitalization under Hong Kong GAAP as of December 31, 2002. Our capitalization is presented:

- on an actual basis, and
- as adjusted to reflect the issuance of the notes.

This table should be read in conjunction with our consolidated financial statements beginning on page F-1. For further information about our short-term debt and capitalization, see "Use of Proceeds" and "Management's Discussion and Analysis of Financial Condition and Results of Operations—Liquidity and Capital Resources—Financing Activities."

	As of December 31, 2002			
	Actual		As adjusted	
	Rmb	US$	Rmb	US$
	(in millions)			
Cash and cash equivalents(1)(2)	7,839	947	11,865	1,433
Time deposits with maturities of over three months	4,690	566	4,690	566
Short-term investments	6,531	789	6,531	789
Current portion of long-term bank loans	298	36	298	36
Long-term bank loans, net of current portion	941	114	941	114
US$500 million in 6.375% long-term guaranteed notes due 2012(3)	4,071	492	4,071	492
Notes offered hereby	—	—	4,140	500
Shareholders' equity:				
Ordinary shares, par value HK$0.10 per ordinary share:				
Paid-in capital issued and outstanding	877	106	877	106
Share premium	20,761	2,508	20,761	2,508
Revaluation reserves	275	33	275	33
Cumulative translation reserves	(14)	(2)	(14)	(2)
Statutory reserves	2,232	270	2,232	270
Retained earnings	16,437	1,985	16,437	1,985
Total shareholders' equity	40,568	4,900	40,568	4,900
Total capitalization(4)	45,580	5,505	49,720	6,005

(1) Cash and cash equivalents, as adjusted, include the proceeds of the notes offered hereby, before deducting expenses relating to the offering.

(2) On January 1, 2003, we acquired interests in the Tangguh LNG Project in Indonesia for an aggregate consideration of approximately US$275 million. The expenditures associated with this acquisition are not accounted for in this presentation.

(3) On March 8, 2002, we, through CNOOC Finance (2002) Limited, a wholly owned finance subsidiary, issued US$500,000,000 in 6.375% guaranteed notes due 2012. The obligations in respect of these notes are unconditionally and irrevocably guaranteed by us.

(4) Excludes current portion of long-term debt.

Except as disclosed or contemplated in this offering memorandum, there has been no material adverse change in our consolidated indebtedness or capitalization since December 31, 2002.

SELECTED HISTORICAL CONSOLIDATED FINANCIAL AND OPERATING DATA

The following tables present our selected historical consolidated financial data as of and for each of the years in the five-year period ended December 31, 2002.

The selected income statement data and cash flow data for the year ended December 31, 2002 and the selected balance sheet data as of December 31, 2002 have been derived from our consolidated financial statements audited by Ernst & Young, our current independent public accountants. The selected income statement data and cash flow data for the years ended December 31, 2000 and 2001 and the selected balance sheet data as of December 31, 2000 and 2001 have been derived from our consolidated financial statements audited by Arthur Andersen & Co, our independent public accountants prior to 2002. The selected income statement data and cash flow data for the years ended December 31, 1998 and 1999 and the selected balance sheet data as of December 31, 1998 and 1999 are derived from our consolidated financial statements audited by Arthur Andersen & Co, which are not included in this offering memorandum. This financial information reflects the October 1999 reorganization and has been prepared as if our current structure had been in existence at the beginning of the relevant periods. The financial information included herein may not necessarily reflect our results of operations, financial position and cash flows in the future or what they would have been had we been a separate, stand-alone entity during the periods presented. The selected financial data should be read in conjunction with our consolidated financial statements and "Management's Discussion and Analysis of Financial Condition and Results of Operations" included elsewhere in the offering memorandum. Our consolidated financial statements are prepared and presented in accordance with Hong Kong GAAP. For an explanation of the reconciliation of our net income and shareholders' equity to U.S. GAAP, see note 38 to our consolidated financial statements beginning on page F-1.

On June 6, 2002, Ernst & Young replaced Arthur Andersen & Co as our independent public accountants. For a discussion on such change of accountants, see "Risk Factors—Risks relating to our business—You may not be able to assert claims against Arthur Andersen, our independent public accountants for periods prior to December 31, 2001, nor may you be able to assert claims against our current independent public accountants for financial statements previously audited by Arthur Andersen" and "Management's Discussion and Analysis of Financial Condition and Results of Operations—Change of Accountants."

Selected Historical Consolidated Financial Data

	Year ended December 31,					
	1998	1999	2000	2001	2002	2002
	Rmb	Rmb	Rmb	Rmb	Rmb	US$
			(in millions)			
Income Statement Data:						
Hong Kong GAAP						
Operating revenues:						
Oil and gas sales	7,814	11,398	18,819	17,561	23,779	2,872
Marketing revenues	1,488	3,805	5,126	2,537	2,377	287
Other income	10	108	279	722	217	26
Total operating revenues	9,312	15,311	24,224	20,820	26,374	3,185
Expenses:						
Operating expenses	(1,954)	(1,855)	(2,124)	(2,329)	(3,775)	(456)
Production taxes	(383)	(579)	(1,037)	(884)	(1,023)	(124)
Exploration expenses	(584)	(247)	(553)	(1,039)	(1,318)	(159)
Depreciation, depletion and amortization	(1,954)	(2,373)	(2,578)	(2,567)	(4,020)	(486)
Dismantlement	(188)	(177)	(104)	(90)	(126)	(15)
Crude oil and product purchases	(1,432)	(3,737)	(5,098)	(2,453)	(2,326)	(281)
Selling and administrative expenses	(650)	(517)	(456)	(616)	(1,007)	(122)
Other	(109)	(5)	(217)	(618)	(31)	(4)
	(7,254)	(9,490)	(12,167)	(10,596)	(13,626)	(1,647)
Interest income	117	54	237	318	148	18
Interest expenses	(608)	(622)	(475)	(117)	(295)	(36)
Exchange gain (loss), net	(303)	(432)	381	235	(114)	(14)
Investment income	—	—	—	221	193	23
Share of profit of an associate	—	13	218	90	165	20
Non-operating profit (loss), net	580	(1)	(195)	35	(71)	(9)
Income before tax	1,844	4,833	12,223	11,006	12,774	1,540
Tax	(295)	(722)	(1,926)	(3,048)	(3,541)	(428)
Net income	1,549	4,111	10,297	7,958	9,233	1,112
U.S. GAAP						
Operating revenues:						
Oil and gas sales	7,814	11,398	18,819	17,561	23,779	2,872
Marketing revenues	1,488	3,805	5,126	2,537	2,377	287
Other income	10	108	279	722	217	26
Total operating revenues	9,312	15,311	24,224	20,820	26,374	3,185
Net Income	1,549	4,113	10,302	7,920	9,088	1,098

	As of December 31,					
	1998	1999	2000	2001	2002	2002
	Rmb	Rmb	Rmb	Rmb	Rmb	US$
			(in millions)			
Balance Sheet Data:						
Hong Kong GAAP						
Cash and cash equivalents	426	879	2,797	6,394	7,839	947
Time deposits with maturities over three months	—	—	3,425	2,050	4,690	566
Short-term investments	—	—	300	8,896	6,531	789
Current assets	2,102	4,987	9,472	20,030	24,487	2,957
Property, plant and equipment, net	18,963	20,907	22,654	23,828	36,072	4,357
Investment in an associate	260	274	471	462	537	65
Total assets	21,325	26,168	32,597	44,320	61,096	7,378
Current liabilities	2,813	9,177	8,768	4,392	7,134	862
Long-term bank loans, net of current portion	8,333	6,033	4,749	3,256	941	114
US$500 million in 6.375% long-term guaranteed notes due 2012	—	—	—	—	4,071	492
Total long-term liabilities	12,153	8,607	7,707	6,617	13,393	1,618
Total liabilities	14,966	17,784	16,475	11,009	20,527	2,479
Shareholders' equity	6,359	8,384	16,122	33,311	40,568	4,900
U.S. GAAP						
Total assets	21,325	26,000	32,330	44,062	59,984	7,244
Total long-term liabilities	12,153	7,562	7,707	6,617	13,393	1,618
Shareholders' equity	6,359	9,261	15,855	33,053	39,884	4,817

	Year ended December 31,					
	1998	1999	2000	2001	2002	2002
	Rmb	Rmb	Rmb	Rmb	Rmb	US$
	(in millions, except percentages and ratios)					
Other Financial Data:						
Hong Kong GAAP						
Capital expenditures paid	3,576	4,070	4,404	4,343	6,833	825
Cash provided by (used for):(1)						
Operating activities	3,942	7,323	13,233	11,759	14,597	1,763
Investing activities	(2,952)	(4,442)	(7,861)	(11,366)	(11,724)	(1,416)
Financing activities	(895)	(2,428)	(3,454)	3,204	(1,428)	(172)
EBITDE(2)	5,364	8,630	15,315	14,366	18,499	2,235
EBITDE margin(3)	57.6%	56.4%	63.2%	69.0%	70.1%	70.1%
Ratio of EBITDE to gross interest expense(4)	7.5x	12.3x	32.2x	45.5x	45.7x	45.7x
Ratio of total debt to EBITDE	1.9x	1.1x	0.4x	0.3x	0.3x	0.3x
Ratio of total debt to total capitalization(5)	68.3%	63.1%	27.5%	12.3%	11.6%	11.6%
U.S. GAAP						
Cash provided by (used for):						
Operating activities(6)	3,942	7,323	13,233	11,759	14,597	1,763
Investing activities	(2,952)	(4,442)	(7,861)	(11,366)	(11,724)	(1,416)
Financing activities	(895)	(2,428)	(3,454)	3,204	(1,428)	(172)
Ratio of cash provided by operating activities to gross interest expense(4)(7)	5.5x	10.5x	27.9x	37.2x	44.6x	44.6x
Ratio of total debt to cash provided by operating activities(6)	2.5x	1.2x	0.4x	0.4x	0.4x	0.4x
Net income(7)	1,549	4,113	10,302	7,920	9,088	1,098
Net income margin(6)(8)	16.6%	26.9%	42.5%	38.0%	34.5%	34.5%
Ratio of net income to gross interest expense(4)(7)	2.2x	5.9x	21.7x	25.1x	27.8x	27.8x
Ratio of total debt to net income(7)	6.5x	2.2x	0.6x	0.6x	0.6x	0.6x
EBITDE(2)	5,364	8,630	15,315	14,319	18,483	2,232
EBITDE margin(3)	57.6%	56.4%	63.2%	68.8%	70.1%	70.1%
Ratio of EBITDE to gross interest expense(4)	7.5x	12.3x	32.2x	45.4x	56.6x	56.6x
Ratio of total debt to EBITDE	1.9x	1.1x	0.4x	0.3x	0.3x	0.3x
Ratio of total debt to total capitalization(5)	68.3%	59.5%	27.9%	12.4%	11.8%	11.8%

(1) In accordance with a new accounting pronouncement, SSAP 15 "Cash Flow Statements," the presentation of cash flows for 1998, 1999, 2000 and 2001 conforms to the presentation of cash flows for 2002. For further information on HK SSAP 15, see "Management's Discussion and Analysis of Financial Condition and Results of Operations—Recent Accounting Pronouncements."

(2) We have defined EBITDE to mean earnings before interest income, interest expense, income taxes, depreciation, depletion, amortization, dismantlement, exploration expenses, impairment losses related to property, plant and equipment and exchange gains or losses as computed under Hong Kong and U.S. GAAP. EBITDE is not a standard measure under either Hong Kong or U.S. GAAP. You should not consider our definition of EBITDE in isolation or construe it as an alternative to net income, cash provided by operating activities or any other measure of performance or as an indicator of operating performance, liquidity or any other standard measure under either Hong Kong or U.S. GAAP. We believe net income and cash provided by operating activities are the most directly comparable financial measures for EBITDE as an indicator of our operating performance and liquidity, respectively. For our management's explanation of how we define EBITDE and why we use it, see "Management's Discussion and Analysis of Financial Condition and Results of Operations—Overview—Non-GAAP Financial Measures."

(3) EBITDE margin represents EBITDE as a percentage of our total operating revenues, as computed under both Hong Kong and U.S. GAAP. EBITDE margin is used as an indicator of operating performance.

(4) Gross interest expense includes capitalized interest.

(5) Total capitalization excludes current portion of long-term debt.

(6) We have included data relating to cash provided by operating activities in this table because we believe it is the most directly comparable Hong Kong and U.S. GAAP measure to EBITDE as an indicator of liquidity. EBITDE is not a standard measure under either Hong Kong or U.S. GAAP.

(7) We have included net income data in this table because we believe it is the most directly comparable Hong Kong and U.S. GAAP measure to EBITDE as an indicator of operating performance. EBITDE is not a standard measure under either Hong Kong or U.S. GAAP.

(8) Net income margin represents net income as a percentage of our total operating revenues, as computed under U.S. GAAP.

Selected Operating and Reserves Data

The following table sets forth our operating data and our net proved reserves as of and for the periods indicated.

	Year ended December 31,		
	2000	2001	2002
Net Production:			
Oil (daily average bbls/day)	206,347	228,873	298,625
Gas (daily average mmcf/day)	197.9	195.0	272.6
Oil equivalent (BOE/day)	239,335	261,379	346,639
Average net realized prices:			
Oil (per bbl)	US$28.21	US$23.34	US$24.35
Gas (per mcf)	3.09	3.08	2.98
Offshore China lifting costs (per BOE)(1)	4.45	4.16	3.92
Overseas lifting costs (per BOE)(1)(2)	—	—	9.06
Three-year average finding and development costs (per BOE)(3)	US$2.77	US$4.86	US$4.59
Adjusted three-year average finding and development costs (per BOE)(4)	US$3.82	US$4.15	US$4.54
Net Proved Reserves (end of period):			
Oil (mmbbls)	1,215.8	1,245.9	1,424.4
Gas (bcf)	3,249.7	3,247.6	3,547.9
Total (million BOE)	1,757.4	1,787.1	2,015.8
Proved developed reserves (million BOE)	638.6	710.0	794.3
Annual reserves replacement ratio	104%	131%	281%
Estimated reserves life (years)	20.1	18.7	15.9
Present value of estimated future net revenues before income taxes (discounted at 10%) (million Rmb)	108,423	69,860	140,798
Standardized measure of discounted future net cash flows (million Rmb)	93,391	51,082	100,141

(1) Includes operating expenses and production taxes. During the years ended December 31, 2000 and 2001, our overseas operations were not material and our overseas lifting costs were included in our offshore China lifting costs for those years.

(2) Overseas lifting costs reflect lifting costs associated with our operations in Indonesia and are calculated using the net entitlement method.

(3) The three-year average finding and development costs for each of 2000, 2001 and 2002 are calculated by taking the sum of total costs incurred for exploration and development of oil and gas fields in immediately preceding three-year period and dividing it by the sum of the reserve additions, extensions and revisions for the same three years.

(4) Because a high percentage of our net proved reserves are classified as proved undeveloped, we also presented the adjusted three-year average finding and development cost to reflect the estimated future costs of developing these proved undeveloped reserves as of December 31, 2000, 2001 and 2002, as estimated by Ryder Scott Company. The actual future costs of developing these reserves may differ from these estimates. See the definition of "adjusted finding and development cost per BOE" in "Certain Oil and Gas Terms."

At our request, Ryder Scott Company, independent petroleum engineering consultants, carried out an independent evaluation of the reserves of selected properties as of December 31, 2000, 2001 and 2002. We have obtained a summary report from Ryder Scott Company describing its procedures and conclusions as of December 31, 2002, and their summary report appears as Appendix A to this offering memorandum. For further information regarding our reserves, see "Risk Factors—Risks relating to our business—The oil and gas reserve estimates in this offering memorandum may require substantial revision as a result of future drilling, testing and production," and "Business—Oil and Natural Gas Reserves."

The following table sets forth summary information with respect to our estimated net proved reserves of crude oil and natural gas as at the dates indicated.

	Net proved reserves at December 31,		Net proved reserves at December 31, 2002		
	2000	2001	Developed	Undeveloped	Total
Bohai Bay:					
Crude oil (mmbbls)	923.9	961.3	381.1	611.4	992.5
Natural gas (bcf)	591.4	629.1	182.1	416.5	598.6
Total (million BOE):	1,022.4	1,066.2	411.4	680.9	1,092.3
Independent (million BOE)	774.2	689.7	326.8	268.3	595.1
Production sharing contracts (million BOE)	248.2	376.5	84.6	412.6	497.2
Western South China Sea:					
Crude oil (mmbbls)	141.1	131.6	99.0	61.4	160.4
Natural gas (bcf)	2,593.0	2,421.5	499.6	2,011.6	2,511.2
Total (million BOE):	573.3	535.1	182.3	396.6	578.9
Independent (million BOE)	372.0	373.3	50.9	383.3	434.2
Production sharing contracts (million BOE)	201.3	161.8	131.4	13.3	144.7
Eastern South China Sea:					
Crude oil (mmbbls)	136.8	132.2	58.9	61.4	120.3
Natural gas (bcf)	—	—	—	42.8	42.8
Total (million BOE):	136.8	132.2	58.9	68.6	127.5
Independent (million BOE)	—	—	—	—	—
Production sharing contracts (million BOE)	136.8	132.2	58.9	68.6	127.5
East China Sea:					
Crude oil (mmbbls)	4.5	12.4	2.9	9.6	12.5
Natural gas (bcf)	65.3	197.0	42.1	137.3	179.4
Total (million BOE):	15.4	45.2	9.9	32.5	42.4
Independent (million BOE)	15.4	45.2	9.9	32.5	42.4
Production sharing contracts (million BOE)	—	—	—	—	—
Overseas:					
Crude oil (mmbbls)	9.5	8.4	114.8	23.9	138.7
Natural gas (bcf)	—	—	101.5	114.4	215.9
Total (million BOE):	9.5	8.4	131.8	42.9	174.7
Independent (million BOE)	—	—	—	—	—
Production sharing contracts (million BOE)	9.5	8.4	131.8	42.9	174.7
Total:					
Total crude oil (mmbbls)	1,215.8	1,245.9	656.7	767.7	1,424.4
Total natural gas (bcf)	3,249.7	3,247.6	825.2	2,722.7	3,547.9
Total (million BOE):	1,757.4	1,787.1	794.3	1,221.5	2,015.8
Independent (million BOE)	1,161.6	1,108.2	387.6	684.1	1,071.7
Production sharing contracts (million BOE)	595.8	678.9	406.7	537.4	944.1

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion and analysis should be read in conjunction with our consolidated financial statements, selected historical consolidated financial data and operating and reserves data, in each case together with the accompanying notes, contained in this offering memorandum. Our consolidated financial statements have been prepared in accordance with Hong Kong GAAP, which differ in certain material respects from U.S. GAAP. Note 38 to our consolidated financial statements beginning on page F-1 provides an explanation of the reconciliation to U.S. GAAP of our net income and shareholders' equity. Certain statements set forth below constitute "forward-looking statements" within the meaning of the Reform Act. See "Special Note Regarding Forward-Looking Statements." On June 6, 2002, we terminated our engagement with Arthur Andersen & Co, our independent public accountants prior to such date. For a discussion of the change of accountants, see "—Change of Accountants" and "Risk Factors—Risks relating to our business—You may not be able to assert claims against Arthur Andersen, our independent public accountants for periods prior to December 31, 2001, nor may you be able to assert claims against our current independent public accountants for financial statements previously audited by Arthur Andersen."

Overview

We are an oil and gas company engaged in the exploration, development, production and sale of crude oil and natural gas primarily offshore China. We are the dominant producer of crude oil and natural gas offshore China and the only company permitted to conduct exploration and production activities with international oil and gas companies offshore China. As of December 31, 2002, we had estimated net proved reserves of 2,015.8 million BOE, comprised of 1,424.4 million barrels of crude oil and condensate and 3,547.9 billion cubic feet of natural gas. For the year 2002, our net production averaged 298,625 barrels per day of crude oil, condensate and natural gas liquids and 272.6 million cubic feet per day of natural gas, which together totaled 346,639 BOE per day.

Our revenues and profitability are largely determined by our production volume and the prices we charge for our crude oil and natural gas, as well as the costs of our exploration and development activities. Although crude oil prices depend on various market factors and have been volatile historically, our production volume has increased steadily over the past few years.

The following table sets forth our net production of crude oil, condensate and natural gas liquids and net income for the periods indicated.

	Year ended December 31,			
	1999	2000	2001	2002
Net production of crude oil, condensate and natural gas liquids (BOE/day)	174,745	206,347	228,874	298,625
Net production of natural gas (mmcf/day)	204.4	197.9	195.0	272.6
Net income (Rmb in millions)	4,111.1	10,296.6	7,957.6	9,232.8

Most of our crude oil production is sold in the PRC domestic market to customers affiliated with Sinopec or PetroChina. Most of our natural gas production is sold to Castle Peak Power Company Limited under a long-term take-or-pay contract.

For a further description of these factors and certain other factors affecting our financial performance, see "Risk Factors."

Relationship with CNOOC

Prior to the October 1999 reorganization of CNOOC, we did not exist as a separate legal entity and our business and operations were conducted by CNOOC and its various affiliates. In connection with the reorganization, CNOOC's oil and gas exploration, development, production and sales business and operations conducted both inside and outside China were transferred to us. See "Relationship with CNOOC and Certain Related Party Transactions" and note 27 to our consolidated financial statements beginning on page F-1.

Before the reorganization, certain PRC subsidiaries of CNOOC provided various materials, utilities and ancillary services for CNOOC's exploration and production activities. In connection with the reorganization, we entered into various new agreements under which we continued to use various services and properties provided by these CNOOC subsidiaries. These agreements include: (i) a materials, utilities and ancillary services supply agreement; (ii) technical service agreements; (iii) agreements for the sale of crude oil, condensate oil and liquefied petroleum gas; (iv) various lease agreements with other affiliates of CNOOC for office and residential premises used by us; and (v) a research and development services agreement with China Offshore Oil Research Center for the provision of general geophysical exploration services, comprehensive exploration research services, information technology services and seismic study. In 2002, CNOOC consolidated most of its oilfield services operations and established China Oilfield Services Limited. This CNOOC affiliate now provides most of the technical services to us.

For a description of the services provided under these agreements, see "Relationship with CNOOC and Certain Related Party Transactions."

Acquisitions and Overseas Activities

On January 1, 2003, we acquired BP Muturi Limited, which owns a 44.0% interest in the Muturi production sharing contract offshore Indonesia, and BP Wiriagar Limited's 42.4% interest in the Wiriagar production sharing contract offshore Indonesia for a total of approximately US$275 million. The Muturi production sharing contract and Wiriagar production sharing contract, together with the Berau production sharing contract, make up the Tangguh LNG Project. Our interests in these two production sharing contracts represent approximately 12.5% of the total reserves and upstream production of the Tangguh LNG Project. The remaining interests are held by BP Berau (34.2%), BP Muturi (0.2%), BP Wiriagar (2.7%), MI Berau (16.3%), Nippon (12.2%), BG (10.7%), KG Berau (8.6%), KG Wiriagar (1.4%) and Indonesia Natural Gas Resources Muturi (1.1%). The Tangguh LNG Project is a greenfield project located offshore Indonesia and represents one of the largest natural gas projects in Asia.

Before acquiring our interest in the Tangguh LNG Project, the partners in the Tangguh LNG Project entered into a conditional 25-year supply contract beginning in 2007 to provide up to 2.6 million tons of liquefied natural gas per year to a liquefied natural gas terminal project in Fujian Province, China.

On October 21, 2002, we entered into a key terms agreement to acquire an aggregate interest of approximately 5.56% in the reserves and upstream production of Australia's North West Shelf Gas Project for approximately US$365.6 million subject to certain adjustments. Under the terms of this agreement, we will purchase our interest from the six current partners to this project: BHP Billiton, BP, ChevronTexaco, Japan Australia LNG (MIMI), Shell and Woodside Energy. Our estimated share of reserves from this project would be approximately 1.2 trillion cubic feet of natural gas. Our share of natural gas together with associated liquids would be approximately 210 million BOE. Woodside Petroleum is the operator for the project.

Under the terms of this agreement, we would also acquire a 25% interest in the China LNG Joint Venture, which is being established by the six current partners to supply liquefied natural gas from the North West Shelf Gas Project to a liquefied natural gas terminal currently being developed by CNOOC, our controlling shareholder, and various partners in Guangdong Province, China. The terms of this transaction require us to pay the other partners in the North West Shelf Gas Project for gas production and processing services provided over the term of the China LNG Joint Venture. We expect to complete our acquisition of the interests in the North West Shelf Gas Project and China LNG Joint Venture in 2003. See "Business—Natural Gas Business—Overseas Activity."

On April 19, 2002, we completed the acquisition of Repsol YPF, S.A.'s interests in a portfolio of oil and gas production sharing and technical assistance contracts in contract areas located offshore and onshore Indonesia. The agreement took effect as of January 1, 2002. Under the terms of the acquisition, we paid a consideration of US$585 million, subject to a final oil price adjustment. See note 5 to our consolidated financial statements beginning on page F-1. The assets include a 65.3% interest in the South East Sumatra production sharing contract, a 36.7% interest in the Offshore North West Java production sharing contract, a direct 25.0% interest in the West Madura production sharing contract, a 50.0% interest in the Poleng technical assistance contract and a 16.7% interest in the Blora production sharing contract.

We completed our acquisition of the Repsol subsidiaries on April 19, 2002. For accounting purposes, the operations from these acquired subsidiaries are included in our consolidated financial statements from April 1, 2002. The profit accrued to us prior to April 1, 2002 has been treated as a purchase price reduction. See note 5 to our consolidated financial statements beginning on page F-1.

Further details of the Repsol acquisition are discussed under "Business—Principal Oil and Gas Regions—Overseas Activity."

Production Sharing Contracts Offshore China

We conduct a significant amount of our offshore China oil and gas activities through production sharing contracts with international oil and gas companies. Under these production sharing contracts, our foreign partners are required to bear all exploration costs during the exploration period. The parties to the contracts may recover exploration costs after commercial discoveries are made and production begins. The amount of exploration costs recoverable is derived from a production sharing formula set forth in each contract. Our production sharing contracts provide us with the option to take a participating interest in properties covered by the production sharing contracts which we may exercise after the foreign partners have made viable commercial discoveries. The foreign partners retain the remaining participating interests. We and the foreign partners fund our development and operating costs according to our respective participating interests. Based on a formula contained in the applicable contract, we are entitled to allocate specified amounts of the annual gross production of petroleum from those producing fields. See "Business—Production Sharing Contracts—Offshore China—Production Sharing Formula."

Before we exercise our option to take a 51% participating interest in a production sharing contract, we do not account for the exploration costs incurred, as these costs were incurred by our foreign partners. After we exercise the option to take a participating interest in a production sharing contract, we account for the oil and gas properties using the "proportional method" under which we recognize our share of development costs, revenues and expenses from such operations based on our participating interest in the production sharing contracts. See note 6 to our consolidated financial statements beginning on page F-1.

The foreign partners have the right to either take possession of their petroleum for sale in the international market or sell their petroleum to us for resale in the PRC market. See "Business—Production Sharing Contracts—Offshore China." For the years ended December 31, 2000, 2001 and 2002, the percentage of foreign partners' oil that was resold by us in the PRC market amounted to approximately 53%, 57% and 50%, respectively. The foreign partners sold the remaining portion of their oil in the international markets.

As described above, production of crude oil and natural gas is allocated among us, our foreign partners and the PRC government according to a formula contained in the production sharing contracts. We have excluded the government's share oil from net sales in our historical consolidated financial statements. Since our historical consolidated financial statements already exclude the government's share oil from our net sales figure, we do not expect any future share oil payments to affect our results of operations or operating cash flows differently than the effects reflected in our historical consolidated financial statement. For information regarding the historical amounts of government share oil payable to the government, see note 8 to our consolidated financial statements beginning on page F-1. For information regarding treatment of the PRC government's share oil, see "Business—Production Sharing Contracts—Offshore China—Production Sharing Formula."

We have one associated company, Shanghai Petroleum and Natural Gas Company Limited, which owns the Pinghu field. Our 30% equity interest in this company is accounted for using the equity method, under which our proportionate share of the net income or loss of Shanghai Petroleum and Natural Gas Company Limited is included in our consolidated statements of income as a share of income or loss of the associated company.

Our cost structures for production sharing contracts and for independent operations are different. The total expenses per unit of production under production sharing contracts are generally higher due to our foreign partners' use of expatriate staff, who generally command higher wages, as well as administrative and overhead costs that may be allocated by the operators, a higher percentage of capital expenditures and larger proportion of imported equipment.

Production from Independent Operations versus Production from Production Sharing Contracts

Historically we have cooperated with foreign partners under production sharing contracts, which have provided us with the expertise to undertake our independent operations more effectively. The percentage of our net production arising from independent operations offshore China was 51.6%, 58.4% and 53.9% for the years ended December 31, 2000, 2001 and 2002, respectively. Although we will continue to focus on independent operations, we plan to continue seeking appropriate opportunities to cooperate with foreign partners under production sharing contracts.

Provision for dismantlement

Prior to 2002, we estimate future dismantlement costs for our oil and gas properties and accrue the costs over the economic lives of the assets using the unit-of-production method. We estimate future dismantlement costs for oil and gas properties with reference to the estimates provided from either internal and external engineers after taking into consideration the anticipated method of dismantlement required in accordance with current legislation and industry practice. During the year, we changed the method of accounting for the provision for dismantlement in compliance with Hong Kong Statement of Standard Accounting Practice or HK SSAP 28, "Provisions, contingent liabilities and contingent assets." HK SSAP 28 requires the provision to be recorded for a present obligation whether that obligation is legal or constructive. The associated cost is capitalized and the liability is discounted and accretion expense is recognized using the credit adjusted risk-free rate in effect when the liability is initially recognized. The dismantlement costs for the years ended December 31, 2000, 2001 and 2002 was Rmb 103.6 million, Rmb 90.4 million and Rmb 126.1 million, respectively. The accrued liability is reflected in our consolidated balance sheet under "provision for dismantlement." See notes 3 and 28 to our consolidated financial statements beginning on page F-1.

Production Imbalance

We account for oil overlifts and underlifts using the entitlement method, under which we record overlifts as liabilities and underlifts as assets. An overlift occurs when we sell more than our percentage interest of oil from a property subject to a production sharing contract. An underlift occurs when we sell less than our participating interest of oil from a property under a production sharing contract. During the historical periods presented in our consolidated financial statements, we had no gas imbalances. We believe that production imbalance has not had a significant effect on our operations, liquidity or capital resources.

Allowances for Doubtful Accounts

We evaluate our accounts receivable by considering the financial condition of our customers, their past payment history and credit standing and other specific factors, including whether the accounts receivable in question are under dispute. We make provisions for accounts receivable when they are overdue for six months and we are concerned about our ability to collect them. For the years ended December 31, 2000, 2001 and 2002, allowances for doubtful accounts were not material in the context of total operating expenses and did not have a material effect on our results of operations or financial condition.

Non-GAAP Financial Measures

We use a financial measure that we define as EBITDE to provide additional information about our operating performance and our liquidity. EBITDE refers to our earnings before the following items:

- interest income and interest expense;
- income taxes;
- depreciation, depletion and amortization;
- dismantlement, exploration expenses and impairment losses related to property, plant and equipment; and
- exchange gains or losses.

EBITDE is not a standard measure under either U.S. or Hong Kong GAAP. However, we believe the investor community commonly uses this type of financial measure to assess the operating performance of oil and gas companies like us and the ability of such companies to service debt obligations and meet capital expenditure and working capital requirements.

As a measure of our operating performance, we believe that the most directly comparable U.S. and Hong Kong GAAP measure to EBITDE is net income. We operate in a capital intensive industry. We use EBITDE in addition to net income because net income includes many accounting items associated with capital expenditures, such as depreciation, exploration expenses and dismantlement costs. These accounting items may vary between companies depending on the method of accounting adopted by a company. For example, we use the successful efforts method of accounting whereby we capitalize successful exploration projects and expense unsuccessful efforts. Other companies may use the full cost method whereby they capitalize all of their exploration costs regardless of whether their exploration efforts prove successful. By minimizing differences in capital expenditures and the associated depreciation and exploration expenses as well as reported exploratory success rates, financial leverage and tax positions, EBITDE provides further information about our operating performance and an additional measure for comparing our operating performance with other companies' results.

The following table reconciles our net income under U.S. GAAP to our definition of EBITDE for the periods indicated.

	Year ended December 31,					
	1998	1999	2000	2001	2002	2002
	Rmb	Rmb	Rmb	Rmb	Rmb	US$
	(in millions)					
Net income	1,549	4,113	10,302	7,920	9,088	1,098
Tax	295	722	1,926	3,048	3,482	421
Interest and exchange gain/(loss), net	794	1,000	(143)	(436)	261	30
Depreciation, depletion and amortization	1,954	2,371	2,573	2,558	4,011	485
Dismantlement costs	188	177	104	90	323	39
Exploration expenses	584	247	553	1,039	1,318	159
Impairment losses related to property, plant and equipment	—	—	—	100	—	—
EBITDE	5,364	8,630	15,315	14,319	18,483	2,232

As a measure of our liquidity, we believe that the most directly comparable U.S. and Hong Kong GAAP measure to EBITDE is cash provided by operating activities. We use EBITDE in addition to this standard measure because EBITDE excludes exploration expenses, which depend on a company's method of accounting for exploration activity and fluctuate based on the company's reported success rate. EBITDE provides an additional measure for comparing our cash provided by operating activities before accounting for exploration expenses with other companies' figures.

The following table reconciles our cash provided by operating activities under U.S. GAAP to our definition of EBITDE for the periods indicated.

	Year ended December 31,					
	1998	1999	2000	2001	2002	2002
	Rmb	Rmb	Rmb	Rmb	Rmb	US$
			(in millions)			
Cash provided by operating activities	3,942	7,323	13,233	11,759	14,597	1,763
plus/(less): movements in working capital	(70)	164	326	(583)	4	—
plus/(less): returns on investments and servicing of finance	598	651	317	(346)	(181)	(22)
plus: taxation paid	52	198	880	2,611	2,846	343
plus: short-term investment income	—	—	—	221	193	23
plus/(less): recovery (provision) for doubtful debts	(58)	5	58	5	—	—
plus: share of profit of an associate	—	13	218	90	165	20
plus/(less): gain on sale/loss on disposals and write-off of property, plant and equipment	575	—	(220)	(457)	(437)	(52)
other adjustments	(259)	29	(50)	23	(12)	(1)
less: realized and unrealized holding gains from available-for-sale marketable securities	—	—	—	(43)	(10)	(1)
plus: exploration expenses	584	247	553	1,039	1,318	159
EBITDE	5,364	8,630	15,315	14,319	18,483	2,232

You should not consider our definition of EBITDE in isolation or construe it as an alternative to net income or cash provided by operating activities or as an indicator of operating performance, liquidity or any other standard measure under either U.S. or Hong Kong GAAP. Our definition of EBITDE fails to account for taxes, interest expenses, other non-operating cash expenses and exploration expenses. EBITDE also does not consider any functional or legal requirements of our business that may require us to allocate funds for purposes other than debt service or exploration and development activities. Our EBITDE measures may not be comparable to similarly titled measures used by other companies.

Critical Accounting Policies

We prepare our consolidated financial statements in accordance with Hong Kong GAAP. The preparation of these financial statements requires management to make estimates and judgments that affect the reported amounts of our assets and liabilities, the disclosure of our contingent assets and liabilities as of the date of our financial statements and the reported amounts of our revenues and expenses during the periods reported. Management makes these estimates and judgments based on historical experience and other factors that are believed to be reasonable under the circumstances. Actual results may differ from these estimates under different assumptions or conditions. We believe that the following significant accounting policies may involve a higher degree of judgment in the preparation of our consolidated financial statements. For additional discussion of our significant accounting policies, see note 4 to our consolidated financial statements beginning on page F-1.

Oil and Gas Properties, Land and Buildings

For oil and gas properties, we have adopted the successful efforts method of accounting. As a result, we capitalize initial acquisition costs of oil and gas properties and recognize impairment of initial acquisition costs based on exploratory experience and management judgment. Upon discovery of commercial reserves, we transfer acquisition costs to proved properties and capitalize the costs of drilling and equipping successful exploratory wells, all development costs, and the borrowing costs arising from borrowings used to finance the development of oil and gas properties before they are substantially ready for production. We treat the costs of unsuccessful exploratory wells and all other related exploration costs as expenses when incurred. We amortize capitalized acquisition costs of proved properties by the unit-of-production method on a property-by-property basis based on the total estimated units of proved reserves. We estimate future dismantlement costs for oil and gas properties with reference to the estimates provided from either internal or external engineers after taking into consideration the anticipated method of dismantlement required in accordance with current legislation and industry practices. The associated cost is capitalized and the liability is discounted and an accretion expense is recognized using the credit-adjusted risk-free interest rate in effect when the liability is initially recognized.

Land and buildings represent our onshore buildings and our land use rights which are stated at valuation less accumulated depreciation and accumulated impairment losses. Professional valuations are performed periodically, our last valuation was performed on December 31, 2000. In intervening years, our directors review the carrying value of land and buildings and make adjustment where in their opinion there has been a material change in value. Any increase in land and building valuation is credited to the revaluation reserves; any decrease is first offset against an increase in an earlier valuation in respect of the same property and is thereafter charged to the income statement. Depreciation is calculated on the straight-line basis at an annual rate estimated to write off the valuation of each asset over its expected useful life, ranging from 30 to 50 years.

Impairment of Assets

We make an assessment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable, or when there is any indication that an impairment loss previously recognized for an asset in prior years may no longer exist or may have decreased. In any event, we would make an estimate of the asset's recoverable amount, which is calculated as the higher of the asset's value in use or its net selling price. We recognize an impairment loss only if the carrying amount of an asset exceeds its recoverable amount. We charge an impairment loss to the income statement in the period in which it arises unless the asset is carried at a revalued amount. For a revalued asset, we account for the impairment loss in accordance with the relevant accounting policy for such revalued asset. A previously recognized impairment loss is reversed only if there has been a change in our estimates used to determine the recoverable amount of an asset. However, no reversal may put the value of the asset higher than the carrying amount that we would have determined (net of any depreciation/amortization) had no impairment loss been recognized for the asset in prior years.

A reversal of an impairment loss is credited to the income statement in the period in which it arises, unless the asset is carried at a revalued amount, when the reversal of the impairment loss is accounted for in accordance with the relevant accounting policy for that revalued asset.

Provisions

We recognize a provision when a present obligation (legal or constructive) has arisen as a result of a past event and it is probable that a future outflow of resources will be required to settle the obligation so long as a reliable estimate can be made of the amount of the obligation. When the effect of discounting is material, the amount recognized for a provision is the present value at the balance sheet date of the future expenditures expected to be required to settle the obligation. The increase in the discounted present value amount arising from the passage of time is included in finance costs in the income statement. We make provisions for dismantlement based on the present value of our future costs expected to be incurred, on a site by site basis, in respect of our expected dismantlement costs at the end of the related oil exploration and recovery activities.

Deferred Tax

Deferred tax is provided, using the liability method, on all significant timing differences to the extent it is probable that the liability will crystallize in the foreseeable future. We do not recognize a deferred tax asset until its realization is assured beyond reasonable doubt.

Recognition of Revenue from Oil and Gas Sales and Marketing

We recognize revenue when it is probable that the economic benefits will flow to us and when the revenue can be measured reliably. For oil and gas sales, our revenues represent the invoiced value of sales of oil and gas attributable to our interests, net of royalties and any government share oil that is lifted and sold on behalf of the PRC government. Sales are recognized when the significant risks and rewards of ownership of oil and gas have been transferred to customers. Oil and gas lifted and sold by us above or below our participating interests in any production sharing contract result in overlifts and underlifts. We record these transactions in accordance with the entitlement method under which overlifts are recorded as liabilities and underlifts are recorded as assets at year-end oil prices. Settlement will be in kind when the liftings are equalized or in cash when production ceases. We enter into gas sales contracts with customers which typically contain take-or-pay clauses. These clauses require our customers to take a specified minimum volume of gas each year. If a customer fails to take the minimum volume of gas, the customer must pay for the gas even though it did not take the gas. The customer can offset the deficiency payment against any future purchases in excess of the specified volume. We record any deficiency payment as deferred revenue which is included in other payables until any make-up gas is taken by the customer or the expiry of the contract. Our marketing revenues represent sales of oil purchased from the foreign partners under our production sharing contracts and revenues from the trading of oil through our subsidiary in Singapore. The title, together with the risks and rewards of the ownership of such oil purchased from the foreign partners, are transferred to us from the foreign partners and other unrelated oil and gas companies before we sell such oil to our customers. The cost of the oil sold is included in crude oil and product purchases.

Results of Operations

Overview

The following table summarizes the components of our revenues and net production as percentages of our total revenues and total net production for the periods indicated:

	Year ended December 31,					
	2000		2001		2002	
	(Rmb in millions, except percentages, production data and prices)					
Revenues:						
Oil and gas sales:[1]						
Crude oil	17,189	71.0%	15,916	76.4%	21,498	81.5%
Natural gas	1,630	6.7	1,645	7.9	2,281	8.7
Total oil and gas sales	18,819	77.7%	17,561	84.3%	23,779	90.2%
Marketing revenues	5,126	21.2	2,537	12.2	2,377	9.0
Other income	279	1.1	722	3.5	217	0.8
Total revenues	24,224	100.0%	20,820	100.0%	26,374	100.0%
Net production (million BOE):						
Crude oil	75.5	86.2%	83.5	87.5%	109.0	86.2%
Natural gas	12.1	13.8	11.9	12.5	17.5	13.8
Total net production	87.6	100.0%	95.4	100.0%	126.5	100.0%
Average net realized prices:						
Crude oil (per bbl)	US$28.21		US$23.34		US$24.35	
Natural Gas (per mcf)	3.09		3.08		2.98	

(1) These figures do not include our revenues from the Pinghu gas field.

The following table sets forth, for the periods indicated, certain income and expense items in our consolidated income statements as a percentage of total revenues:

	Year ended December 31,		
	2000	2001	2002
Operating Revenues:			
Oil and gas sales	77.7%	84.3%	90.2%
Marketing revenues	21.1	12.2	9.0
Other income	1.2	3.5	0.8
Total revenues	100.0%	100.0%	100.0%
Expenses:			
Operating expenses	(8.8)%	(11.2)%	(14.3)%
Production taxes	(4.3)	(4.2)	(3.9)
Exploration costs	(2.3)	(5.0)	(5.0)
Depreciation, depletion and amortization	(10.6)	(12.3)	(15.2)
Dismantlement	(0.4)	(0.4)	(0.5)
Crude oil and product purchases	(21.0)	(11.8)	(8.8)
Selling and administrative expenses	(1.9)	(3.0)	(3.8)
Other	(0.9)	(3.0)	(0.1)
	(50.2)%	(50.9)%	(51.6)%
Interest income	1.0	1.5	0.5
Interest expenses	(2.0)	(0.5)	(1.1)
Exchange gain (loss), net	1.6	1.1	(0.4)
Investment income	—	1.1	0.7
Share of profit of an associate	0.9	0.4	0.6
Non-operating profit (loss), net	(0.8)	0.2	(0.3)
Income before tax	50.5	52.9	48.4
Tax	(8.0)	(14.6)	(13.4)
Net income	42.5%	38.3%	35.0%

Calculation of Revenues

China

We report total revenues, which consist of oil and gas sales, marketing revenues and other income, in our consolidated financial statements. With respect to revenues derived from our offshore China operations, oil and gas sales represent gross oil and gas sales less royalties and share oil payable to the PRC government. These amounts are calculated as follows:

- gross oil and gas sales consist of our percentage interest in total oil and gas sales, comprised of (i) a 100% interest in our independent oil and gas properties and (ii) our participating interest in the properties covered under our production sharing contracts, less an adjustment for production allocable to foreign partners under our production sharing contracts as reimbursement for exploration expenses attributable to our participating interest;

- royalties represent royalties we pay to the PRC government on production with respect to each of our oil and gas fields. The amount of royalties varies from 0% up to 12.5% based on the annual production of the relevant property. We pay royalties on oil and gas we produce independently and under production sharing contracts;

- government share oil, which is only paid on oil and gas produced under production sharing contracts, is calculated as described under "—Overview—Production Sharing Contracts Offshore China;"

- other income mainly represents project management fees charged to our foreign partners and handling fees charged to end customers—both fees are recognized when the services are rendered; and

- we pay production taxes to the PRC government that are equal to 5% of the oil and gas we produce independently and under production sharing contracts. Before May 1, 2001, we paid an additional 0.5% local surcharge on the oil and gas that we produced independently. This surcharge no longer exists. Our oil and gas sales are not reduced by production taxes. Production taxes are included in our expenses under "production taxes."

Marketing revenues represent our sales of our foreign partners' oil and gas produced under our production sharing contract and purchased by us from our foreign partners under such contracts as well as from international oil and gas companies through our wholly owned subsidiary in Singapore. Net marketing revenues represent the marketing revenues net of the cost of purchasing oil and gas from foreign partners and from international oil and gas companies. Our foreign partners have the right to either take possession of their oil and gas for sale in the international market or to sell their oil and gas to us for resale in the PRC market.

Our share of the oil and gas sales of our associated company is not included in our revenues, but our share of the profit or loss of our associated company is included in our consolidated statements of income under "share of profit of an associate."

Indonesia

The oil and gas sales from our subsidiaries in Indonesia consist of our participating interest in the properties covered under the relevant production sharing contracts, less adjustments for share oil payable under our Indonesian production sharing contracts to Pertamina, the Indonesian state-owned oil and gas company, and for a domestic market obligation under which the contractor must sell a specified percentage of its crude oil to the local Indonesian market at a reduced price.

First Quarter 2003 Financial and Operating Results

On March 30, 2003, we announced certain information relating to our revenues, expenditures and production results for the first quarter of 2003. Our financial data for this period has not been audited by our independent public accountants, and is presented here only for your information. You should not rely on this financial or production data in making an investment decision with respect to the notes.

During the first quarter of 2003, our revenues from the sale of oil and gas were Rmb 7.5 billion (US$905.8 million). Our daily average crude oil production was 308,777 barrels per day during this period, compared to 298,625 barrels per day in 2002, while our daily average natural gas production was 242 million cubic feet per day, compared to 272.6 million cubic feet per day in 2002. The average net realized price of our crude oil was US$30.33 per barrel during the first quarter of 2003, compared to US$24.35 per barrel in 2002, while the average net realized price of our natural gas was US$2.99 per thousand cubic feet, compared to US$2.98 per thousand cubic feet in 2002. The higher average net realized price of our crude oil during the recent quarterly period primarily reflected the impact of the Iraqi conflict on oil prices.

2002 versus 2001

Our oil and gas sales for the year 2002 were Rmb 23,779.3 million (US$2,871.9 million), an increase of Rmb 6,218.5 million (US$751.0 million), or 35.4%, from Rmb 17,560.8 million in the year 2001. The increase primarily reflects the rise in our production level, as well as the increase in global crude oil prices during 2002. Of the increase in oil and gas sales, Rmb 5,417.0 million (US$654.2

million) was attributable to our increased production volume, while Rmb 801.5 million (US$96.8 million) was attributable to the rise in crude oil prices. In 2002, as a result of the commencement of production in our new oil and gas properties as well as our successful acquisition of overseas oil and gas properties, our production volume increased significantly compared to 2001. Our net production level in 2002 increased by 33% compared to the same period last year, one of the highest growth years in our history. The net crude oil and condensate production volume per day was 298,625 barrels in 2002, compared to 228,873 barrels in 2001, an increase of 30.5%. Our Indonesian oil and gas operations accounted for 15% of the increase in our production volume. Production volume increases offshore China primarily resulted from the commencement of production at our new oil and gas properties, including new platforms in Suizhong 36-1 (Phase II), Qinhuangdao 32-6, Wenchang 13-1 and Wenchang 13-2. Our daily average production for natural gas in 2002 was 272.6 million cubic feet, an increase of 77.6 cubic feet, or 39.8%, from 195.0 million cubic feet in 2001. The increase was primarily attributable to contributions from our Indonesian operations. Our crude oil sales prices are determined in accordance with international crude oil prices. The average realized price for our crude oil was US$24.35 per barrel in 2002, an increase of US$1.01, or 4.3%, compared to US$23.34 per barrel in 2001. The average realized price of natural gas was US$2.98 per thousand cubic feet in 2002, a decrease of US$0.10, or 3.2%, from US$3.08 per thousand cubic feet in 2001. The decrease was due to the lower realized price of natural gas from our Indonesian properties relative to the realized price of natural gas from our offshore China properties.

Our marketing revenues in 2002 were Rmb 2,377.5 million (US$287.1 million), a decrease of Rmb 159.5 million (US$19.3 million), or 6.3%, from Rmb 2,537.0 million in 2001.

Our other income, reported on a net basis in 2002, was Rmb 217.1 million (US$26.2 million) and consisted primarily of project management and handling fees. This was at a similar level to 2001. In 2001, our other income on a net basis was Rmb 203.7 million, which was derived from our other income of Rmb 721.7 million less corresponding costs of Rmb 517.9 million.

Our operating expenses were Rmb 3,775.3 million (US$456.0 million) in 2002, an increase of Rmb 1,446.2 million (US$174.7 million), or 62.1%, from Rmb 2,329.1 million in 2001. The increase primarily resulted from operating expenses in connection with the Indonesian oil and gas properties and the commencement of operations in new properties offshore China. The operating expenses for the Indonesian oil and gas properties were Rmb 1,237.8 million (US$149.5 million) in 2002. On a unit of production basis, operating expenses were Rmb 30.3 (US$3.66) per BOE in 2002, which were higher than operating expenses of Rmb 24.9 per BOE in 2001. The increase was largely attributable to the higher operating expenses on a unit of production basis for the Indonesian oil and gas properties, resulting from the different fiscal regime applicable to Indonesia. Our operating expenses excluding Indonesia in 2002 were Rmb 23.6 (US$2.85) per BOE.

Our production taxes for the year 2002 were Rmb 1,023.0 million (US$123.6 million), an increase of 15.8%, or Rmb 139.2 million (US$16.8 million) from Rmb 883.8 million in 2001. The increase was due to an increase in sales revenues in 2002.

Our exploration costs for the year 2002 were Rmb 1,318.3 million (US$159.2 million), an increase of Rmb 279.0 million (US$33.7 million), or 26.8%, from Rmb 1,039.3 million in 2001. The increase primarily resulted from a higher level of exploration activities.

Our depreciation, depletion and amortization expenses for 2002 were Rmb 4,019.5 million (US$485.4 million), an increase of Rmb 1,452.6 million (US$175.4 million), or 56.6%, from Rmb 2,566.9 million in 2001. On a unit of production basis, depreciation, depletion and amortization expenses for the year 2002 were Rmb 32.3 (US$3.90) per BOE, an increase of 17.5% compared to Rmb 27.5 (US$3.32) per BOE in 2001. The primary reason for the increase was the newly acquired Indonesian oil and gas properties, and the commencement of production at new oil and gas properties offshore China.

Our dismantlement costs for the year 2002 was Rmb 126.1 million (US$15.2 million), an increase of Rmb 35.7 million (US$4.3 million), or 39.5%, from Rmb 90.4 million in 2001. The increase was primarily due to an upward revision of the estimated dismantlement costs and the commencement of production at new oil and gas properties offshore China.

We had no impairment losses related to oil and gas assets in 2002.

Our crude oil and product purchases for the year 2002 were Rmb 2,326.3 million (US$281.0 million), a decrease of Rmb 127.0 million (US$15.3 million), or 5.2%, from Rmb 2,453.3 million in 2001. We handle crude oil sales in China for our foreign partners. Upon their request, we purchase their share of crude oil for resale in China, since we are one of the only three companies authorized to market and sell crude oil in the PRC. We do not have control over our foreign partners' decisions regarding the sale of their share of production, and therefore have no control over the volume that we may be asked to handle in any particular period.

Our selling and administrative expenses for the year 2002 were Rmb 1,006.5 million (US$121.6 million), an increase of Rmb 391.1 million (US$47.2 million), or 63.6%, from Rmb 615.4 million in 2001. On a unit of production basis, selling and administrative expenses were Rmb 8.1 (US$0.98) per BOE in 2002, an increase of 22.7% from Rmb 6.6 per BOE in 2001. The primary reason for the increase was the Rmb 272.1 million (US$32.9 million) selling and administrative expenses incurred in connection with the acquisition of Indonesian oil and gas properties and the commencement of production at the new oil and gas properties offshore China. Our selling and administrative expenses excluding Indonesia in 2002 were Rmb 6.8 (US$0.82) per BOE.

Our net interest expense for 2002 was Rmb 146.9 million (US$17.7 million), an increase of Rmb 348.0 million (US$42.0 million) from a net interest income of Rmb 201.1 million in 2001. This increase was primarily due to interest expense associated with US$500 million guaranteed notes in 2002, which led to an increase in interest expense of Rmb 135.0 million (US$16.3 million). Further, the net interest expenses recognized under SSAP 28, which we adopted in 2002, relating to dismantlement costs were Rmb 77.9 million (US$9.4 million).

Our exchange loss for 2002 was Rmb 113.8 million (US$13.7 million) compared with an exchange gain of Rmb 235.4 million in 2001. The decrease was partly attributable to exchange rate fluctuations related to our Japanese yen-denominated loans in 2002. On December 27, 2002, we prepaid a sum of JPY 21,162 million in Japanese yen-denominated loans, after which our outstanding Japanese yen-denominated loans were JPY 1,357 million. Since the outstanding amount of our Japanese yen-denominated loans is hedged using foreign currency swaps, we do not expect similar exchange gains or losses in the future.

Our investment income for 2002 was Rmb 193.3 million (US$23.3 million), a decrease of Rmb 27.4 million (US$3.3 million), or 12.4%, from Rmb 220.7 million in 2001. The decrease was primarily due to a decline in short-term interest rates in 2002.

Our share of profit of an associate for the year 2002 was Rmb 165.4 million (US$20.0 million), an increase of Rmb 75.4 million (US$9.1 million), or 83.8%, from Rmb 90.0 million in 2001. This item reflected our share of profit generated by Shanghai Petroleum and Natural Gas Company Limited, our associated company. This company experienced a decrease in its amortization cost resulting from an increase in exploitable reserves.

Our non-operating loss for the year 2002 was Rmb 71.4 million (US$8.6 million), a decrease of Rmb 106.3 million (US$12.8 million) from non-operating profit of Rmb 34.9 million in 2001, primarily due to the losses incurred in the disposal of certain assets in 2002.

Our taxation for the year 2002 was Rmb 3,541.4 million (US$427.7 million), an increase of Rmb 493.2 million (US$59.6 million), or 16.2%, from Rmb 3,048.2 million in 2001. The primary reason for the increase was the increase in profit before tax. The effective tax rate for both 2001 and 2002 was 27.2%. See "—Taxation."

Our consolidated net income after tax was Rmb 9,232.8 million (US$1,115.4 million) in 2002, an increase of Rmb 1,275.2 million (US$154.0 million), or 16.0%, from Rmb 7,957.6 million in 2001.

2001 versus 2000

Our oil and gas sales for the year 2001 were Rmb 17,560.8 million, a decrease of Rmb 1,258.5 million, or 6.7%, from Rmb 18,819.3 million in 2000. Due to lower oil prices, our oil and gas sales from properties already operating prior to 2001 decreased approximately Rmb 3,351.5 million, which was partially offset by approximately Rmb 2,093.0 million in additional sales brought on by the commencement of operations at new oil and gas properties in 2001. Our average net realized crude oil price was US$23.34 per barrel in 2001, a decrease of US$4.87, or 17.3%, from US$28.21 per barrel in 2000, due to decreases in international oil prices. Our average net realized natural gas price was US$3.08 per thousand cubic feet in 2001, essentially unchanged from US$3.09 per thousand cubic feet in 2000. Net crude oil and condensate production in 2001 averaged approximately 228,873 barrels per day, an increase of 22,572 barrels, or 10.9% compared to 206,347 barrels per day in 2000. The increase in production primarily resulted from the commencement of production at new oil properties during 2001, including Suizhong 36-1 (Phase II), Qikou 17-2 and Qinhuangdao 32-6. Net natural gas production in 2001 averaged 195.0 million cubic feet per day, a decrease of approximately 2.9 million cubic feet, or 1.5%, from 197.9 million cubic feet per day in 2000. This decrease was primarily due to the increased thermal capacity of natural gas produced at Yacheng 13-1, which caused lower consumption of such natural gas by the contract user of Yacheng 13-1.

Our marketing revenues for the year 2001 were Rmb 2,537.0 million, a decrease of Rmb 2,589.0 million, or 50.5%, from Rmb 5,126.0 million in 2000.

Our other income was Rmb 721.7 million in 2001, an increase of Rmb 443.1 million, or 159.0%, compared to Rmb 278.6 million in 2000. The increase in other income primarily resulted from increases in project management fees and handling fees for production sharing contract blocks.

Our operating expenses for the year 2001 were Rmb 2,329.1 million, an increase of Rmb 205.0 million, or 9.7%, from Rmb 2,124.1 million in 2000, primarily due to increased costs associated with the commencement of productions at new oil and gas properties. On a unit of production basis, operating expenses in the year 2001 was Rmb 24.9 per BOE, compared to Rmb 24.8 per BOE in 2000.

Our production taxes for the year 2001 were Rmb 883.8 million, a decrease of Rmb 152.9 million, or 14.7%, from Rmb 1,036.7 million in 2000. The decrease was primarily due to lower sales revenue caused by significant drops in oil prices.

Our exploration costs for the year 2001 were Rmb 1,039.3 million, an increase of Rmb 486.4 million, or 88.0%, from Rmb 552.9 million in 2000 primarily due to the higher investment in significantly increasing exploration work in 2001 and the writing-off of expenses associated with exploration work on wells for uncertain reserves in earlier years.

Our depreciation, depletion and amortization expenses for the year 2001 were Rmb 2,566.9 million, a decrease of Rmb 11.0 million, or 0.4%, from Rmb 2,577.9 million in 2000. On a unit of production basis, depreciation, depletion and amortization expenses for the year 2001 was Rmb 27.5 per BOE, a decrease of Rmb 2.5, or 8.3%, compared to Rmb 30.0 per BOE in 2000. The primary reason for the decrease was that the increase in proved reserves in certain high-production oil and gas fields resulted in a decrease in the unit depreciation, depletion and amortization cost of those fields, thereby leading to the decrease in our total depreciation, depletion and amortization cost.

Our dismantlement costs for the year 2001 was Rmb 90.4 million, a decrease of Rmb 13.2 million, or 12.7%, from Rmb 103.6 million in 2000. The decrease was due to full provisioning of the allowance for certain mature fields in earlier years.

Our impairment losses related to oil and gas assets were Rmb 99.7 million for the year 2001, which reflected the estimated impairment resulting from two oilfields not being expected to fully recover their net book values through future cash flows.

Our crude oil and product purchases for the year 2001 were Rmb 2,453.3 million, a decrease of Rmb 2,644.5 million, or 51.9%, from Rmb 5,097.8 million in 2000.

Our selling and administrative expenses for the year 2001 were Rmb 615.4 million, an increase of Rmb 159.4 million, or 35.0%, from Rmb 456.0 million in 2000. On a unit of production basis, selling and administrative expenses were Rmb 6.6 per BOE in 2001, an increase of Rmb 1.3, or 25.0% from Rmb 5.3 per BOE in 2000. The relative increase resulted from a combination of the following factors: in 2000, selling and administrative expenses were lower, in part due to the recovery of Rmb 57.7 million in doubtful accounts; in 2001, we made a Rmb 40.0 million provision for staff and workers bonus and welfare funds in accordance with a resolution of our board of directors; there was an increase of salary and staff benefits as a result of employee compensation reform; and there was also an increase of public facilities, office administrative, telecommunication and travelling expenses as a result of greater business volume and higher office rents.

Our net interest income for the year 2001 was Rmb 201.1 million, an increase of Rmb 439.5 million, or 184.4%, from a net interest expense of Rmb 238.4 million in 2000. This increase was due to an increase in interest income resulting from significantly higher cash balances after our initial public offering in 2001 and lower interest expenses resulting from lower outstanding balances in respect of long-term indebtedness.

Our net exchange gain for the year 2001 was Rmb 235.4 million, a decrease of Rmb 145.9 million compared to Rmb 381.3 million in 2000.

Our investment income for 2001 was Rmb 220.7 million, which represented the income generated from investing the unused net proceeds from our initial public offering in low-risk short-term money market funds. There was no investment income in 2000.

Our share of profit of an associate for the year 2001 was Rmb 90.0 million, a decrease of Rmb 128.3 million, or 58.8%, compared to a gain of Rmb 218.3 million in 2000. Our associated company experienced a decrease in profit in 2001 as compared to 2000 primarily due to an increase in its exploration costs and an increase in its amortization cost resulting from lower exploitable reserves, as well as a decline in 2001 in the realized price of its condensate.

Our net non-operating profit for the year 2001 was Rmb 34.9 million, an increase of Rmb 230.9 million from a net non-operating loss of Rmb 196.0 million in 2000, primarily due to the losses incurred in the disposal of certain assets in 2000.

Our taxation for the year 2001 was Rmb 3,048.2 million, an increase of Rmb 1,122.1 million, or 58.3%, from Rmb 1,926.1 million in 2000. The primary reason for the increase was that the period for which our PRC subsidiary enjoyed preferential enterprise income tax treatment expired after 2000 and the applicable enterprise income tax rate for our PRC subsidiary was adjusted from 15% to the normal rate of 30% for enterprises with foreign investment under the Laws of the PRC for Joint Venture Using Chinese and Foreign Investment with effect from 2001.

Our consolidated net income was Rmb 7,957.6 million in 2001, a decrease of Rmb 2,339.0 million, or 22.7%, from Rmb 10,296.6 million in 2000.

Liquidity and Capital Resources

The following table summarizes cash flows for the periods presented:

	Year ended December 31,		
	2000	**2001**	**2002**
	(Rmb in millions)		
Cash provided by (used for):			
Operating activities	13,233	11,759	14,597
Investing activities	(7,861)	(11,366)	(11,724)
Financing activities	(3,454)	3,204	(1,428)
Net increase in cash and cash equivalents	1,918	3,597	1,445

Cash Provided by Operations

Cash provided by operations in 2002 amounted to Rmb 17,262.0 million (US$2,084.8 million), an increase of Rmb 3,237.0 million (US$390.9 million), or 23.1%, from Rmb 14,025.0 million in 2001. In addition to an increase in profit before tax of Rmb 1,768.4 million (US$213.6 million), the increase in cash provided by operations was also due in part to adjustments related to an increase in net interest expenses of Rmb 348.0 million (US$42.0 million), an increase in net exchange loss of Rmb 375.1 million (US$45.3 million), an increase in depreciation, depletion and amortization expenses of Rmb 1,452.6 million (US$175.4 million), an increase in dismantlement costs of Rmb 35.7 million (US$4.3 million), a decrease in short-term investment income of Rmb 27.4 million (US$3.3 million) and an increase in amortization of a discount for long-term guaranteed notes of Rmb 6.1 million (US$0.7 million).

The increase was partially offset by the growth in our share of income of associated companies of Rmb 75.4 million (US$9.1 million), a decrease in provision for impairment of property, plant and equipment of Rmb 99.7 million (US$12.0 million) and a decrease in loss on disposals and write-off of property, plant and equipment of Rmb 19.0 million (US$2.3 million).

In addition, operating cash flow was adversely affected by an increase in current liabilities from operating activities of Rmb 500.8 million (US$60.5 million), and a simultaneous increase in current assets excluding cash and bank balances of Rmb 504.7 million (US$61.0 million). See note 32 to our consolidated financial statements beginning on page F-1.

Cash provided by operations in 2001 decreased Rmb 1,473.2 million, or 11.1%, to Rmb 11,759.5 million from Rmb 13,232.7 million in 2000. The decrease resulted from a decrease in profit before tax of Rmb 1,216.8 million, adjustments related to a decrease in net interest expenses of Rmb 439.5 million and an increase in short-term investment gains of Rmb 274.3 million. The decrease in cash flow was partly offset by a non-cash write-off of exploration dry hole expenses and disposal of fixed assets of Rmb 236.7 million, non-cash impairment losses related to oil and gas assets of Rmb 99.7 million, a decrease in share of profit of an associated company of Rmb 128.3 million and a decrease in unrealized foreign exchange gain of Rmb 62.9 million.

In addition, operating cash flow was favorably affected by a net decrease in working capital. The decrease in working capital resulted from an increase of Rmb 268.4 million in accounts payable and accrued liabilities and a decrease of Rmb 314.9 million in accounts receivable and other current assets.

As of December 31, 2002, we had a working capital surplus of Rmb 17,352.1 million (US$2,095.7 million), an increase of Rmb 1,713.6 million (US$207.0 million) from Rmb 15,638.5 million (US$1,888.7 million) in 2001. The increase mainly resulted from an increase in accounts receivable of Rmb 1,869.1 million (US$225.8 million), an increase in inventory of Rmb 221.3 million (US$26.7 million), an increase in other receivables of Rmb 645.2 million (US$77.9 million) and a decrease in current portion of long-term bank loans of Rmb 934.3 million (US$112.8 million). Accounts receivable as of December 31, 2002 were significantly higher than the corresponding figures as of December 31, 2001 primarily as a result of significantly higher sales in December 2002 compared with December 2001. As we settle our crude oil sales based on 30-day payment terms, which is the industry practice, our total sales volume and sale prices on a rolling basis significantly affect accounts receivable. This increase in working capital was partially offset by an increase in accounts payable and accrued liabilities of Rmb 2,967.4 million (US$358.5 million), an increase in taxes payable of Rmb 491.0 million (US$59.3 million) and an increase in amounts due to related companies and parent company of Rmb 218.7 million (US$26.4 million). Our higher accounts payable as of December 31, 2002, reflected increased purchases of materials and supplies associated with our capital expenditure program and also included an accrual for a routine payment obligation to operators of certain production sharing contracts, which was paid subsequent to the date of the balance sheet.

Capital Expenditures and Investments

In line with our use of the successful efforts method of accounting, historical capital expenditures and investments primarily include successful exploration and development expenditures. Total capital expenditures were Rmb 11,566.9 million (US$1,397.0 million) in 2002, an increase of Rmb 7,224.3 million (US$872.5 million), or 166.4%, from Rmb 4,342.6 million (US$524.5 million) in 2001. The capital expenditure in 2002 included Rmb 585.6 million (US$70.7 million) for capitalized exploration activities, Rmb 6,247.1 million (US$754.5 million) for development activities, and Rmb 4,734.2 million (US$517.8 million) for acquiring Indonesian oilfields. Our development expenditures in 2002 related principally to the development of Suizhong 36-1 (Phase II), Qinhuangdao 32-6, Wenchang 13-1, Wenchang 13-2, Penglai 19-3 and Panyu 4-2/5-1.

Total capital expenditures were Rmb 4,342.6 million in 2001, a decrease of Rmb 61.4 million, or 1.4%, from Rmb 4,404.0 million in 2000. The capital expenditures in 2001 included Rmb 311.5 million for capitalized exploration activities and Rmb 4,013.1 million for development activities. Our development expenditures in 2001 related principally to the development of Suizhong 36-1 (Phase II) and Qinhuangdao 32-6 and Wenchang 13-1, Wenchang 13-2 and Dongfang 1-1.

Our total capital expenditures for general exploration and development activities for 2002 was approximately US$978 million. Over the next two years, we have budgeted approximately US$3.5 billion for capital expenditures, approximately US$308 million of which is budgeted for general exploration activities offshore China and approximately US$2.7 billion is budgeted for development activities offshore China.

The following table sets forth actual or budgeted capital expenditures for our key operating areas for the periods indicated.

	Year ended December 31,		
	2002[1]	2003[2]	2004[2]
	(US$ in millions)		
Operating Area:			
Bohai Bay			
Development	261	588	1,080
Exploration	55	63	51
Western South China Sea			
Development	269	158	258
Exploration	69	25	37
East China Sea			
Development	52	137	116
Exploration	18	20	20
East South China Sea			
Development	122	152	168
Exploration	42	43	49
Overseas			
Development	90	359	140
Total	978	1,545	1,919

(1) Figures for 2002 represent our actual spending for capital expenditure purposes.
(2) Figures for 2003 and 2004 represent our budgeted capital expenditures.

In addition to the budgeted development and exploration expenditures relating to the oil and gas properties described above, we may make additional capital expenditures and investments in these periods consistent with our business strategy. For example, the above budgeted amounts do not include any investments we may make in the liquefied natural gas project located in Guangdong Province, other natural gas projects and overseas natural gas properties. See "Business—Business Strategy."

Our ability to maintain and grow our revenues, net income and cash flows depends upon continued capital spending. We adjust our capital expenditure and investment budget on an annual basis. Our capital expenditure plans are subject to a number of risks, contingencies and other factors, some of which are beyond our control. Therefore, our actual future capital expenditures and investments will likely be different from our current planned amounts, and such differences may be significant. See "Risk Factors—Risks relating to our business—Our future prospects largely depend on our capital expenditure plans, which are subject to various risks."

Financing Activities

We had net cash outflows from financing activities of Rmb 1,428.1 million (US$172.5 million) in 2002, resulting primarily from our repayment of Rmb 3,367.3 million (US$406.7 million) in bank loans and dividend distributions of Rmb 2,265.1 million (US$273.6 million). Of the total bank loans that we repaid, we prepaid Rmb 2,956.0 million (US$357.0 million), including JPY 21,162 million in Japanese yen-denominated debt, US$103.4 million in dollar-denominated debt and Rmb 639.0 million in Renminbi-denominated debt. This cash outflow was offset by cash inflow of Rmb 4,059.3 million (US$490.3 million) resulting from our March 2002 offering of US$500 million in 6.375% guaranteed notes due 2012.

We have debt service obligations consisting of principal and interest payments on our outstanding indebtedness. The following table summarizes the maturities of our long-term debt outstanding as of December 31, 2002. Other than this offering, we have not incurred any material long-term debt since December 31, 2002.

	Debt maturities principal only				
	Original currency			Total Rmb	Total US$
Due by December 31,	**US$**	**JPY**	**Rmb**	**equivalents**	**equivalents**
	(in millions, except percentages)				
2003	31.4	271.5	18.9	297.5	35.9
2004-2006	100.0	814.4	38.4	922.4	111.4
2007-2008	—	271.5	—	18.7	2.3
2009 and beyond	500.0	—	—	4,140.0	500.0
Total	631.4	1,357.4	57.3	5,378.6	649.6
Percentage of total debt	97.2%	1.7%	1.1%	100.0%	100.0%

In early 2003, we prepaid a further US$31.4 million in U.S. dollar-denominated debt and all of our then existing Renminbi-denominated debt. As of the date of this offering memorandum, we had a total U.S. dollar debt of US$600.0 million and a total foreign currency debt of US$611.3 million. Through the debt offering and prepayment of debt, we extended the average maturity of our debt portfolio from three years to approximately eight years, and, through the prepayment of the majority of our Japanese yen-denominated debt, largely eliminated our Japanese yen exposure risk and improved our debt structure.

In 2001, we had net cash inflows from financing activities of Rmb 3,204.1 million. Net cash flows from financing activities in 2001 resulted primarily from Rmb 10,101.6 million in proceeds from our initial public offering, including the exercise of the related over-allotment option, in early 2001 and short-term bank loans of Rmb 2,500 million, offset in part by cash outflows of Rmb 4,268.5 million for dividends paid, Rmb 3,497.5 million for repayment of bank loans and Rmb 1,660.0 million for retirement fund payments to our parent company. See "—Employee Benefits."

After we became a separate entity as part of CNOOC's reorganization in October 1999, we paid dividends of Rmb 1,045.4 million in March 2000 and declared a dividend of Rmb 6,426.4 million on December 20, 2000, which was paid in full prior to February 1, 2001. On August 27, 2001, we declared a dividend of Rmb 871.8 million, which was paid in full prior to October 31, 2001. On June 6, 2002, we declared a dividend of Rmb 1,306.7 million (US$157.8 million), which was paid in full by June 19, 2002. On August 23, 2002, we declared a divided of Rmb 958.3 million (US$115.7 million), which was paid in full by September 27, 2002. The payment and the amount of any dividends in the future will depend on our results of operations, cash flows, financial condition, the payment by our subsidiaries of cash dividends to us, future prospects and other factors which our directors may consider relevant. The amount of dividends we paid historically is not indicative of the dividends that we will pay in the future.

We believe our future cash flows from operations, borrowing capacity and the proceeds of this offering will be sufficient to fund planned capital expenditures and investments, debt maturities and working capital requirements through at least 2004. Several large financial institutions have expressed an interest in supporting our business development, although we have not entered into any agreements for additional financing with these institutions. However, our ability to obtain adequate financing to satisfy our capital expenditure and debt service requirements may be limited by our financial condition and results of operations and the liquidity of international and domestic financial markets, including the following factors:

- Any failure by us to achieve timely rollover, extension or refinancing of our short-term debt may result in our inability to meet our obligations in connection with debt service, accounts payable and/or other liabilities when they become due and payable.

- Our primary operating subsidiary is a PRC incorporated company. Therefore, prior to accessing the international capital markets we will be subject to limitations imposed by various PRC government authorities, including the State Administration for Foreign Exchange and the People's Bank of China, depending on the type of international financing raised. We may also need to obtain PRC government support for any project involving significant capital investment in the operations of our PRC subsidiary.

- In addition, financing sources often look to similarly situated entities when determining whether, and at what rates, to provide financing. Successful or unsuccessful financings by Hong Kong and PRC entities similarly situated to us could have an impact on our ability to obtain external financing.

See "Risk Factors—Risks relating to our business—Our future prospects largely depend on our capital expenditure plans, which are subject to various risks" and "—We may not be able to obtain external financing that is acceptable to us for business development purposes."

Employee Benefits

All of our full-time employees in the PRC are covered by a government-regulated pension plan and are entitled to an annual pension at their retirement dates. The PRC government is responsible for the pension liabilities to these retired employees under this government pension plan. The actual pension payable to each retiree is subject to a formula based on the status of the individual pension account, general salary and inflation movements. We are required to make annual contributions to the government pension plan at rates ranging from 12% to 22.5% of our employees' base salaries. The related pension costs are expensed as incurred.

When we became a separate entity as part of CNOOC's reorganization in October 1999, CNOOC retained all liabilities for retirement benefits for its employees, both former and current, who had not been transferred to us. As compensation for CNOOC's retention of liabilities for retirement benefits payable to approximately 7,000 retired CNOOC employees who were previously engaged in the oil and gas business that was transferred to us in the reorganization, we made a one-time payment to CNOOC of Rmb 1,660.0 million in 2001.

For the years ended December 31, 2000, 2001 and 2002, our retirement expenses attributed to the current government plan were Rmb 12.8 million, Rmb 6.4 million and Rmb 7.0 million, respectively.

The expenses attributable to mandatory contributions under the current government pension plan are included in our historical consolidated statements of income under either operating expenses for our production staff or selling and administrative expenses for our administrative staff. We expect that, under the current PRC rules and regulations regarding employee retirement benefits, the future costs of the current government plan will be comparable to our historical costs, subject to customary increases largely in line with salary increases of our employees.

Our Indonesian subsidiaries employ approximately 1,000 employees, including approximately 30 managerial staff and technicians. We provide expatriate staff with employee benefits that we believe to be in line with customary international practices. Our non-expatriate employees in Indonesia enjoy welfare benefits mandated by Indonesia labor laws.

Holding Company Structure

We are a holding company. Our entire petroleum exploration, development, production and sales business in the PRC is owned and conducted by CNOOC China Limited, our wholly foreign-owned enterprise in the PRC. Our entire petroleum exploration, development and production business outside of the PRC is owned and conducted by CNOOC International Limited, our wholly owned subsidiary incorporated in the British Virgin Islands. International sales of crude oil are conducted by China

Offshore Oil (Singapore) International Pte. Ltd., our wholly owned subsidiary incorporated in Singapore. Accordingly, our future cash flow will consist principally of dividends from our subsidiaries. The subsidiaries' ability to pay dividends to us is subject to various restrictions, including legal restrictions in their jurisdictions of incorporation. For example, legal restrictions in the PRC permit payment of dividends only out of net income determined in accordance with PRC accounting standards and regulations. In addition, under PRC law, CNOOC China Limited is required to set aside a portion of its net income each year to fund certain reserve funds. These reserves are not distributable as cash dividends.

Inflation/Deflation

According to the China Statistical Bureau, China experienced an overall national deflation rate in 2000, 2001 and 2002, as represented by the general consumer price index, of 0.4%, 0.7% and 0.8%, respectively. The deflation has not had a significant impact on our results of operations in those years.

U.S. GAAP Reconciliation

Our consolidated financial statements are prepared in accordance with Hong Kong GAAP, which differ in certain material respects from U.S. GAAP. These differences relate primarily to the revaluation of properties and land use rights performed in connection with the reorganization, the treatment of impairment of long-lived assets, the treatment of stock compensation plans, the treatment of unrealized holding gains from available-for-sale investments in marketable securities and the provision for dismantlement liabilities. Except for the accounting treatment of the property revaluation and the recognition of stock compensation costs, the unrealized holding gains from available-for-sale investments in marketable securities and the provision for dismantlement liabilities, there are no material differences between Hong Kong GAAP and U.S. GAAP that affect our net income or shareholders' equity. See note 38 to our consolidated financial statements beginning on page F-1.

Taxation

We are subject to income taxes on an entity basis on income arising in or derived from the tax jurisdictions in which we and each of our subsidiaries are domiciled and operate. We are not liable for income taxes in Hong Kong as we currently do not have any assessable income from Hong Kong sources. Pursuant to a notice issued by the State Administration of Taxation in March 2001, we will be entitled to all tax benefits conferred by Chinese law on foreign invested enterprises.

Our PRC subsidiary, absent exemptions, is subject to enterprise income tax at the rate of 33%. Following the October 1999 reorganization, our PRC subsidiary became a wholly foreign owned enterprise and accordingly was exempted from 3% local surcharges, reducing its enterprise income tax rate to the current rate of 30%. Moreover, entities now comprising our PRC subsidiary were exempted from enterprise income taxes for two years starting from the first year of profitable operation in 1996 and were entitled to a 50% reduction of enterprise income taxes for three years beginning in 1998 and ending on December 31, 2000. This tax exemption increased our earnings by Rmb 1,920.7 million during the year ended December 31, 2000. Since January 1, 2001, the PRC subsidiary has been subject to the 30% enterprise income tax rate. The PRC enterprise income tax is levied based on taxable income including income from operations as well as other components of earnings, as determined in accordance with the generally accepted accounting principles in the PRC, or PRC GAAP. Besides income taxes, our PRC subsidiary also pays certain other taxes, including:

- production taxes equal to 5% of independent production and production under production sharing contracts; and

- business tax of 5% on other income.

Our subsidiary in Singapore, China Offshore Oil (Singapore) International Pte. Ltd., is subject to income tax at the rate of 10% and 26% for its oil trading activities and other income-generating activities, respectively. Our subsidiaries that own interests in oil properties in Indonesia along the Malacca Strait are subject to corporate and branch profit tax of 44%. The nine subsidiaries of Repsol-YPF, S.A. in Indonesia acquired by us during 2002 are all subject to corporate and branch profit tax at a rate of 48%. None of our other subsidiaries were subject to any income taxes in their respective jurisdictions for the year presented.

We calculate deferred taxation to account for timing differences between our tax bases, which is used for income tax reporting and prepared in accordance with applicable tax guidelines, and our accounting bases, which is prepared in accordance with applicable financial reporting requirements. Major timing differences include accelerated amortization allowances for oil and gas properties, which are offset in part by provision for dismantlement and a provision for impairment of property, plant and equipment and write-off of unsuccessful exploratory drilling. As of December 31, 2001 and 2002, we had Rmb 1,763.6 million (US$213.0) million and Rmb 6,141.1 million (US$741.9 million), respectively, in net deferred tax liabilities. The increase was primarily due to the acquisition of the Indonesia properties. See note 14 to our consolidated financial statements beginning on page F-1.

Market Risks

Our market risk exposures primarily consists of fluctuations in oil and gas prices, exchange rates and interest rates.

Commodity Price Risks

We are exposed to fluctuations in prices of crude oil and natural gas, which are commodities whose prices are determined by reference to international market prices. International oil and gas prices are volatile and this volatility has a significant effect on our net sales and net income. We do not hedge market risk resulting from fluctuations in oil and gas prices. See "—Overview" and "Risk Factors—Risks relating to our business—Our business, revenues and profits fluctuate with changes in oil and gas prices."

Currency Risk

Our foreign exchange exposure gives rise to market risk associated with exchange rate movements.

Substantially all of our oil and gas sales are denominated in Renminbi and U.S. dollars. In the last nine years, the PRC government's policy of maintaining a stable exchange rate and China's ample foreign reserves have contributed to the stability of the Renminbi. Our domestic oil and gas prices are quoted in U.S. dollars based on international U.S. dollar oil prices. Therefore we believe we are largely able to offset Renminbi exchange rate risk. In the past three years, our major foreign currency risk arose from our Japanese yen-denominated loan. On December 31, 2002, the outstanding amount of our Japanese yen-denominated loan was JPY 1,357 million. Since the outstanding amount of our Japanese yen loan is hedged using foreign currency swaps, we do not expect significant exchange gains or losses on this outstanding amount in the future. For a discussion of our currency risk, see "Risk Factors—Risks relating to the PRC—Government control of currency conversion and future movements in exchange rates may adversely affect our operations and financial condition."

Interest Rate Risk

We are exposed to interest rate risk arising from our loans. An upward fluctuation in interest rates increases the cost of new debt. We may use interest rate swap transactions, from time to time, to adjust our interest rate exposure when considered appropriate, based on existing and anticipated market conditions.

As of December 31, 2002, our total outstanding debt, including both foreign currency-denominated and Renminbi-denominated loans, was US$649.4 million, US$31.4 million of which was floating rate debt and US$618.0 million of which was fixed rate debt. After our prepayment of certain debt in early 2003 and as of the date of this offering memorandum, all of our outstanding long-term loans were fixed rate debt.

The following table sets forth additional information about the expected maturity dates of our outstanding debt as of December 31, 2002.

	2003	2004	2005	2006	2007	2008 and after	Total	Fair value as of December 31, 2002
	(Rmb in millions, except percentages)							
Long-term debt, including current portion								
Fixed rate	76	19	19	846	19	—	979	1,389
Average interest rate	8.185%	8.495%	8.592%	8.692%	4.000%	—		
Variable rate	260	—	—	—	—	—	260	260
Average interest rate	1.383%	—	—	—	—	—		
6.375% long-term guaranteed notes								
Fixed rate	—	—	—	—	—	4,140	4,140	4,482
Average interest rate	6.375%	6.375%	6.375%	6.375%	6.375%	6.375%		

The above table takes into account our early repayment of certain loans prior to the date of the offering memorandum.

For additional discussions of our market risks, see "Risk Factors."

Change of Accountants

On June 6, 2002, we terminated the engagement of Arthur Andersen & Co as our independent public accountants. Prior to such date, Arthur Andersen had audited our consolidated financial statements, including financial statements for the two year period ended December 31, 2001 included elsewhere in this offering memorandum. On June 15, 2002, Arthur Andersen was convicted of federal obstruction of justice charges in connection with the U.S. government's investigation of Enron Corporation. On August 31, 2002, Arthur Andersen voluntarily relinquished its licenses to practice public accountancy in all states of the United States and, accordingly, cannot furnish any written consent to the issue of this offering memorandum with the inclusion in it of its reports in the form and context in which they are included. For a discussion of risks related to Arthur Andersen, see "Risk Factors—Risks relating to our business—You may not be able to assert claims against Arthur Andersen, our independent public accountants for periods prior to December 31, 2001, nor may you be able to assert claims against our current independent public accountants for financial statements previously audited by Arthur Andersen."

On June 6, 2002, we appointed Ernst & Young as our independent accountants. Ernst & Young audited our consolidated financial statements for the year ended December 31, 2002, beginning on page F-1 of this offering memorandum.

Recent Accounting Pronouncements

The following recently-issued and revised Hong Kong Society of Accountants Statements of Standard Accounting Practice, or SSAPs, are effective for the first time for the current year's financial statements:

- SSAP 1 (Revised) - "Presentation of financial statements;"
- SSAP 11 (Revised) - "Foreign currency translation;"

- SSAP 15 (Revised) - “Cash flow statements;”
- SSAP 34 - “Employee benefits;”
- Interpretation 14 - “Evaluating the substance of transactions involving the legal form of a lease;”
- Interpretation 15 - “Business combinations - ‘Date of exchange’ and fair value equity instruments;” and
- Interpretation 18 - “Consolidation and equity method - Potential voting rights and allocation of ownership interests.”

These SSAPs prescribe new accounting measurement and disclosure practices. The major effects on our accounting policies and on the amounts disclosed in these financial statements of adopting these SSAPs and Interpretations are summarized as follows:

SSAP 1 (Revised) prescribes the basis for the presentation of financial statements and sets out guidelines for their structure and minimum requirements for their content. The principal impact of the revision to this SSAP is that a consolidated statement of changes in equity is now presented in place of the consolidated statement of recognized gains and loses that was previously required and in place of our reserves note.

SSAP 11 (Revised) prescribes the basis for the translation of foreign currency translations and financial statements. The principal impact of the revision of this SSAP on our consolidated financial statements is that the income statement of overseas subsidiaries is now translated into Renminbi at the exchange rates on the date of the transaction, or at an approximation thereto, whereas previously they were translated at the exchange rates at the balance sheet date. The adoption of the revised SSAP 11 has not had a material effect on our financial statements.

SSAP 15 (Revised) prescribes the revised format for the cash flow statement. The principal impact of the revision of this SSAP is that the consolidated cash flow statement now presents cash flows under three headings, cash flows from operating, investing and financing activities, rather than the five headings previously required. In addition, cash flows from overseas subsidiaries arising during the year are now translated into Renminbi at the exchange rates on the date of the transaction or at an approximation thereto, whereas previously they were translated at the exchange rate on the balance sheet date.

SSAP 34 prescribes the principles to be applied for recognition, measurement and disclosure for employee short-term and long-term benefits. In addition, disclosure is now required in respect of our share option scheme as detailed in note 29 to our consolidated financial statements. This share option scheme disclosure is similar to the Hong Kong Stock Exchange listing rules disclosure previously included in the report of the directors which are now required to be included in the notes to the financial statements as a consequence of the SSAP. The SSAP requirements have not had a material effect on the amounts previously recorded in the financial statements, therefore no prior year adjustment has been required.

The following two recently issued and revised accounting standards are effective for the 2003 financial year.

SSAP 12 (Revised) requires full provision for deferred taxes using the liability method. Under this new approach, the tax is calculated using tax rates expected to be in effect when the timing difference occurs. In prior periods, we provided deferred taxes for timing differences only to the extent that it was probable a liability or asset would crystallize in the foreseeable future. The new method of accounting for deferred income tax is similar to the method that has been used under U.S. GAAP. For the year ended December 31, 2002, there was no difference in the amount of deferred income tax we recognized under Hong Kong and U.S. GAAP. We do not believe the revised SSAP will have a significant impact on our financial position or results of operations under Hong Kong GAAP.

In addition to the SSAPs issued by the Hong Kong Society of Accountants, which affect our financial statements under Hong Kong GAAP, the U.S. Financial Accounting Standards Board implemented the Statement of Financial Accounting Standards No. 143, or SFAS No. 143, which relates to accounting for asset retirement obligations under U.S. GAAP. SFAS No. 143 requires that the fair value of a liability for an asset retirement obligation be recognized in the period in which it is incurred if a reasonable estimate of its fair value can be determined. The associated asset retirement costs must be capitalized as part of the carrying amount of the long-lived asset. This new practice also requires the liability to be discounted and the accretion expense to be recognized using the credit-adjusted risk-free interest rate in effect when the liability was initially recognized. The adoption of this statement will likely result in an increase in both our cost of assets and total amount of liabilities as presented under U.S. GAAP. We are currently assessing this new methodology and have not determined whether or the extent to which it will affect our financial statements.

THE PRC PETROLEUM INDUSTRY

The information in this offering memorandum relating to the PRC is derived from various government and private publications or obtained in communications with various PRC government agencies. This information has not been prepared or independently verified by us, the issuer, the initial purchasers or any of their respective affiliates or advisers. The information may not be consistent with other information compiled within or outside the PRC. Unless otherwise stated, statements regarding China do not apply to Hong Kong, Macau or Taiwan.

Overview

The PRC government views petroleum as an important strategic resource and since 1949 has adopted policies to develop its national petroleum industry. The PRC government made its first major onshore petroleum discovery in the Daqing oilfield in northeast China in 1959. This and other large onshore fields were more than sufficient for national consumption through the late 1970s, but as demand accelerated and production of key onshore fields declined, further exploration and development of reserves became important. China's offshore area and far western onshore region provided significant reserve potential, but initial exploration and development required foreign technology, expertise and capital. The State Council of China formed CNOOC in 1982 to conduct exploration and production in China's offshore areas, both independently and as the exclusive Chinese partner with foreign entities.

Since CNOOC's inception in 1982, China has experienced rapid economic growth, which has generated a strong increase in demand for petroleum and other primary energy sources. Between 1991 and 2001, China's gross domestic product, or GDP, increased at a compound real annual growth rate of 9.9%, making China one of the fastest growing economies in the world. During the same period, petroleum consumption increased at a compound annual growth rate of 5.7% and China's oil production grew at a compound annual growth rate of 1.6%. Since 1996, China has been a net importer of oil, further increasing the significance of exploration and development, and offshore activities have become critical to China's crude oil production.

There are three major oil and gas companies in China. We are the dominant offshore petroleum company in China. PetroChina Company Limited, or PetroChina, a subsidiary of China National Petroleum Corporation, is the largest petroleum company in China by reserve size and has the largest production capacity for oil and gas. PetroChina's assets and principal markets are focused in the northern and western regions of onshore China. PetroChina has been publicly listed since April 2000.

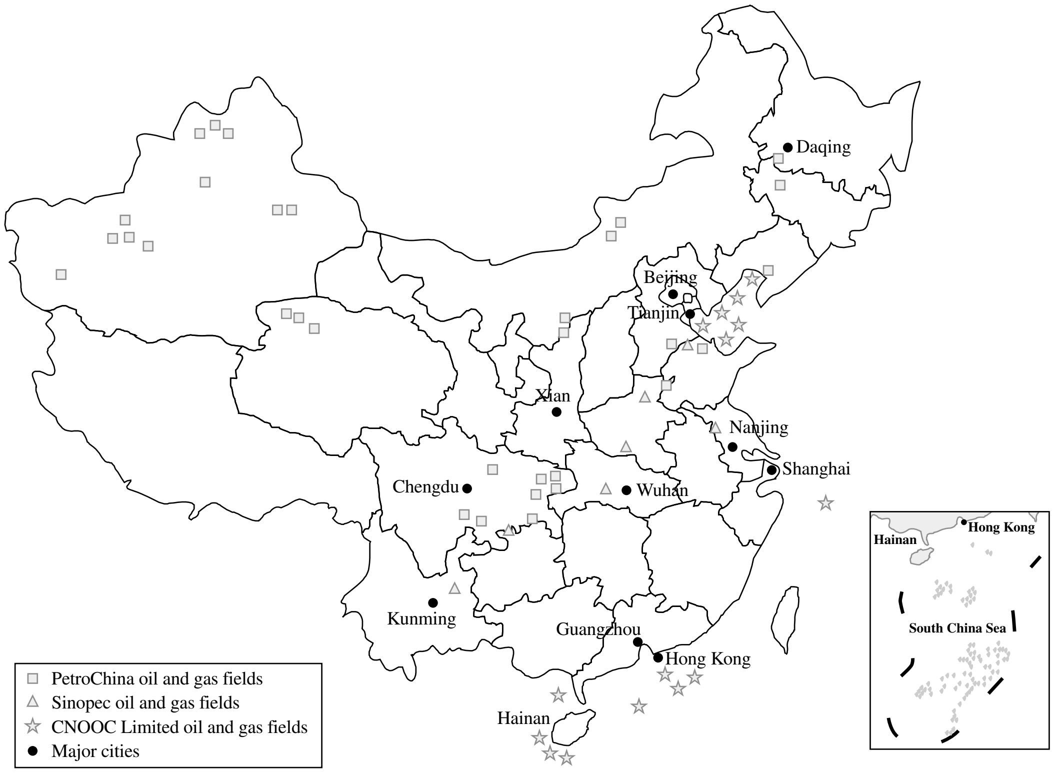
China Petroleum & Chemical Corporation, or Sinopec, is the second largest petroleum company in China by reserve size, with the largest refining, petrochemical, and marketing operations in the country. Sinopec's assets and principal markets are focused in the eastern, southern and central areas of onshore China. As the leading refiner in China, Sinopec has historically been our largest single domestic customer for crude oil, though we have the right to sell to any other customer, both domestic and abroad. Sinopec has been publicly listed since October 2000. A subsidiary of Sinopec is also engaged in offshore exploration and production.

The following table sets forth recent reserve and production levels for the three major petroleum companies of China:

Company	Net proved reserves as of December 31, 2002	Net production Year ended December 31, 2002	
		Crude oil	Natural Gas
	(million BOE)	(mmbbls/day)	(mmcf/day)
CNOOC Limited	2,016	299	273
PetroChina	17,406	2,109	1,658
Sinopec	3,875	739	490

Sources: PetroChina 2002 Annual Report, Sinopec 2002 Annual Report, CNOOC Limited 2002 Annual Report.

The following map highlights China's principal oil and gas exploration and production areas and the oil and gas fields for China's three largest petroleum companies:



Sources: PetroChina Prospectus, March 30, 2000, Sinopec Prospectus, October 12, 2000, and CNOOC Limited.

Petroleum Consumption

The rapid growth of China's economy in recent years has generated significant growth in the consumption of total primary energy in China. According to U.S. Energy Information Administration, China was the world's second largest consumer of primary energy and the third largest consumer of oil and gas products in 2000. Historically, coal has been the main source of primary energy in China. Driven by environmental and efficiency concerns, coal consumption as a percentage of total energy consumption decreased from 76.1% in 1991 to 67.0% in 2001, while crude oil and natural gas increased from 19.1% to 26.1% over the same period according to National Bureau of Statistics of China. Consumption of natural gas increased significantly between 1997 and 2001, at a compound annual growth rate of 8.9%. Despite such growing consumption, the oil and gas portion of primary energy consumed in 2000 was still far below the world average, especially for natural gas, which was only 3.1% of the total primary energy consumption. China's primary energy consumption on a per capita basis remains significantly lower than the top energy consumers in the world, especially with regard to oil and gas.

The following table lists some of the world's leading primary energy consuming countries in 2001 and includes their oil and gas consumption levels:

Country	Total primary energy consumed (BTU quadrillion)	Crude oil consumption (million BOE)	Crude oil consumption per capita (BOE)	Crude oil share of total consumption (%)	Natural gas share of total consumption (%)
USA	97.0	7,171.8	25.3	39.5%	23.9%
China	39.7	1,815.9	1.4	25.8%	3.1%
Russia	28.2	947.2	6.6	19.2%	51.6%
Japan	21.9	1,978.5	15.5	50.1%	13.5%
Germany	14.4	1,026.8	12.5	40.6%	22.8%
India	12.8	777.5	0.8	34.4%	6.5%
Canada	12.5	697.1	22.4	30.3%	23.6%
France	10.5	742.2	12.5	39.9%	15.3%
United Kingdom	9.8	626.3	10.5	35.2%	35.3%
Brazil	8.8	802.6	4.7	50.8%	4.0%
World total	403.9	28,150.6	4.6	38.7%	23.1%

Source: International Energy Annual 2001 by U.S. Energy Information Administration.

Petroleum Production

China's crude oil production grew at an annual compound rate of only 1.7% between 1990 and 2002, while its consumption grew at an annual compound rate of 5.8% over the same period. By 1996, China's total crude oil consumption exceeded its production, and the country became a net importer of crude oil. Natural gas production grew at a compound annual growth rate of 6.6% during the same period. The following table breaks down crude oil consumption, production, and net imports (exports) and natural gas production in China during this period:

Year	Crude oil		
	Domestic production	Net import (export)	Production of natural gas
	(in million tons)		(bcf)
1990	138.3	(21.1)	540.3
1991	141.0	(16.6)	567.5
1992	142.1	(10.2)	557.6
1993	145.2	(3.8)	592.2
1994	146.1	(6.2)	620.1
1995	150.1	(1.8)	633.9
1996	157.3	2.3	710.2
1997	160.7	15.6	801.6
1998	161.0	11.2	822.1
1999	160.2	29.4	889.9
2000	162.3	59.8	979.1
2001	164.8	52.7	1,177.6
2002	170.3	62.2	1,160.6

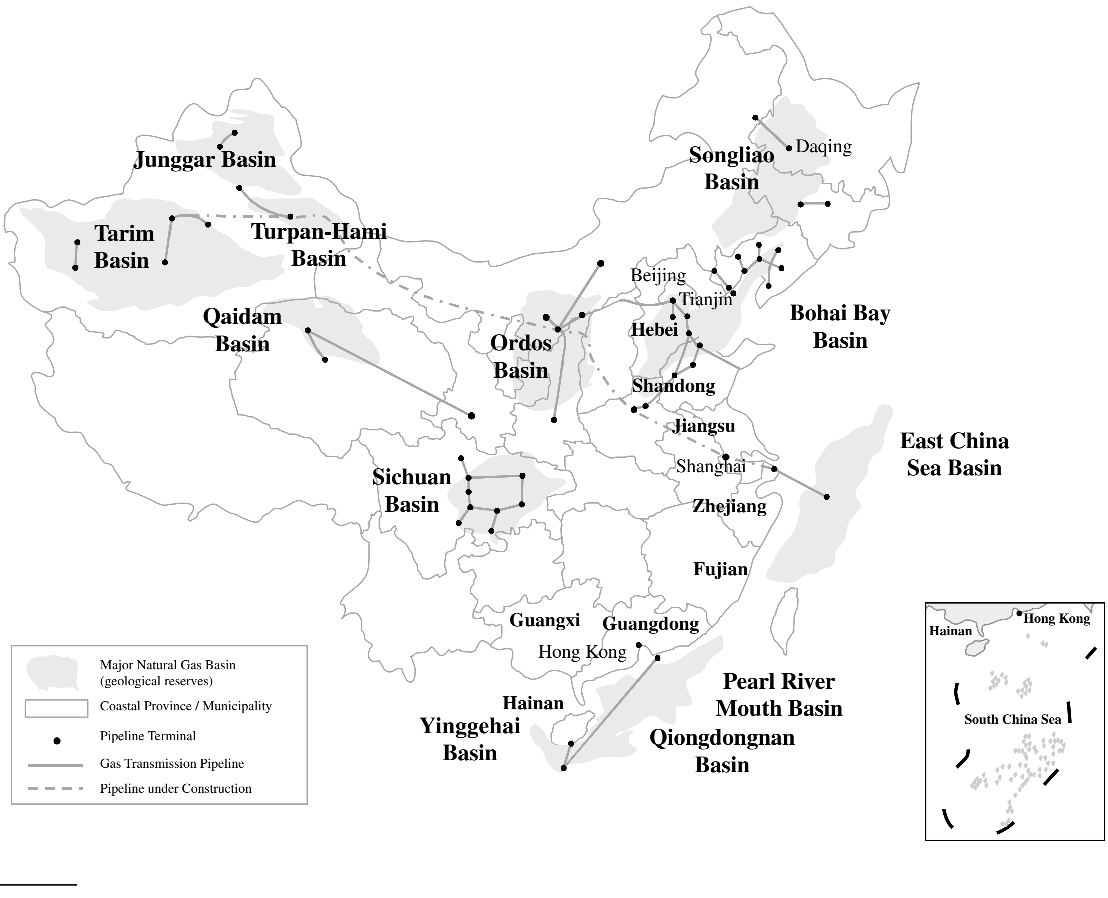
Sources: Petroleum and Chemical Statistical Digest, China OGP.

Natural Gas Market Development

The PRC government is promoting the development of natural gas as an important primary energy source, especially in the high-growth coastal areas. Natural gas accounted for approximately 3.0% of the PRC's primary energy consumption in 2000. This relatively low figure primarily results from China's historical reliance on coal and the lack of infrastructure needed to transport gas from gas fields to end users. The construction of natural gas infrastructure such as transmission pipelines often requires significant capital expenditures and time to complete. This is less of an issue when gas fields are close to areas of market demand. The largest potential natural gas market in China lies along its coastal region, the area with the highest forecast gas demand and the highest GDP growth rates. This region, including all coastal provinces, and Beijing, Tianjin and Shanghai municipalities, accounted for 66.3% of the country's GDP in 2001. This region's nominal GDP compound annual growth rate for 1998-2001 was the highest in China at 9.8% versus a national rate of 7.0%. According to the China Natural Gas Report (2002), published by China OGP of Xinhua News Agency, the coastal region is projected to have the largest share of natural gas demand in China over the next 10 years.

The PRC government has actively promoted the use of natural gas as an alternative fuel, particularly as a substitute for coal in power generation. Such efforts include granting royalty tax benefits for offshore gas production, and encouraging construction of gas transmission lines and natural gas-fired power plants. In addition to being more environmentally friendly, natural gas-fired power plants burn a more energy-efficient fuel, have lower capital development costs, and provide greater load flexibility. In 1999, natural gas accounted for only 0.2% of fuel consumed by China's power plants. The PRC State Power Corporation estimates it will grow to 5% by 2010.

According to China Natural Gas Report (2002), natural gas consumption in China is expected to grow at a compound annual growth rate of 17.1% between 2001 and 2010 reaching 4,065 billion cubic feet in 2010, while domestic China's total gas production is expected to reach 3,418 billion cubic feet. This would result in an approximately 15.9% projected shortfall in supply. Despite planned developments of national natural gas reserves and transmission infrastructure, a predicted shortfall in long-term gas supply has resulted in the consideration and planning of liquefied natural gas import projects. CNOOC is currently engaged in a project to build China's first liquefied natural gas import facility in Guangdong Province. CNOOC has granted us an option to acquire all of CNOOC's investment in the project. In addition, CNOOC plans to develop another liquefied natural gas import project in Fujian Province. See "Business—Natural Gas Business."



Sources: China Natural Gas Report (2002) by China OGP.

Our three major gas reserves basins are located in the Western South China Sea near Hainan Province and Hong Kong, in the Bohai Bay near Shandong Province and Tianjin, and the East China Sea near Shanghai. We have already constructed approximately 1,400 kilometers of gas pipelines to transport our gas to Hong Kong, Shanghai, Tianjin and other coastal cities. For a further discussion of our gas reserves, production and strategy, see "Business."

PetroChina holds the PRC's largest percentage of natural gas proved reserves. However, with the exception of the Songliao Basin in northeast China, its major natural gas fields are located far from the coastal region of China. The Sichuan Basin is in Sichuan Province, the Ordos Basin is in Inner Mongolia, and the large Tarim Basin is in Xinjiang Uygur Autonomous Region. PetroChina has developed the gas markets adjacent to several of its key fields by constructing over 13,391 kilometers of gas pipelines. However, at present, there is no national transmission link from these large reserves to the east and south coasts of China. In 2002, a joint venture was formed to construct and operate a 4,000 kilometer west-to-east natural gas pipeline, originating in Tarim Basin in Xinjiang Uygur Autonomous Region and terminating in Shanghai, running through the provinces Gansu, Shaanxi, Shanxi, Henan, Anhui, Jiangsu and the Ningxia Hui Autonomous Region. PetroChina holds a 50% interest in the joint venture and is the single largest shareholder. An international consortium consisting of Royal Dutch Shell, Gasprom and ExxonMobil holds a 45% interest and Sinopec holds the remaining 5% interest. The pipeline will be developed in two phases. The first phase, comprised of the 1,516-kilometer eastern section which links Jingbian and Shanghai, commenced construction in 2002 and is expected to commence operations by the end of 2003. The second phase, comprising of the remainder of the pipeline or the western section, is expected to complete construction and commence operation in 2005.

Sinopec has less remaining recoverable natural gas reserves than us or PetroChina. Based on China Natural Gas Report (2002), as of December 31, 2001, Sinopec had 162 billion cubic meters remaining recoverable natural gas reserves, compared to 1,588 billion cubic meters for PetroChina and 188 billion cubic meters for us.

Regulatory Framework

Government Control

The PRC government owns all of China's petroleum resources and exercises regulatory control over petroleum exploration and production activities in China. Prior to March 2003, we were required to obtain various governmental approvals, including those from the Ministry of Land and Resources, the State Administration for Environmental Protection, the State Development and Planning Commission and the Ministry of Foreign Trade and Economic Cooperation before we were permitted to conduct production activities. For joint exploration and production with foreign enterprises, we were required to obtain various governmental approvals, through CNOOC, including those from:

- the Ministry of Land and Resources, for a permit for exploration blocks, an approval of a geological reserve report submitted through CNOOC and an exploration permit for the approved blocks;

- the Ministry of Land and Resources or the State Development and Planning Commission to designate such blocks as an area for foreign cooperation;

- the Ministry of Foreign Trade and Economic Cooperation for the production sharing contracts between CNOOC and the foreign enterprises;

- the State Administration for Environmental Protection for an environmental impact report submitted through CNOOC;

- the State Development and Planning Commission for an overall development plan submitted through CNOOC; and

- the Ministry of Land and Resources, for an extraction permit.

Although our sales were coordinated by the State Development and Planning Commission, historically we have been given flexibility to sell our crude oil based on the international spot price and to determine where we sell our crude oil.

Since the conclusion of the meeting of the National People's Congress in March 2003, the PRC government has undergone substantial reform. The State Development and Planning Commission has been replaced by the State Development and Reform Commission. The latter's mission is to propose economic and social development policy and provide guidance to the various government ministries on reform of the overall economic structure. The State Economic and Trade Commission and the Ministry of Foreign Trade and Economic Cooperation have been replaced by the Ministry of Commerce, whose functions include regulating the domestic market, attracting foreign investment, and providing assistance to domestic companies competing overseas. The newly formed State Asset Commission is expected to exercise certain functions formerly held by the State Economic and Trade Commission. The functions of these new administrative bodies remain unclear, but it is believed that market-oriented reforms will continue.

Special Policies Applicable to the Offshore Petroleum Industry in China

Since the early 1980s, the PRC government has adopted policies and measures to encourage the development of the offshore petroleum industry. These policies and measures, which were applicable to CNOOC's operations prior to the reorganization, became applicable to our operations in accordance with an undertaking agreement between us and CNOOC. As approved by the relevant PRC government authorities, including the Ministry of Land and Resources and the Ministry of Foreign Trade and Economic Cooperation, these policies and measures have provided us with the following benefits:

- the exclusive right to explore for, develop and produce petroleum offshore China in cooperation with international oil and gas companies and to sell this petroleum in China;

- the flexibility to set our prices in accordance with international market prices and determine where to sell our crude oil, with only minimal supervision from the PRC government;

- a favorable 5% production tax on the crude oil and natural gas we produce both independently and under production sharing contracts, rather than the 17% rate generally applicable to the independent production of domestic petroleum companies in China; and

- production from one of our major gas fields, Yacheng 13-1, is exempt from the PRC royalties under an approval by the State Tax Bureau in May 1989 and the 5% production tax applicable to the oil and gas produced under other production sharing contracts in accordance with an approval by the Ministry of Finance in August 1985. Our natural gas revenues from Yacheng 13-1 for the six years ended December 31, 1997, 1998, 1999, 2000, 2001 and 2002 represented approximately 8.7%, 12.5%, 10.4%, 6.7%, 7.3% and 5.6%, respectively, of our total oil and natural gas sales in those years.

Although we historically have benefited from the foregoing special policies, we cannot assure you that such policies will continue in the future. We are also regulated by the PRC government in various other aspects of our business and operations, including required government approvals for new independent exploration and production projects and new production sharing contracts. For a further discussion of ways in which we are regulated by the PRC government, see "—Government Control."

Policies Applicable to International Oil and Gas Companies Operating in Offshore China

The PRC government encourages foreign participation in offshore petroleum exploration and production through exclusive cooperation with CNOOC. In 1982, the State Council promulgated the Regulation of the People's Republic of China on Exploitation of Offshore Petroleum Resources in Cooperation with Foreign Enterprises, which grants to CNOOC the exclusive right to enter into joint cooperation arrangements with foreign enterprises for offshore petroleum exploration and production. From 1982 to 2000, CNOOC successfully completed several rounds of bidding for offshore petroleum exploration and production projects, and many international oil and gas companies have been involved and awarded exploration blocks for joint exploration, development and production with CNOOC.

In October 2001, the State Council amended the regulation referred to above as a part of the comprehensive review of all business laws and regulations by the Chinese government to ensure their compliance with its WTO commitments. The amendment revised such terms in the law governing offshore exploration as restrictive provisions on technology transfers and domestic components requirements in procurement. The removal of these restrictions will provide a level playing field for all oilfield service contractors, domestic or international. These amendments are expected to benefit CNOOC's businesses as well as our exploration and production business and further increase production sharing contract activities offshore China. CNOOC will continue to enjoy the exclusive right to conduct production sharing contract activities with foreign contractors and is entitled to all rights and privileges under the previous regulation. The regulation also states that CNOOC, as a state-owned enterprise, is to be in charge of all efforts to exploit petroleum resources with contractors in Chinese waters. Currently, international oil and gas companies can only undertake offshore petroleum exploration and production activities in China after they have entered into a production sharing contract with CNOOC.

THE ISSUER

The issuer, our wholly owned subsidiary, was incorporated as an international business company with limited liability on April 2, 2003 in the British Virgin Islands under the International Business Companies Act. The issuer's registration number is 540274. Its registered office is located at Romasco Place, Wickhams Cay 1, P.O. Box 3140, Road Town, Tortola, British Virgin Islands. Under section 4(1) of the issuer's memorandum of association, the issuer may engage in any act or activity that is not prohibited under any law for the time being in force in the British Virgin Islands. The issuer's primary purpose is to act as one of our financing subsidiaries. The issuer will remain our wholly owned subsidiary as long as the notes are outstanding and will advance the net proceeds of the notes to us or our subsidiaries. The issuer has no material assets.

We are the sole director of the issuer. Further information on the particulars and experience of our directors is set forth in "Management."

The authorized share capital of the issuer is US$1,000, divided into 1,000 ordinary shares of US$1.00 par value each, all of which are issued and outstanding. No part of the equity securities of the issuer is listed or dealt on any stock exchange and no listing or permission to deal in such securities is being or is proposed to be sought. The issuer does not have any assets or liabilities other than its paid-in capital and the notes now being issued. The issuer has no subsidiaries.

The issuer has not published, and does not propose to publish, any of its accounts since it is not required to do so under the laws of the British Virgin Islands. However, the issuer is required to keep such accounts and records as its director considers necessary or desirable in order to reflect the financial position of the issuer.

BUSINESS

Overview

We are an oil and gas company engaged in the exploration, development, production and sale of crude oil and natural gas primarily offshore China. We are the dominant producer of crude oil and natural gas offshore China and the only company permitted to conduct exploration and production activities with international oil and gas companies offshore China. As of December 31, 2002, we had estimated net proved reserves of 2,015.8 million BOE, comprised of 1,424.4 million barrels of crude oil and condensate and 3,547.9 billion cubic feet of natural gas. For the year 2002, our net production averaged 298,625 barrels per day of crude oil, condensate and natural gas liquids and 272.6 million cubic feet per day of natural gas, which together totaled 346,639 BOE per day.

Our net proved reserves increased from 668 million BOE as of December 31, 1995 to 2,015.8 million BOE as of December 31, 2002, which represents a compound annual growth rate of 17.1%. Based on net proved reserves, we are one of the largest independent oil and gas exploration and production companies in the world. In the petroleum industry, an "independent" company owns oil and gas reserves independently of other downstream assets, such as refining and marketing assets, whereas an integrated company owns downstream assets in addition to oil and gas reserves. As of December 31, 2002, approximately 60.6% of our net proved reserves were classified as net proved undeveloped. We plan to spend approximately US$2.7 billion developing our reserves offshore China and approximately US$308 million for independent exploration offshore China from 2003 through 2004.

We conduct exploration, development, production and sale activities through both independent operations and production sharing contracts with foreign partners. We have added to our reserves in recent years primarily through our independent operations. As of December 31, 2002, independent properties accounted for approximately 53.2% of our total net proved reserves and approximately 56.0% of our total net proved undeveloped reserves. We are the operator of all of our independent producing properties. For the year ended December 31, 2002, production from our independent properties accounted for 46.3% of total net production.

Through our parent company, CNOOC, we have the exclusive right to enter into contracts with international oil and gas companies to conduct exploration and production activities offshore China. Under these production sharing contracts, we have the sole right to acquire, at no cost, up to a 51% participating interest in any successful discovery offshore China made by our foreign partners. Our foreign partners can recover their exploration costs under the production sharing contracts only if a commercially viable discovery is made. As of December 31, 2002, we had approximately 28 foreign partners under our production sharing contracts offshore China, all of which are international oil and gas companies, including Agip, BP, Burlington Resources, ChevronTexaco, ConocoPhillips, Devon Energy, Husky, Kerr-McGee, Newfield Exploration and Royal Dutch Shell. As of December 31, 2002, we were a party to 31 production sharing contracts and one joint study agreement. We are currently the operator or joint operator of most of the properties developed under our production sharing contracts. In the early years of our existence, we conducted most of our activities through production sharing contracts. Production sharing contracts have enabled us to develop technical and management expertise and provided us with the cash flows necessary to increase our independent exploration and production activities.

Natural gas is becoming an increasingly important part of our business strategy because of rapidly growing domestic demand. In view of the domestic natural gas supply shortfall forecasted by the Chinese government, we have continued to develop our natural gas reserves and invested in liquefied natural gas related upstream projects outside the PRC. We continue to explore for natural gas and develop natural gas properties. We have acquired interests in gas reserves located in Tangguh, Indonesia and entered into an agreement to acquire interests in gas reserves located in the North West Shelf of Australia. In addition, CNOOC has granted us an option to invest in liquefied natural gas projects or other natural gas related businesses in the PRC in which CNOOC has invested or proposes to invest, including an option for us to acquire CNOOC's 33% interest in a liquefied natural gas terminal being constructed in Guangdong Province, China. Furthermore, in connection with this option, CNOOC will at its own expense procure all necessary PRC government approvals needed for our participation in the related projects or businesses.

On April 19, 2002, we completed the acquisition of Repsol YPF, S.A.'s interest in a portfolio of oil and gas production sharing and technical assistance contracts in areas located offshore and onshore Indonesia. The acquisition was implemented retroactively from January 1, 2002. Under the terms of the acquisition, we paid a consideration of US$585 million, subject to a final oil price adjustment. See note 5 to our consolidated financial statements beginning on page F-1. The assets include a 65.3% interest in the South East Sumatra production sharing contract, a 36.7% interest in the Offshore North West Java production sharing contract, a 25.0% interest in the West Madura production sharing contract, a 50.0% interest in the Poleng technical assistance contract and a 16.7% interest in the Blora production sharing contract.

CNOOC, our parent company and controlling shareholder, was formed in 1982 when the Regulations of the People's Republic of China on Exploitation of Offshore Petroleum Resources in Cooperation with Foreign Enterprises gave CNOOC the exclusive right to enter into production sharing contracts with foreign partners to conduct exploration and production activities offshore China. As a result of CNOOC's October 1999 reorganization, we became the only entity through which CNOOC engages in the upstream petroleum business. CNOOC continues to perform administrative functions relating to our upstream petroleum business. For further details regarding this reorganization, see "Relationship with CNOOC and Certain Related Party Transactions."

Competitive Strengths

We believe that our historical success and future prospects are directly related to a combination of our strengths, including the following:

- large proved reserve base with significant exploitation opportunities;
- sizable operating area with demonstrated exploration potential;
- successful independent exploration and development record;
- competitive cost structure;
- reduced risks and access to capital and technology through production sharing contracts;
- strategic position in China's growing natural gas markets; and
- experienced management team.

Large proved reserve base with significant exploitation opportunities. Based on net proved reserves as of December 31, 2002 and average net daily production for the year ended December 31, 2002, we had a reserve-to-production ratio of approximately 15.9 years. As of December 31, 2002, approximately 60.6% of our net proved reserves were classified as net proved undeveloped. We expect our production to grow significantly as these undeveloped properties begin producing.

Sizable operating area with demonstrated exploration potential. The offshore China exploration area is approximately 1.3 million square kilometers in size, about twice as large as the U.S. Gulf of Mexico exploration area. As of December 31, 2002, a total of 797 exploration wells had been drilled offshore China. Only limited exploration has been conducted in prospective natural gas regions of the Western South China Sea and the East China Sea. Since CNOOC's inception in 1982 to the end of 2002, a total of 674 exploration wells have been drilled offshore China, including 430 wildcat wells with a success rate of approximately 37.5%. Between the beginning of 1999 and December 31, 2002, we made 15 discoveries and foreign parties made 15 discoveries offshore China.

Successful independent exploration and development record. From the inception of CNOOC in 1982 to December 31, 2002, we achieved a success rate of approximately 50% on our 177 offshore China independent wildcat wells, while our foreign partners achieved a success rate of approximately 29% on their 253 offshore China wildcat wells. Reserve additions from independent operations have accounted for approximately 67% of our total reserve additions offshore China since the beginning of 1997. Between late 1995 and the end of 2002, we completed seven of our major independent development projects on time and under budget.

Competitive cost structure. For the year ended December 31, 2002, our total offshore China lifting costs were US$3.92 per BOE. Total lifting costs for independent operations offshore China were US$3.89 per BOE during the same period. Lifting costs consist of operating expenses and production taxes. We have kept our offshore China lifting costs low through various measures including more efficient use of existing offshore facilities, the linking of employee bonuses to cost reduction and the adoption of new technology in our operations. Our average finding and development cost for the three years ended December 31, 2002 was US$4.59 per BOE, or US$4.54 per BOE as adjusted for the estimated future costs of developing proved undeveloped reserves. We believe that this cost structure allows us to compete effectively even in a low crude oil price environment.

Reduced risks and access to capital and technology through production sharing contracts. Production sharing contracts help us minimize our offshore China finding costs, exploration risks and capital requirements because our foreign partners are responsible for all costs associated with exploration. Our foreign partners recover their exploration costs only if a commercially viable discovery is made.

Strategic position in China's growing natural gas markets. The proximity of our natural gas reserves to the major demand areas in the coastal regions of China provides us with a competitive advantage over other natural gas suppliers in China, whose natural gas reserves are located primarily in northwest and southwest China. We have natural gas fields near many of China's rapidly growing coastal areas, including Hong Kong, Shanghai and Tianjin. We have also acquired interests in gas reserves located in Tangguh, Indonesia and entered into an agreement to acquire interests in gas reserves located in the North West Shelf of Australia. In addition, CNOOC has granted us an option to invest in liquefied natural gas projects or other natural gas related businesses in the PRC in which CNOOC has invested or proposes to invest, which includes an option to acquire CNOOC's interest in a liquefied natural gas terminal in Guangdong Province, China. For further information, see "—Natural Gas Business."

Experienced management team. Our senior management team has extensive experience in the oil and gas industry, and most of our executives have been with the CNOOC group since its inception in 1982. We evolved from a company heavily reliant on production sharing contracts with foreign partners to a company with a balance of both independent and production sharing contract operations. Our management team and staff have had the opportunity to work closely with foreign partners both within and outside China. We have implemented international management practices including incentive compensation schemes for our employees. In addition, we have adopted a share option scheme for our employees. See "Management—Share Option Scheme."

Business Strategy

We intend to continue expanding our oil and gas exploration and production activities and, where appropriate, to continue making strategic investments in natural gas businesses. While our expansion strategy will continue to focus primarily on offshore China, we may also consider overseas acquisition opportunities that may be presented to us. The principal components of our strategy are as follows:

- increase production primarily through the development of our net proved undeveloped reserves;
- add to our reserves through independent exploration and production sharing contracts;
- capitalize on the growing demand for natural gas in China;
- selectively pursue acquisitions to ensure long-term production growth, geographical reserves risk diversification, and to further our natural gas strategy;
- maintain operational efficiency and low production costs; and
- maintain financial flexibility through conservative financial practices.

Increase production primarily through the development of our net proved undeveloped reserves. As of December 31, 2002, approximately 60.6% of our proved reserves were classified as net proved undeveloped, which gives us the opportunity to achieve substantial production growth even without additional reserve discoveries, assuming that we will be able to develop these reserves more quickly than we deplete our currently producing reserves. We are currently undertaking a number of large development projects located primarily in the Bohai Bay and the Western South China Sea, which will substantially increase production. We plan to spend approximately US$2.7 billion from 2003 through the year 2004 to develop our net proved undeveloped reserves offshore China.

Add to our reserves through independent exploration and production sharing contracts. We plan to concentrate our independent exploration efforts in existing operating areas with a particular emphasis on natural gas. We plan to spend approximately US$308 million from 2003 through 2004 on independent exploration activities. We plan to augment independent exploration efforts and reduce capital requirements and exploration risks by continuing to enter into production sharing contracts with foreign partners. We currently have identified 23 drilling prospects. In 2003, we plan to drill approximately 33 exploration wells, acquire approximately 16,100 kilometers of 2D seismic data and acquire approximately 1,180 square kilometers of 3D seismic data independently. Our foreign partners under existing production sharing contracts plan to drill approximately 10 to 11 exploration wells, acquire approximately 1,500 kilometers of 2D seismic data and acquire approximately 923 square kilometers of 3D seismic data in 2003.

Capitalize on the growing demand for natural gas in China. The Chinese government forecasts significant growth in domestic natural gas demand and has promoted the use of natural gas as a clean and more efficient fuel. We plan to capitalize on this growth potential through the following initiatives:

- continue to develop natural gas fields and focus independent exploration efforts on natural gas;
- evaluate whether to exercise the option to invest in the planned Guangdong liquefied natural gas project; and
- evaluate investment opportunities in related natural gas businesses that will help develop markets for our natural gas production.

To the extent we invest in businesses and geographic areas where we have limited experience and expertise, we plan to structure our investments as alliances or partnerships with parties possessing the relevant experience and expertise.

Selectively pursue acquisitions to ensure long-term production growth, geographical reserves risk diversification, and to further our natural gas strategy. We plan to make selective acquisitions that will meet one or more of our strategic objectives of enhancing our production profile, diversifying our reserve base and geographic risk profile and furthering our natural gas strategy. In addition, we evaluate acquisition opportunities based on our expected economic return criteria. In April 2002, we completed the acquisition of certain Indonesian assets from Repsol YPF. These assets increased our near term production and leveraged our expertise and experience in offshore oil and gas activities. We have also completed an acquisition of the equivalent of a 12.5% interest in Indonesia's Tangguh LNG Project in January 2003 and have signed a key terms agreement to acquire an aggregate interest of approximately 5.56% in the reserves and upstream production of Australia's North West Shelf Project. We believe these upstream acquisitions of gas reserves will enhance our natural gas strategy by facilitating the supply of LNG to China's rapidly growing coastal gas market as well as provide us with access to other gas-rich basins for further growth opportunities.

Maintain operational efficiency and low production costs. We will continue to maintain our low cost structure and operational efficiency through the following initiatives:

- Apply up-to-date drilling, production and offshore engineering technology to our operations through our oilfield service providers; this technology includes long-range extension wells, multilateral wells, advanced formation testing, multi-phase transmission, monolayer pipeline and subsea technology, minimal structure techniques and suction foundation technology;

- Proactively manage service contracts and cooperate with our oilfield service providers to improve exploration efficiency and reduce exploration costs; this measure includes using operational techniques such as cluster drilling, which reduces drilling time by one-third and lowers the related costs by up to 40%; and

- Maintain high production volume levels on an individual well basis and increase the productivity of producing wells.

Maintain financial flexibility through conservative financial practices. We will continue to emphasize conservative financial management practices. Currently, we have a strong financial profile with a low leverage ratio. We intend to maintain our financial strength by managing key measures such as capital expenditures, cash flows and fixed charge coverage. We intend to actively manage our accounts receivable and inventory positions to enhance liquidity and improve profitability. We will continue to monitor our foreign currency denominated debt and to minimize our exposure to foreign exchange rate fluctuations.

Exploration and Production

Summary

We currently conduct exploration, development and production activities primarily in four areas offshore China:

- the Bohai Bay;
- the Western South China Sea;
- the Eastern South China Sea; and
- the East China Sea.

In addition, we hold several equity interests in oil and gas properties in Indonesia, including a 39.5% participating interest in a production sharing contract in the Malacca Strait, interests in production sharing contracts and a technical assistance contract we acquired from Repsol YPF in April 2002 and interests in the Tangguh LNG Project, which we recently acquired. We also expect to complete an acquisition for natural gas reserves offshore Australia by the end of 2003. See "—Overseas Activity," "—Natural Gas Business—Overseas Activity" and "Management's Discussion and Analysis of Financial Condition and Results of Operations—Acquisitions and Overseas Activities."

As of December 31, 2002, we had estimated net proved reserves of 2,015.8 million BOE, comprised of 1,424.4 million barrels of crude oil and condensate and 3,547.9 billion cubic feet of natural gas. As of December 31, 2002, we had interests in 25 producing properties and 29 properties under development and appraisal offshore China. We are the operator or joint operator of 21 oil and gas properties under production. In 2002, three properties offshore China commenced production. For the year 2002, net production averaged 298,625 barrels per day of crude oil, condensate and natural gas liquids and 272.6 million cubic feet per day of natural gas, which together totaled 346,639 BOE per day, representing a 32.6% increase over the annual average daily production for the year 2001.

We conduct our exploration, development and production activities independently as well as through production sharing contracts and geophysical survey agreements with foreign partners. A production sharing contract contains provisions regarding the exploration, development, production and operation of an oil and gas field and the formula through which foreign partners may recover exploration, development and production costs and share in the production after the successful development of petroleum reserves. See "—Production Sharing Contracts—Offshore China" for a detailed discussion of these arrangements.

We also conduct exploration efforts through geophysical survey agreements with foreign companies. These geophysical survey agreements allow international oil and gas companies to conduct geophysical studies before deciding whether to negotiate a production sharing contract with CNOOC. If a foreign partner decides to enter into a production sharing contract with CNOOC, the costs and expenses that the foreign partner incurs in conducting geophysical exploration may be recovered in the production period by the foreign partner, subject to our confirmation. See "—Geophysical Survey Agreements" for a detailed discussion of these arrangements. As of December 31, 2002, we were not a party to any geophysical survey agreements, although we may enter such agreements in the future.

The offshore China exploration area is approximately 1.3 million square kilometers in size. We currently have the exclusive right to operate independently or in conjunction with international oil and gas companies in approximately 601,700 square kilometers of the total offshore China exploration area. We currently have rights to operate independently or in conjunction with international oil and gas companies in 133 exploration blocks covering approximately 572,486 square kilometers. We have access to approximately 822,700 kilometers of 2D seismic data and approximately 33,700 square kilometers of 3D seismic data. From the beginning of CNOOC's operations in 1982 to December 31, 2002, a total of 674 exploration wells have been drilled, including 430 wildcat wells, with a success rate of approximately 37.5%. During this period we achieved a success rate of approximately 50% on 177 exploration wildcat wells which were drilled independently, while foreign partners achieved a success rate of approximately 29% on their 253 exploration wildcat wells.

Oil and Natural Gas Reserves

We have a large base of net proved undeveloped reserves as a result of our exploration successes. As of December 31, 2002, approximately 60.6% of net proved reserves were classified as net proved undeveloped. We are currently undertaking a number of large development projects located primarily in the Bohai Bay and the Western South China Sea and expect these projects to substantially increase our production.

Our net proved reserves consist of our percentage interest in total reserves, comprised of (i) our 100% interest in our independent oil and gas properties (excluding the proved reserves attributable to our associated company), (ii) our participating interest in the properties covered under our production sharing contracts in the PRC and Indonesia, and (iii) our 30% interest in the proved reserves of our associated company, less (i) an adjustment for our share of royalties payable to the PRC government under our production sharing contracts in the PRC, (ii) an adjustment for production allocable to foreign partners under our production sharing contracts in the PRC as reimbursement for exploration expenses attributable to our working interest, and (iii) adjustments for share oil payable under our Indonesian production sharing contracts to Pertamina, the Indonesian state-owned oil and gas company, and for a domestic market obligation under which the contractor must sell a specified percentage of its crude oil to the local Indonesian market at a reduced price. Net proved reserves do not include any deduction for production taxes, which are included in our operating expenses. Net production is calculated in the same way as net proved reserves.

We explore for and develop our reserves offshore China under exploration and production licenses granted by the PRC government. The PRC government generally grants exploration licenses for individual blocks while production licenses generally are granted for individual fields. We have production licenses for all of our proved reserves.

At our request, Ryder Scott Company, an independent petroleum engineering consultant, evaluated our selected properties as of December 31, 2000, 2001 and 2002. The Ryder Scott Company summary report describing its procedures and conclusions as of December 31, 2002 appears as Appendix A to this offering memorandum. For further information regarding our reserves, see "Risk Factors—Risks relating to our business—The oil and gas reserve estimates in this offering memorandum may require substantial revision as a result of future drilling, testing and production."

The following tables set forth net proved crude oil reserves, net proved natural gas reserves and total net proved reserves, as of the dates indicated, for our independent and production sharing contract operations in each of our operating areas.

Total Net Proved Crude Oil Reserves
(mmbbls)

	As of December 31,		As of December 31, 2002		
	2000	2001	Developed	Undeveloped	Total
Offshore China					
Independent					
Bohai Bay	675.7	589.9	296.6	211.2	507.8
Western South China Sea	76.4	71.7	47.9	60.5	108.4
Eastern South China Sea	—	—	—	—	—
East China Sea	4.5	12.4	2.8	9.7	12.5
Total	756.6	674.0	347.3	281.4	628.7
Production Sharing Contracts					
Bohai Bay	248.2	371.4	84.5	400.2	484.7
Western South China Sea	64.7	59.9	51.1	0.9	52.0
Eastern South China Sea	136.8	132.2	58.9	61.4	120.3
East China Sea	—	—	—	—	—
Total	449.7	563.5	194.5	462.5	657.0
Combined					
Bohai Bay	923.9	961.3	381.1	611.4	992.5
Western South China Sea	141.1	131.6	99.0	61.4	160.4
Eastern South China Sea	136.8	132.2	58.9	61.4	120.3
East China Sea	4.5	12.4	2.8	9.7	12.5
Total	1,206.3	1,237.5	541.8	743.9	1,285.7
Overseas(1)					
Indonesia	9.5	8.4	114.9	23.8	138.7
Total	9.5	8.4	114.9	23.9	138.7
Total	1,215.8	1,245.9	656.7	767.7	1,424.4

(1) We do not conduct independent overseas operations. Our overseas operations are conducted through production sharing contracts and technical assistance contracts.

Total Net Proved Natural Gas Reserves
(bcf)

	As of December 31,		As of December 31, 2002		
	2000	2001	Developed	Undeveloped	Total
Offshore China					
Independent					
Bohai Bay	591.4	598.9	182.1	342.1	524.2
Western South China Sea	1,773.6	1,809.2	17.5	1,936.7	1,954.2
Eastern South China Sea	—	—	—	—	—
East China Sea	65.3	197.0	42.1	137.3	179.4
Total	2,430.3	2,605.1	241.7	2,416.1	2,657.7
Production Sharing Contracts					
Bohai Bay	—	30.2	—	74.5	74.5
Western South China Sea	819.4	612.3	482.0	75.0	557.0
Eastern South China Sea	—	—	—	42.8	42.8
East China Sea	—	—	—	—	—
Total	819.4	642.5	482.0	192.2	674.2
Combined					
Bohai Bay	591.4	629.1	182.1	416.6	598.6
Western South China Sea	2,593.0	2,421.5	499.6	2,011.5	2,511.2
Eastern South China Sea	—	—	—	42.8	42.8
East China Sea	65.3	197.0	42.1	137.3	179.4
Total	3,249.7	3,247.6	723.7	2,608.3	3,332.0
Overseas(1)					
Indonesia	—	—	101.5	114.4	216.0
Total	—	—	101.5	114.4	216.0
Total	3,249.7	3,247.6	825.2	2,722.7	3,547.9

(1) We do not conduct independent overseas operations. Our overseas operations are conducted through production sharing contracts and technical assistance contracts.

Total Net Proved Reserves
(million BOE)

	As of December 31,		As of December 31, 2002		
	2000	**2001**	**Developed**	**Undeveloped**	**Total**
Offshore China					
Independent					
Bohai Bay	774.2	689.7	326.9	268.3	595.2
Western South China Sea	372.0	373.3	50.9	383.3	434.1
Eastern South China Sea	—	—	—	—	—
East China Sea	15.4	45.2	9.9	32.5	42.4
Total	1,161.6	1,108.2	387.6	684.1	1,071.7
Production Sharing Contracts					
Bohai Bay	248.2	376.5	84.6	412.6	497.1
Western South China Sea	201.3	161.8	131.4	13.4	144.8
Eastern South China Sea	136.8	132.2	58.9	68.6	127.5
East China Sea	—	—	—	—	—
Total	586.3	670.5	274.9	494.5	769.4
Combined					
Bohai Bay	1,022.4	1,066.2	411.5	680.9	1,092.3
Western South China Sea	573.3	535.1	182.3	396.6	578.9
Eastern South China Sea	136.8	132.2	58.9	68.6	127.5
East China Sea	15.4	45.2	9.9	32.5	42.4
Total	1,747.9	1,778.7	662.5	1,178.5	1,841.0
Overseas[1]					
Indonesia	9.5	8.4	131.8	42.9	174.7
Total	9.5	8.4	131.8	42.9	174.7
Total	1,757.4	1,787.1	794.3	1,221.5	2,015.8

(1) We do not conduct independent overseas operations. Our overseas operations are conducted through production sharing contracts and technical assistance contracts.

Oil and Natural Gas Production

The following tables show average daily net oil production, net natural gas production, and average net total production for the periods indicated. Oil production comprises crude oil, condensate and natural gas liquids.

Average Daily Net Production of Crude Oil
(bbls per day)

	Year ended December 31,		
	2000	**2001**	**2002**
Offshore China			
Independent			
Bohai Bay	63,797	97,612	110,989
Western South China Sea	45,828	40,377	35,724
Eastern South China Sea	—	—	—
East China Sea	3,557	3,967	3,223
Total	113,182	141,956	149,936
Production Sharing Contracts			
Bohai Bay	—	2,366	16,767
Western South China Sea	606	900	21,186
Eastern South China Sea	90,097	81,404	73,792
East China Sea	—	—	—
Total	90,703	84,670	111,745
Combined			
Bohai Bay	63,797	99,978	127,756
Western South China Sea	46,434	41,277	56,910
Eastern South China Sea	90,097	81,404	73,792
East China Sea	3,557	3,967	3,223
Total	203,885	226,626	261,681
Overseas(1)			
Indonesia	2,462	2,247	36,944
Total	2,462	2,247	36,944
Total	206,347	228,873	298,625

(1) We do not conduct independent overseas operations. Our overseas operations are conducted through production sharing contracts and technical assistance contracts.

Average Daily Net Production of Natural Gas
(mmcf per day)

	Year ended December 31,		
	2000	2001	2002
Offshore China			
Independent			
Bohai Bay	45.8	46.2	47.2
Western South China Sea	—	—	4.4
Eastern South China Sea	—	—	—
East China Sea	7.8	9.8	12.4
Total	53.6	56.0	64.0
Production Sharing Contracts			
Bohai Bay	—	—	—
Western South China Sea	144.3	139.0	137.9
Eastern South China Sea	—	—	—
East China Sea	—	—	—
Total	144.3	139.0	137.9
Combined			
Bohai Bay	45.8	46.2	47.2
Western South China Sea	144.3	139.0	142.2
Eastern South China Sea	—	—	—
East China Sea	7.8	9.8	12.4
Total	197.9	195.0	201.8
Overseas[(1)]			
Indonesia	—	—	70.8
Total	—	—	70.8
Total	197.9	195.0	272.6

(1) We do not conduct independent overseas operations. Our overseas operations are conducted through production sharing contracts and technical assistance contracts.

Average Daily Net Production
(BOE per day)

	Year ended December 31,		
	2000	**2001**	**2002**
Offshore China			
Independent			
Bohai Bay	71,437	105,322	118,845
Western South China Sea	45,828	40,377	36,456
Eastern South China Sea	—	—	—
East China Sea	4,853	5,599	5,283
Total	122,118	151,298	160,584
Production Sharing Contracts			
Bohai Bay	—	2,366	16,767
Western South China Sea	24,658	24,063	46,747
Eastern South China Sea	90,097	81,404	73,792
East China Sea	—	—	—
Total	114,755	107,833	137,306
Combined			
Bohai Bay	71,437	107,688	135,612
Western South China Sea	70,486	64,440	83,203
Eastern South China Sea	90,097	81,404	73,792
East China Sea	4,853	5,599	5,283
Total	236,873	259,132	297,890
Overseas[1]			
Indonesia	2,462	2,247	48,749
Total	2,462	2,247	48,749
Total	239,335	261,379	346,639

(1) We do not conduct independent overseas operations. Our overseas operations are conducted through production sharing contracts and technical assistance contracts.

Principal Oil and Gas Regions

Bohai Bay

The Bohai Bay holds our largest net proved reserves and, for the year ended December 31, 2002, was our largest producing area for crude oil and natural gas. The Bohai Bay exploration area is located in the northeastern part of China, approximately 200 kilometers east of Beijing and is approximately 58,100 square kilometers in size. As of December 31, 2002, we had rights to operate independently or in conjunction with international oil and gas companies in 16 blocks covering approximately 42,419 square kilometers of the total Bohai Bay exploration area. Our operating area contains numerous oil and gas fields in shallow waters with typical depths ranging from 10 to 30 meters. The crude oil is generally of heavy gravity ranging from 15 to 20 degrees API. As of December 31, 2002, net proved reserves in this region were 992.5 million barrels of crude oil and condensate and 598.6 billion cubic feet of natural gas, totaling 1,092.3 million BOE and representing approximately 54.2% of our total net proved reserves.

The Bohai Bay has been a prolific area with significant oil discoveries in recent years and will continue to be one of our principal areas for exploration in the near future. Nine discoveries were made in 2002, including six by us and three by foreign partners.

The following table sets forth principal exploration blocks under an exploration license to us for both our independent operations and our production sharing contracts in the Bohai Bay as of December 31, 2002.

Block	Approximate block area (km^2)	Partner(s)	Exploration License		2002 exploration drilling	Independent exploration drilling planned for 2003
			Commencement date	Expiration date		
Independent						
Middle of Bohai Bay	5,310	—	08/16/02	08/16/04	2	6
Southern Bohai Bay(1)	573	—	10/08/00	10/08/02	—	2
Western Bohai Bay(1)	1,913	—	03/29/01	03/29/03	1	—
Liaodong Bay	3,344	—	01/31/00	04/08/06	12	7
Eastern Liaodong Bay	2,829	—	07/02/01	07/02/06	—	—
Production Sharing Contracts(2)						
05/36	1,250	Kerr-McGee, Newfield, Sino-American Energy	02/10/02	02/10/04	2	N/A(3)
06/17(1)	2,587	ChevronTexaco, Carigali	02/01/01	02/01/03	1	N/A(3)
Eastern 11/05	3,601	Phillips, Phillips Bohai	08/16/02	02/10/04	—	N/A(3)
Western 11/05	4,076	Phillips, Phillips Bohai	02/10/02	02/10/04	—	N/A(3)
11/19(1)	3,186	ChevronTexaco	03/28/01	03/28/03	—	N/A(3)
09/18	2,226	Kerr-McGee	04/04/01	04/04/04	—	N/A(3)
02/31(1)	3,936	ChevronTexaco, Carigali	04/06/01	04/06/03	5	N/A(3)
04/36	1,694	Kerr-McGee, Sino-American Energy	12/31/01	12/31/03	4	N/A(3)
11/26(1)(4)	3,190	Shell	10/08/00	10/08/02	—	N/A(3)
Other(5)						

(1) An application has been submitted to extend the exploration license.
(2) One production sharing contract expired in 2002, although the exploration license for the block area covered by the production sharing contract remains in effect. One well was drilled in this block during 2002.
(3) Not applicable.
(4) Since this production sharing block area is located within an independent block, its validity period depends on the exploration license granted to the related independent block. To avoid double-counting, the area attributable to this production sharing block has not been included in the total contract area of the related independent block.
(5) We have exploration rights in the Bohai Bay for two additional blocks covering an aggregate area of approximately 2,703 square kilometers.

During the year ended December 31, 2002, we acquired approximately 680 square kilometers of 3D seismic data and our foreign partners acquired approximately 1,150 square kilometers of 3D seismic data in the Bohai Bay. We have independently acquired an aggregate of approximately 171,100 kilometers and 6,230 square kilometers of 2D and 3D seismic data, respectively, in the Bohai Bay. We also have access through our production sharing contract partners to approximately 66,900 kilometers and 8,480 square kilometers, respectively, of additional 2D and 3D seismic data in this area. During the year of 2002, we drilled seven wildcat wells, five of which were successful, and eight appraisal wells, seven of which were successful. During the same period, our production sharing contract partners drilled five wildcat wells, two of which were successful, and eight appraisal wells, seven of which were successful. Our exploration capital expenditures for 2002 were US$54.6 million. In 2003, we plan to drill 15 exploration wells in the Bohai Bay.

For 2002, net production in this region averaged 127,756 barrels per day of crude oil, condensate and natural gas liquids and 47.2 million cubic feet per day of natural gas, representing approximately 39.1% of our total daily net production. As of December 31, 2002, we were undertaking 10 development projects in the Bohai Bay. Our development capital expenditures for the Bohai Bay for 2002 were US$261.1 million.

The following table sets forth our principal oil and gas properties under production in the Bohai Bay as of December 31, 2002.

Block/Field	Operator	Partner(s)	Our interest	Average net production for year 2002 (BOE per day)	Number of net productive wells	Actual or expected production commencement year	Net proved reserves as of December 31, 2002 (million BOE)
Liaoxi							
Suizhong 36-1	CNOOC Limited	—	100%	72,636	244	1993	222.9
Jinzhou 9-3	CNOOC Limited	—	100%	14,671	43	1999	37.5
Jinzhou 20-2	CNOOC Limited	—	100%	9,002	11	1992	49.5
Boxi							
Qikou 18-1	CNOOC Limited	—	100%	2,953	6	1997	5.2
Qikou 17-3	CNOOC Limited	—	100%	1,688	9	1997	1.5
Qikou 17-2	CNOOC Limited	—	100%	11,143	29	2000	18.4
Chengbei oilfield	CNOOC Limited	—	100%	4,158	52	1985	11.9
Qinhuangdao 32-6	CNOOC Limited	BPCEPC, ChevronTexaco	51%	16,762	80	2001	85.6
Bonan							
Bozhong 34-2/4	CNOOC Limited	—	100%	2,594	25	1990	3.3
11/05							
Penglai 19-3	Phillips China	Phillips Bohai	51%	5	4	2002	123.0

The following table sets forth our principal oil and gas properties under development in the Bohai Bay as of December 31, 2002.

Block/Field	Operator	Partner(s)	Our interest	Actual or expected production commencement year	Net proved reserves as of December 31, 2002 (million BOE)
Liaoxi					
Luda 4-2	CNOOC Limited	—	100%	2005	9.0
Luda 5-2	CNOOC Limited	—	100%	2005	33.1
Luda 10-1	CNOOC Limited	—	100%	2005	34.4
Jinzhou 21-1	CNOOC Limited	—	100%	2008	13.1
Boxi					
Qikou 18-9	CNOOC Limited	—	100%	2008	3.5
Qikou 18-2	CNOOC Limited	—	100%	2004	6.1
Bozhong					
Nanbao 35-2	CNOOC Limited	—	100%	2005	75.7
Bonan					
Bonan oilfields	CNOOC Limited	—	100%	2004	68.3
Bozhong 25-1/25-1s	CNOOC Limited	ChevronTexaco	84%	2004	229.6
11/05					
Penglai 25-6	ConocoPhillips	Phillips Bohai	51%	2008	10.7
04/36					
CFD 11-1	Kerr-McGee	Sino-American Energy	51%	2004	40.4
CFD 11-2	Kerr-McGee	Sino-American Energy	51%	2004	7.9
CFD 18-1	Kerr-McGee	Sino-American Energy	51%	2004	1.7

Western South China Sea

The Western South China Sea has been our most important natural gas producing area, and was our second largest producing area for the year ended December 31, 2002. The Western South China Sea is located in the southern part of China southwest of Hong Kong and is approximately 712,480 square kilometers in area. The most important exploration areas in the Western South China Sea are the Beibu Gulf, the Yinggehai Basin, and the Qiongdongnan Basin. As of December 31, 2002, we had rights to operate independently or in conjunction with international oil and gas companies in 36 blocks covering approximately 166,803 square kilometers of the Western South China Sea exploration area. Typical water depths in this region range from 40 meters to 120 meters. The crude oil produced is of medium to light gravity, ranging from 27 to 41 degrees API. As of December 31, 2002, we had net proved reserves of 160.4 million barrels of crude oil and condensate and 2,511.2 billion cubic feet of natural gas in this region, totaling 578.9 million BOE and representing approximately 28.7% of our total net proved reserves.

The Western South China Sea is one of our least explored areas but will become increasingly important as the markets for natural gas in the southern part of China develop. During the year ended December 31, 2002, we drilled 17 wildcat wells, two of which were successful, and three appraisal wells, one of which was successful. Our production sharing contract partners drilled one wildcat well, which was unsuccessful, in this area and did not drill any appraisal wells.

The following table sets forth the principal exploration blocks under an exploration license to us for both our independent operations and our production sharing contracts in the Western South China Sea as of December 31, 2002.

Block	Approximate block area (km^2)	Partner(s)	Exploration License Commencement date	Exploration License Expiration date	2002 exploration drilling	Independent exploration drilling planned for 2003
Independent						
Ledong 01	6,543	—	12/03/01	12/03/03	4	—
Changjiang 25	5,811	—	12/03/01	12/03/03	7	2
Weizhou 12	6,980	—	05/11/01	05/11/06	—	—
Yulin 35	6,050	—	05/11/01	05/11/06	1	—
Qionghai 28	5,208	—	05/11/01	05/11/06	—	1
Qiongdongnan Songtao 22	4,063	—	05/11/01	05/11/06	1	—
Qiongdongnan Songtao 31	5,264	—	05/11/01	05/11/06	1	—
Qiongdongnan Songtao 18	2,566	—	03/31/00	12/16/05	1	—
Wenchang 20	4,979	—	05/11/01	05/11/06	1	1
Lingao 11	4,117	—	05/11/01	05/11/06	1	—
Lingao 15	6,080	—	05/11/01	05/11/06	3	—
Baodao 16	7,583	—	08/08/02	08/08/07	—	—
Baodao 30	6,341	—	08/07/02	08/07/07	—	—
Production Sharing Contracts						
Wanganbei (A, B, C, D) (1)	25,418	Crestone	10/01/01	10/01/03	—	N/A(3)
39/05(2)	5,700	Husky	12/03/01	12/03/03	—	N/A(3)
22/12(2)	608	Rec Oil, Bligh Petsec Petroleum, Oil Australia	05/11/01	05/11/06	1	N/A(3)
23/20(2)	1,543	Husky	05/11/01	05/11/06	—	N/A(3)
23/15(2)	1,327	Husky	05/11/01	05/11/06	—	N/A(3)
Other(4)						

(1) The Wanganbei block area consists of four blocks.

(2) Since this production sharing block area is located within an independent block, its validity period depends on the exploration license granted to the related independent block. To avoid double-counting, the area attributable to this production sharing block has not been included in the total block area of the related independent block.

(3) Not applicable.

(4) We have exploration rights in the Western South China Sea for 15 additional blocks covering an aggregate area of approximately 60,622 square kilometers.

During the year ended December 31, 2002, we acquired approximately 712 square kilometers of 3D seismic data and our foreign partners acquired approximately 460 square kilometers of 3D seismic data in the Western South China Sea. We have independently acquired an aggregate of approximately 159,550 kilometers and 7,010 square kilometers of independent 2D and 3D seismic data, respectively, in the Western South China Sea. We also have access through our production sharing contract partners to approximately 106,900 kilometers and 3,670 square kilometers of additional 2D and 3D seismic data, respectively, in this area. Our exploration capital expenditures for the Western South China Sea for 2002 were US$68.9 million. In 2003, we plan to drill four exploration wells in the Western South China Sea area.

For the year ended December 31, 2002, net production averaged 56,910 barrels per day of crude oil, condensate and natural gas liquids and 142.2 million cubic feet per day of natural gas, representing approximately 24.0% of total daily net production. Our development capital expenditures for the Western South China Sea for 2002 were US$268.5 million.

The following table sets forth the principal oil and gas properties in the Western South China Sea area that were under production or development as of December 31, 2002.

Block/Field	Operator	Partner(s)	Our interest	Average net production for year 2002 (BOE per day)	Number of net productive wells	Actual or expected production commencement year	Net proved reserves as of December 31, 2002 (million BOE)
Production							
Yinggehai							
Yacheng 13-1	BPCEPC	Kufpec	51%	26,953	6	1995	98.3
Yulin 35							
Weizhou 11-4	CNOOC Limited	—	100%	18,821	45	1993	21.2
Weizhou 12-1	CNOOC Limited	—	100%	17,635	17	1999	29.6
Yangjiang 39/05							
Wenchang 13-1/13-2	CNOOC Limited	Husky	60%	19,794	13	2002	46.5
Development							
Yulin 35							
Weizhou 12-1 North	CNOOC Limited	—	100%	—	—	2004	21.5
Changjiang 25							
Dongfang 1-1	CNOOC Limited	—	100%	—	—	2003	218.5
Yangjiang 31 and 32							
Wenchang 8-3	CNOOC Limited	—	100%	—	—	2005	11.6
Wenchang 19-1	CNOOC Limited	—	100%	—	—	2007	26.1
Ledong 01							
Ledong 15-1/22-1	CNOOC Limited	—	100%	—	—	2009	83.2

Eastern South China Sea

The Eastern South China Sea is currently one of our most important oil producing areas in terms of its contribution to our total production and sales. The Eastern South China Sea exploration area is located in the southern part of China, directly southeast of Hong Kong, and is approximately 174,420 square kilometers in size. As of December 31, 2002, we had rights to operate independently or in conjunction with international oil and gas companies in 36 blocks covering approximately 164,550 square kilometers in the Eastern South China Sea exploration area. This area includes the important Pearl River Mouth Basin. Typical water depths in this region range from 100 meters to 120 meters. The crude oil produced is of medium to light gravity, ranging from 30 to 40 degrees API. As of December 31, 2002, we had net proved reserves of 120.3 million barrels of crude oil and condensate and 42.8 billion cubic feet of natural gas in this region, totaling 127.5 million BOE and representing approximately 6.3% of our total net proved reserves.

During the year ended December 31, 2002, we drilled four wildcat wells, two of which were successful, and one successful appraisal well. Our production sharing contract partners drilled two unsuccessful wildcat wells and did not drill any appraisal wells in this area.

The following table sets forth the principal exploration blocks that are under an existing or pending exploration license to us for both our independent operations and our production sharing contracts in the Eastern South China Sea as of December 31, 2002.

Block	Approximate block area (km^2)	Partner(s)	Exploration License Commencement date	Exploration License Expiration date	2002 exploration drilling	Independent exploration drilling planned for 2003
Independent						
Huizhou 31	3,074	—	05/11/01	05/11/06	—	—
Enping 15	5,833	—	05/11/01	05/11/06	—	—
Enping 10	6,547	—	05/11/01	05/11/06	—	—
Panyu 33	4,830	—	05/11/01	05/11/06	—	—
Liuhua 07	4,172	—	05/11/01	05/11/06	4	4
Chaotai	7,834	—	05/14/02	05/14/07	—	1
Xijiang 04	7,969	—	05/11/01	05/11/06	1	—
Lufeng 08	4,723	—	05/11/01	05/11/06	—	3
Huizhou 30	5,862	—	05/11/01	05/11/06	—	—
Production Sharing Contracts						
16/19(1)	415	Agip, ChevronTexaco	10/08/00	03/31/02	—	N/A(2)
15/34	5,124	Devon, Burlington	08/30/00	02/28/04	1	N/A(2)
16/02	3,498	Devon, Energy Development Corporation	03/31/00	03/31/07	—	N/A(2)
15/12	1,895	Shell, Phillips	10/16/00	10/16/06	—	N/A(2)
15/35(1)	1,439	Devon, Burlington	08/10/01	01/31/03	—	N/A(2)
27/10(3)	6,546	Devon, Energy Development Corporation	10/09/01	10/09/03	1	N/A(2)
16/08(1)	541	Agip, ChevronTexaco	04/29/01	04/29/03	—	N/A(2)
16/05	3,009	Devon, Energy Development Corporation	03/31/00	03/31/07	—	N/A(2)
Other(4)						

(1) An application has been submitted to extend the exploration license.
(2) Not applicable.
(3) Since this production sharing block area is located within an independent block, its validity period depends on the exploration license granted to the related independent block. To avoid double-counting, the area attributable to this production sharing block has not been included in the total contract area of the related independent block.
(4) We have exploration rights in this region for 19 additional blocks covering an aggregate area of approximately 91,239 square kilometers.

For the year ended December 31, 2002, we acquired 6,400 kilometers of 2D seismic data and 1,330 square kilometers of 3D seismic data, while our foreign partners acquired approximately 970 kilometers of 2D seismic data and 782 square kilometers of 3D seismic data in the Eastern South China Sea area. We have an aggregate of approximately 55,600 kilometers of independent 2D seismic data and 1,330 square kilometers of 3D seismic data in the Eastern South China Sea. We also have access through our production sharing contract partners to approximately 107,700 kilometers and 6,090 square kilometers of additional 2D and 3D seismic data, respectively, in this area. Our exploration capital expenditures for the Eastern South China Sea for 2002 were US$42.0 million. We plan to drill eight exploration wells in the Eastern South China Sea in 2003.

For the year ended December 31, 2002, net production averaged approximately 73,792 barrels per day of crude oil, representing approximately 21.3% of our total daily net production. Our development capital expenditures for this region for 2002 were US$122.0 million.

The following table sets forth our principal oil and gas properties under production in the Eastern South China Sea as of December 31, 2002.

Production Block/Field	Operator	Partner(s)	Our interest	Average net production for year 2002 (BOE per day)	Number of net productive wells	Actual or expected production commencement year	Net proved reserves as of December 31, 2002 (million BOE)
16/08							
Huizhou 21-1	CACT	Agip, ChevronTexaco	51%	3,015	8	1990	2.5
Huizhou 26-1	CACT	Agip, ChevronTexaco	51%	13,427	11	1991	14.4
Huizhou 32-2	CACT	Agip, ChevronTexaco	51%	3,269	5	1995	1.5
Huizhou 32-3	CACT	Agip, ChevronTexaco	51%	7,113	6	1995	6.4
Huizhou 32-5	CACT	Agip, ChevronTexaco	51%	4,541	2	1999	2.8
15/11							
Xijiang 24-3	CNOOC Limited, ConocoPhillips	Shell	51%	16,732	11	1994	12.4
15/22							
Xijiang 30-2	CNOOC Limited, ConocoPhillips	Shell	40%	14,202	10	1995	9.2
29/04							
Liuhua 11-1	CNOOC Limited, BPCEPC-LIUHUA	Kerr-McGee	51%	7,139	13	1996	6.0
16/06							
Lufeng 13-1	JHN	JHN	25%	2,697	5	1993	2.9
17/22							
Lufeng 22-1	CNOOC Limited, Statoil	Statoil	25%	1,657	1	1997	0.8

The following table sets forth our principal oil and gas properties under development as of December 31, 2002.

Block/Field	Operator	Partner(s)	Our interest	Actual or expected production commencement year	Net proved reserves as of December 31, 2002 (million BOE)
16/08					
Huizhou 21-1 Gas	CACT	Agip, ChevronTexaco	51%	2005	9.5
16/19					
Huizhou 19-1	CACT	Agip, ChevronTexaco	51%	2006	2.0
Huizhou 19-2	CACT	Agip, ChevronTexaco	51%	2005	12.5
Huizhou 19-3	CACT	Agip, ChevronTexaco	51%	2004	11.2
15/34					
Panyu 4-2	Devon	Burlington	51%	2003	16.4
Panyu 5-1	Devon	Burlington	51%	2003	17.0

East China Sea

The East China Sea is the least explored area of our four principal regions offshore China, and an area that we expect to become an important natural gas production base in the future. The East China Sea is approximately 339,580 square kilometers in size and is located east of Shanghai. As of December 31, 2002, we had rights to operate independently or in conjunction with international oil and gas companies in 45 blocks (excluding the Pinghu block) covering approximately 198,713 square kilometers of the total East China Sea. We also own a 50% working interest in the Xihu Trough area within the East China Sea. We and Sinopec, our joint venture partner, have formed a joint management committee and established the East China Sea Xihu Oil and Gas Operating Company to oversee the development of this region. The total block area of the Xihu Trough is approximately 59,565 square kilometers. Typical water depths in this region are approximately 90 meters and the crude oil and condensate are of light gravity. As of December 31, 2002, our net proved reserves in the Xihu Trough were 8.9 million barrels of crude oil and condensate and 127.1 billion cubic feet of natural gas, totaling 30.1 million BOE and representing less than 1.5% of our total net proved reserves. We acquired our interest in the project from CNOOC and are the operator of the project.

During the year ended December 31, 2002, we drilled two appraisal wells, one of which was successful, in cooperation with Sinopec in our independent blocks. We drilled one wildcat well that was successful during 2002. Our foreign partners did not drill any exploration wells in this area in 2002.

The following table sets forth the principal exploration blocks under an existing or pending exploration license to us for both our independent operations and our production sharing contracts in the East China Sea as of December 31, 2002.

Block	Approximate block area (km^2)	Partner(s)	Exploration License: Commencement date	Exploration License: Expiration date	2002 exploration drilling	Independent exploration drilling planned for 2003
Independent						
Pinghu(1)	N/A	Sinopec National Star, Shanghai Municipal Government	N/A	N/A	—	—
Huangyan 04	2,848	—	08/28/01	08/28/08	3	6
Hangzhou 17	4,227	—	08/28/01	08/28/08	—	—
Zhenghai 01	1,536	—	08/28/01	08/28/08	—	—
Fuyang 27	2,526	—	08/28/01	08/28/08	—	—
Lishui-Jiaojiang Trough	6,767	—	03/31/00	11/28/05	—	—
Western Wunansha	242	—	03/31/00	12/16/05	—	—
Dalian 16	6,471	—	05/11/01	05/11/06	—	—
Yantai 04	6,111	—	05/11/01	05/11/06	—	—
Lishui 30	4,085	—	07/01/02	07/01/09	—	—
Qingdao 34	5,745	—	12/07/02	12/07/06	—	—
Production Sharing Contracts						
32/32	513	Primeline Energy, Primeline Petroleum	07/11/02	07/11/04	—	N/A(2)
Other(3)						

(1) This field is covered by a production license to the Shanghai Petroleum and Natural Gas Company in which we have a 30% interest. The production license will expire on December 1, 2020.

(2) Not applicable.

(3) We have exploration rights in this region for 34 additional blocks covering an aggregate area of approximately 157,642 square kilometers.

During the year ended December 31, 2002, we acquired 8,050 kilometers of 2D seismic data in this area. We have independently acquired an aggregate of approximately 107,430 kilometers and 377 square kilometers, respectively, of 2D and 3D seismic data in the East China Sea area. We also have access through our production sharing contract partners to approximately 47,520 kilometers and 475 square kilometers, respectively, of additional 2D and 3D seismic data in this area. Our exploration capital expenditures for the East China Sea for 2002 were US$18.0 million. We plan to drill six exploration wells with other parties, and our foreign partners currently have no plans to drill any exploration wells in the East China Sea in 2003.

For the year ended December 31, 2002, our net production in this region averaged 3,223 barrels per day of crude oil, condensate and natural gas liquids and 12.4 million cubic feet per day of natural gas, representing 1.5% of total daily net production. Our development capital expenditures for the East China Sea for 2002 were US$52.2 million.

The following table sets forth the principal oil and gas properties under production or development in the East China Sea as of December 31, 2002.

Block/Field	Operator	Partner(s)	Our interest	Average net production for year 2002 (BOE per day)	Number of net productive wells	Actual or expected production commencement year	Net proved reserves as of December 31, 2002 (million BOE)
Production							
Pinghu[1]							
Pinghu (I)	CNOOC Limited	Sinopec National Star, Shanghai Municipal Government	30%	5,283	5	1998	9.9
Development							
Pinghu[1]							
Pinghu (II)	CNOOC Limited	Sinopec National Star, Shanghai Municipal Government	30%	—	—	2006	2.4
Xihu Trough							
Canxue	CNOOC Limited	Sinopec	50%	—	—	2007	11.6
Duanqiao	CNOOC Limited	Sinopec	50%	—	—	2008	18.5

(1) This field is under license to the Shanghai Petroleum and Natural Gas Company in which we have a 30% interest.

Overseas Activity

In early 2003, we acquired interests in the Tangguh LNG Project located in Indonesia. For further details of these interests, see "—Natural Gas Business—Overseas Activity."

In October 2002, we entered into a key terms agreement to acquire interests in natural gas reserves located in the North West Shelf of Australia. See "—Natural Gas Business—Overseas Activity."

In April 2002, our wholly owned subsidiary, CNOOC Southeast Asia Limited, acquired subsidiaries in Indonesia formerly owned by Repsol YPF, S.A. These Indonesian subsidiaries together hold a portfolio of interests in oil and gas production sharing and technical assistance contracts in areas located offshore and onshore Indonesia. The acquisition of the Indonesian subsidiaries was consistent with our plan to expand our production and reserves. Furthermore, we believe the acquisition represented a unique opportunity to acquire producing assets that fit with our offshore expertise and experience. The main businesses of the Indonesian subsidiaries are the exploration, development and production of oil and gas offshore and onshore Indonesia. Their main assets comprise a portfolio of interests in four production sharing contracts and a technical assistance contract in that region. We estimate that our net proved reserves of the assets as of December 31, 2002 were approximately 167.1 million BOE.

The interests owned by the Indonesian subsidiaries comprise the following assets:

- *South East Sumatra Production Sharing Contract.* The Indonesian subsidiaries own a 65.3% interest in the South East Sumatra production sharing contract. This contract area covers approximately 8,100 square kilometers located offshore Sumatra and is the largest of the assets held by the Indonesian subsidiaries. It is operated and majority—owned by us. It is also one of the largest offshore oil developments in Indonesia and has produced more than one billion barrels of oil in over 20 years of production. The concession expires in 2018.

- *Offshore North West Java Production Sharing Contract.* The Indonesian subsidiaries own a 36.7% interest in the Offshore North West Java production sharing contract. This contract area covers approximately 13,800 square kilometers in the Southern Java Sea, offshore Jakarta and has produced more than one billion BOE in over 20 years of production. It is operated by a member of the BP group and currently produces crude oil and natural gas. Its natural gas is sold to the Indonesia State Electric Company and the Indonesia State Gas Utility Company. The concession expires in 2017.

- *West Madura Production Sharing Contract and Poleng Technical Assistance Contract.* These subsidiaries own a 25.0% interest in the West Madura production sharing contract and a 50.0% interest in the Poleng technical assistance contract. These contract areas are located offshore Java, near the island of Madura and the Java city of Surabaya and cover approximately 1,600 square kilometers combined. Kodeco Energy Company is the operator for the West Madura production sharing contract and Korea Development Company is the operator for the Poleng technical assistance contract, each assisted by certain of the Indonesian subsidiaries. These contract areas currently produce crude oil and natural gas. Their natural gas is sold to the Indonesia State Electric Company. The West Madura production sharing contract expires in May 2011. The Poleng technical assistance contract expires in December 2013.

- *Blora Production Sharing Contract.* The Indonesian subsidiaries own a 16.7% interest in the Blora production sharing contract. This contract area lies entirely onshore Java and covers an area of approximately 4,800 square kilometers. There has been no production of crude oil or natural gas from this concession. The current operator is Coparex Blora. The concession expires in 2026.

The remaining interests in the above assets at the time of our acquisition were owned by independent third parties, including Lundin Petroleum, BP, Kodeco, Kalila Energy, BG Group, Pertamina, INPEX, Kanematsu, Nissho Iwai, Nisseki Mitsubishi, Paladin Resources, C. Itoh and Co. and Amerada Hess.

In addition to our Indonesian subsidiaries and the acquisition of interests in the Tangguh LNG Project, we have a 39.5% participating interest in a production sharing contract in the Malacca Strait in Indonesia. As of December 31, 2002, our net proved reserves in this property were 7.6 million barrels of crude oil. For 2002, net production from this property averaged 2,579 barrels per day of crude oil, condensate and natural gas liquids, representing approximately 0.7% of total daily net production. Production has been declining in recent years due to water cut increases and natural production declines. Our interests in the production sharing contract are held by our wholly owned subsidiaries.

We currently conduct all of our international oil sales through China Offshore Oil (Singapore) International Pte. Ltd., our wholly owned Singapore subsidiary. In the past, this subsidiary has also engaged in oil trading activities.

The following table sets forth the principal oil and gas properties under production in our overseas interests as of December 31, 2002. There is no data for the number of productive wells and actual or expected production commencement year because we only recently acquired our interests in these properties from other parties.

Production Sharing Contract	Operator	Partner(s)	Our interest	Average net production for year 2002 (BOE per day)	Net proved reserves as of December 31, 2002 (million BOE)
Repsol					
South East Sumatra	CNOOC Limited	INPEX Sumatra KNOC Sumatra MC Oil & Gas Sumatra Paladin Indonesia (Sunda) Paladin UK (Southeast Sumatra) Paladin Resources (Bahamas) CNOOC Limited	65.3%	24,921	87.42
Offshore North West Java	BP	CNOOC ONWJ INPEX Jaws MC Oil and Gas Java C. ITOH Energy Paladin Resources (Sunda) BP West Java	36.7%	15,405	64.86
West Madura	Kodeco Energy	Pertamina CNOOC Madura KODECO Energy	25.0%	1,895	8.29
Poleng(1)	Korea Development	CNOOC Poleng Korea Development	50.0%	3,945	6.52
Blora	Lundin Blora	CNOOC Blora Paladin Resources Amerada Hess Lundin Blora	16.7%	—	—
Malacca					
Malacca Strait	Kondur Petroleum	CNOOC Limited OOGC Malacca Mallaca Petroleum Imbang Tata Alam Kondur Petroleum	39.5%	2,579	7.63

(1) Our interest in this contract area is in the form of a technical assistance contract.

Other Oil and Gas Data

Production Cost Data

The following table sets forth average sales prices per barrel of crude oil, condensate and natural gas liquids sold, average sales prices per thousand cubic feet of natural gas sold and production costs per BOE produced for each of our independent, production sharing contract and combined operations for the periods indicated.

	Year ended December 31,		
	2000	2001	2002
		(US$)	
Average Sales Prices of Petroleum Produced			
Per Barrel of Crude Oil, Condensate and Natural Gas Liquid Sold	28.21	23.34	24.35
Per Thousand Cubic Feet of Natural Gas Sold	3.09	3.08	2.98
Offshore China Average Lifting Costs per BOE Produced(1)			
Independent	4.00	3.88	3.89
Production Sharing Contracts	4.86	4.51	3.95
Offshore China Average	4.45	4.16	3.92
Overseas Average Lifting Costs per BOE Produced(1)			
Net Entitlement	—	—	9.06

(1) Our overseas operations during the years ended December 31, 2000 and 2001 were not material, and the related lifting costs have been included in our offshore China lifting costs for those years.

Drilling and Productive Wells

The following table sets forth our exploratory and productive wells drilled offshore China as of December 31, 2002 by independent and production sharing contract operations in each of our operating areas. There is no data for exploratory and productive wells drilled overseas because we only recently acquired our interests in these properties from other parties.

	As of December 31, 2002				
	Total Offshore China	Bohai Bay	Western South China Sea	Eastern South China Sea	East China Sea
Independent					
Net Exploratory Wells	430.0	262.0	148.0	7.0	13.0
Net Productive Wells	431.5	373.0	54.0	—	4.5
Crude Oil	418.1	362.0	54.0	—	2.1
Natural Gas	13.4	11.0	—	—	2.4
Production Sharing Contracts					
Net Exploratory Wells	2.0	—	—	—	2.0
Net Productive Wells	175.1	83.1	18.2	73.8	—
Crude Oil	168.5	83.1	12.6	72.8	—
Natural Gas	6.6	—	5.6	1.0	—
Totals					
Net Exploratory Wells	432.0	262.0	148.0	7.0	15.0
Net Productive Wells	606.6	456.1	72.2	73.8	4.5
Crude Oil	586.6	445.1	66.6	72.8	2.1
Natural Gas	20.0	11.0	5.6	1.0	2.4

Drilling Activity

The following tables set forth our net exploratory and development wells broken down by independent and production sharing contract operations in each of our operating areas for the year ended December 31, 2002.

	Year ended December 31, 2002					
	Total	**Bohai Bay**	**Western South China Sea**	**Eastern South China Sea**	**East China Sea**	**Overseas**
Independent						
Net Exploratory Wells Drilled	41.5	15.0	20.0	5.0	1.5	—
Successful	19.0	12.0	3.0	3.0	1.0	—
Dry	22.5	3.0	17.0	2.0	0.5	—
Net Development Wells Drilled	14.0	2.0	12.0	—	—	—
Successful	14.0	2.0	12.0	—	—	—
Dry	—	—	—	—	—	—
Production Sharing Contracts						
Net Exploratory Wells Drilled	3.1	—	—	—	—	3.1
Successful	1.9	—	—	—	—	1.9
Dry	1.2	—	—	—	—	1.2
Net Development Wells Drilled	65.0	20.2	3.6	3.1	—	38.1
Successful	60.7	20.2	3.6	3.1	—	33.8
Dry	4.3	—	—	—	—	4.3

	Year ended December 31, 2001					
	Total	**Bohai Bay**	**Western South China Sea**	**Eastern South China Sea**	**East China Sea**	**Overseas**
Independent						
Net Exploratory Wells Drilled	13.0	4.0	6.0	1.0	2.0	—
Successful	5.0	2.0	2.0	1.0	—	—
Dry	8.0	2.0	4.0	—	2.0	—
Net Development Wells Drilled	76.0	76.0	—	—	—	—
Successful	76.0	76.0	—	—	—	—
Dry	—	—	—	—	—	—
Production Sharing Contracts						
Net Exploratory Wells Drilled	1.0	—	—	—	1.0	—
Successful	—	—	—	—	—	—
Dry	1.0	—	—	—	1.0	—
Net Development Wells Drilled	41.7	34.7	4.8	—	0.6	1.6
Successful	40.7	34.7	3.8	—	0.6	1.6
Dry	1.0	—	1.0	—	—	—

	Year ended December 31, 2000					
	Total	Bohai Bay	Western South China Sea	Eastern South China Sea	East China Sea	Overseas
Independent						
Net Exploratory Wells Drilled	12.0	5.0	4.0	1.0	2.0	—
Successful	6.0	5.0	1.0	—	—	—
Dry	6.0	—	3.0	1.0	2.0	—
Net Development Wells Drilled	65.2	61.0	3.0	—	1.2	—
Successful	65.2	61.0	3.0	—	1.2	—
Dry	—	—	—	—	—	—
Production Sharing Contracts						
Net Exploratory Wells Drilled	1.4	—	—	—	1.0	0.4
Successful	1.0	—	—	—	1.0	—
Dry	0.4	—	—	—	—	0.4
Net Development Wells Drilled	24.4	22.4	—	—	—	2.0
Successful	24.4	22.4	—	—	—	2.0
Dry	—	—	—	—	—	—

Natural Gas Business

Natural gas is becoming an increasingly important part of our business strategy. We intend to exploit our natural gas reserves to meet rapidly growing domestic demand for natural gas. Because of a domestic natural gas shortfall forecasted by the Chinese government, we have made strategic investments in liquefied natural gas projects outside the PRC and may continue to do so in the future.

PRC Activity

CNOOC, our controlling shareholder, has granted us an option to invest in liquefied natural gas projects or other natural gas related business in which CNOOC has invested or proposes to invest. CNOOC is currently involved in the following large-scale natural gas projects.

Guangdong LNG Facility. CNOOC is currently engaged in a project to build China's first proposed liquefied natural gas import facility in Guangdong Province in southern China. CNOOC has granted us the option to acquire CNOOC's interest in the project. The terms of this option require us, if we exercise the option, to reimburse CNOOC for any contribution CNOOC has made with respect to the facility together with interest calculated at the prevailing market rate. We have not entered into any negotiations with CNOOC on the detailed terms under which we may acquire CNOOC's interest in this facility. CNOOC has committed to take a 33% ownership interest in the project. Other partners include Hongkong Electric and Hong Kong and China Gas, each committed to 3% ownership interests, and five customers of the proposed facility who have collectively committed to a 31% ownership interest. Through a competitive selection process, BP Global Investment Limited was selected as the foreign partner to take the remaining 30% interest in the project.

The project involves the construction of a receiving terminal with capacity of three million metric tons per year, a 215-kilometer trunkline and two branch trunklines with a total length of 111 kilometers. Project construction is expected to begin in the second quarter of 2003. The facility is scheduled to commence operations in 2006. The total cost of the facility is estimated to be approximately US$600 million. CNOOC will help us procure all necessary government approvals for our participation in this project should we exercise our option. We are currently evaluating the exercise of this option and may exercise it at any time.

Zhejiang Network. In September 2001, CNOOC signed an agreement with Zhejiang Provincial Energy Group Company Limited and Zhejiang Southeast Electric Power Company Limited to invest in a joint venture to develop an intra-provincial natural gas distribution network. CNOOC will hold a 37% equity interest in the joint venture company. We have an option to take CNOOC's share in the joint venture company in an arrangement similar to our option for the Guangdong liquefied natural gas project. The business scope of the joint venture includes the construction, operation and management of natural gas pipelines, the intra-provincial wholesale and distribution of natural gas, and the development of gas-fired power plants and other natural gas related infrastructure and projects.

Shandong Pipeline. In September 2001, CNOOC signed an agreement with the Shandong Province Development Planning Commission and Shandong International Trust & Investment Corporation in connection with the construction of a gas pipeline and the importation of liquefied natural gas in Shandong Province. A steering committee was established by the parties to study the prospect of gas utilization in Shandong Province, including the feasibility of constructing a main gas pipeline in Shandong and importing liquefied natural gas to Shandong through Qingdao. CNOOC intends to use gas resources from the Bohai Bay. CNOOC expects that natural gas from the Bohai Bay will land in Longkou of Shandong Province in 2003, which can be further transported to Qingdao and Yantai in Shandong Province by pipeline. The pipeline between Longkou and Yantai will be 95 kilometers; the pipeline between Longkou and Qingdao will be 2,101 kilometers.

Fujian Development. In October 2001, CNOOC signed an agreement with the Fujian provincial government on natural gas market development in Fujian Province. The agreement provides for a joint investment commitment of increasing natural gas supply and gas market development in Fujian Province by both parties. Both parties are committed to sourcing gas, including liquefied natural gas, from all viable sources, including from offshore production and overseas. The parties also agreed to invest in gas-fired power plants and related infrastructure. We have the option to take CNOOC's working interest in the project and have recently acquired an interest in the Tangguh LNG Project in Indonesia, which will supply liquefied natural gas to this project.

Overseas Activity

On January 1, 2003, we acquired BP Muturi Limited, which owns a 44.0% interest in the Muturi production sharing contract offshore Indonesia, and BP Wiriagar Limited's 42.4% interest in the Wiriagar production sharing contract offshore Indonesia for a total of approximately US$275 million. The Muturi production sharing contract and Wiriagar production sharing contract, together with the Berau production sharing contract, make up the Tangguh LNG Project. The Tangguh LNG Project is a greenfield project located offshore Indonesia and represents one of the largest natural gas projects in Asia.

Our interests in these two production sharing contracts represent approximately 12.5% of the total reserves and upstream production of the Tangguh LNG Project. The remaining interests in the Tangguh LNG Project are held by BP Berau (34.2%), BP Muturi (0.2%), BP Wiriagar (2.7%), MI Berau (16.3%), Nippon (12.2%), BG (10.7%), KG Berau (8.6%), KG Wiriagar (1.4%) and Indonesia Natural Gas Resources Muturi (1.1%). The partners in the Tangguh LNG Project have applied to the Indonesia government to consolidate the three production sharing contracts and expect that BP will serve as the operator for the project.

Before acquiring interest in the Tangguh LNG Project, the partners in the Tangguh LNG Project entered into a conditional 25-year supply contract beginning in 2007 to provide up to 2.6 million tons of liquefied natural gas per year to a liquefied natural gas terminal project in Fujian Province, China. In addition, a repurchase agreement was entered into whereby put options and call options were granted to us and the sellers, respectively, to sell or repurchase, as the case may be, the interests in these production sharing contracts. The exercise prices of the options are determined based on the original consideration plus interest and additional investment and draw down made during the interim period. The options are exercisable if on or before December 31, 2004:

- the LNG supply contract is terminated due to the non-satisfaction of the conditions precedent to the LNG supply contract; or

- the LNG supply contract is otherwise legally ineffective.

See "—PRC Activity—Fujian Development." Given the proximity of the Tangguh LNG Project to many major industrial and commercial areas, we expect the project to secure additional LNG supply contracts in the near future.

In October 2002, we entered into a key terms agreement to acquire an aggregate interest of approximately 5.56% in the reserves and upstream production of Australia's North West Shelf Gas Project for approximately US$365.6 million, subject to certain adjustments. Under the terms of this agreement, we would purchase our interest from the six current partners to this project: BHP Billiton, BP, ChevronTexaco, Japan Australia LNG (MIMI), Shell and Woodside Energy. Our estimated share of reserves from this project would be approximately 1.2 trillion cubic feet of natural gas. Our share of natural gas together with associated liquids would be approximately 210 million BOE. Woodside Petroleum is the operator for the project.

Under the terms of this agreement, we would also acquire a 25% interest in the China LNG Joint Venture, which is being established by the six current partners to supply liquefied natural gas from the North West Shelf Gas Project to a liquefied natural gas terminal currently being developed by CNOOC, our controlling shareholder, and various partners in Guangdong Province, China. The terms of this transaction require us to pay the other partners in the North West Shelf Gas Project for gas production and processing services provided over the term of the China LNG Joint Venture. We expect to complete our acquisition of the interests in the North West Shelf Gas Project and China LNG Joint Venture in 2003. See "Business—Natural Gas Business—Overseas Activity."

To the extent we invest in businesses and geographic areas where we have limited experience and expertise, we plan to structure our investments as alliances and partnerships with parties possessing the relevant experience and expertise.

Sales and Marketing

Sales of Offshore Crude Oil

We sell crude oil and natural gas to the PRC market through our wholly owned PRC subsidiary, CNOOC China Limited, and sell to the international market through our wholly owned subsidiary, China Offshore Oil (Singapore) International Pte. Ltd., located in Singapore.

We submit production and sales plans to the State Economic and Trade Commission each year. Based on information provided by China's three crude oil producers, PetroChina, Sinopec and us, the State Development and Planning Commission compiles an overall national plan for coordinating sales. We have been allowed to determine where we sell our production, both domestically and internationally. Our sales of crude oil to the international market also require us to obtain export licenses issued by the Ministry of Foreign Trade and Economic Cooperation. Historically, we have obtained all required export licenses.

Pricing

We price our crude oil with reference to prices for crude oil of comparable quality in the international market, including a premium or discount mutually agreed upon by us and our customers according to market conditions at the time of the sale. Prices are quoted in U.S. dollars, but domestic sales are billed and paid in Renminbi.

We currently produce three types of crude oil: Nanhai Light, Medium Grade and Heavy Crude. The table below sets forth the sales and marketing volumes, pricing benchmarks and average realized prices for each of these three types of crude oil for the periods indicated.

	Year ended December 31,		
	2000	**2001**	**2002**
Sales and Marketing Volumes (benchmark) (mmbbls)[(1)]			
Nanhai Light (APPI[(2)] Tapis[(3)])	39.1	32.2	26.4
Medium Grade (Daqing OSP[(4)])	58.3	57.1	64.7
Heavy Crude (APPI[(2)] Duri[(5)])	25.4	37.4	52.7
Average Realized Prices (US$/bbl)[(6)]			
Nanhai Light	US$29.49	US$24.96	US$24.79
Medium Grade	28.98	24.16	25.92
Heavy Crude	26.53	21.01	22.79
Benchmark Prices (US$/bbl)			
APPI[(2)] Tapis[(3)]	US$29.53	US$24.99	US$25.49
Daqing OSP[(4)]	28.53	23.92	24.95
APPI[(2)] Duri[(5)]	26.39	21.26	21.94
ICP[(7)] Cinta[(8)]	—	—	24.08
ICP Widuri[(9)]	—	—	24.08
West Texas Intermediate (US$/bbl)	US$30.35	US$25.89	US$26.16

(1) Includes the sales volumes of us and our foreign partners under production sharing contracts.
(2) Asia petroleum price index.
(3) Tapis is a light crude oil produced in Malaysia.
(4) Daqing official selling price. Daqing is a medium crude oil produced in northeast China.
(5) Duri is a heavy crude oil produced in Indonesia.
(6) Includes the average realized prices of us and our foreign partners under production sharing contracts.
(7) Indonesian crude price.
(8) Cinta is a medium crude oil produced in Indonesia and was not a relevant benchmark for our crude oil sales prior to the acquisition of the Indonesian subsidiaries in 2002.
(9) Widuri is a medium crude oil produced in Indonesia and was not a relevant benchmark for our crude oil sales prior to the acquisition of the Indonesian subsidiaries in 2002.

The international benchmark crude oil price, West Texas Intermediate, was US$31.21 per barrel as of December 31, 2002 and US$29.17 per barrel as of May 14, 2003.

Markets and Customers

We sell most of our crude oil production in the PRC domestic market. We also sell to customers in South Korea, Japan, the United States and Australia, as well as to crude oil traders in the spot market. For the years ended December 31, 2000, 2001 and 2002, we sold approximately 67.0%, 79.9% and 85.1%, respectively, of our crude oil in the PRC, and exported approximately 33.0%, 20.1% and 14.9%, respectively.

Most of our crude oil production sales in the PRC domestic market are to refineries and petrochemical companies that are affiliates of Sinopec, PetroChina and CNOOC, our controlling shareholder. Sales volume to Sinopec has been high historically because most of the PRC refineries and petrochemical companies were affiliates of Sinopec. After the restructuring of the PRC petroleum industry in July 1998, some refineries and petrochemical companies were transferred to PetroChina from Sinopec. As a result, sales to Sinopec decreased and sales to PetroChina increased. For the years ended December 31, 2000, 2001 and 2002, sales to Sinopec were approximately 52.8%, 52.7% and 44.7%, respectively, and sales to PetroChina were approximately 12.6%, 13.8% and 7.7%, respectively, of total crude oil sales in the PRC domestic market. Together these two customers accounted for approximately 65.4%, 66.5% and 52.4%, respectively, of the total crude oil sales in the PRC domestic market. For further information about our sales to CNOOC-affiliated companies, please see note 27 to our consolidated financial statements beginning on page F-1.

In recent years, we have diversified our domestic client base by targeting companies not affiliated with Sinopec or PetroChina. These targeted companies typically are involved in bitumen processing, fuel blending and mixing, power generation and production of fertilizer feed stocks. We plan to continue our efforts to diversify our client base.

The following table presents, for the periods indicated, our revenues sourced in the PRC and outside the PRC:

	Year ended December 31,		
	2000	2001	2002
	(Rmb in millions, except percentages)		
Revenues sourced in the PRC	17,559	18,105	22,781
Revenues sourced outside the PRC	6,665	2,715	3,593
Total revenues	24,224	20,820	26,374
% of revenues sourced outside the PRC	27.5%	13.0%	13.6%

Sales Contracts

We sign sales contracts with customers for each shipment. Sales contracts are standard form contracts containing ordinary commercial terms such as quality, quantity, price, delivery and payment. All sales are made on free-on-board terms. PRC customers are required to make payments within 30 days after the shipper takes possession of the crude oil cargo at our delivery points. During the years ended December 31, 2000, 2001 and 2002, the accounts receivable turnover were approximately 39.5 days, 32.3 days and 32.7 days, respectively. Doubtful accounts provision during the years ended December 31, 2000, 2001 and 2002 were Rmb 15.7 million, Rmb 10.7 million and nil, respectively.

We have a credit control policy, including credit investigation of customers and periodic assessment of credit terms. Sales clerks are directly responsible for liaising with customers on the collection of receivables within the credit terms.

We price our crude oil in U.S. dollars. PRC customers are billed and make actual payments in Renminbi based on the exchange rate prevailing at the bill of lading date, while overseas customers are billed and are required to make payments in U.S. dollars within 30 days of the bill of lading date.

Sales of Natural Gas from Offshore China

Driven by environmental and efficiency concerns, the PRC government is increasingly encouraging residential and industrial use of natural gas to meet primary energy needs. In 1989, in order to encourage natural gas production, the PRC government adopted a favorable royalty treatment, which provides a royalty exemption for natural gas production up to two billion cubic meters (70.6 billion cubic feet or

11.8 million BOE) per year as compared to a royalty exemption available for crude oil production of up to one million tons or approximately seven million BOE per year. The favorable treatment also includes lower royalty rates on incremental increases in natural gas production as compared with the royalty rates for crude oil production.

Since 1989, the PRC government has adopted the following sliding scale of royalty payments of up to 3% of the annual gross production of natural gas:

Annual gross production	Royalty rate
Less than 2 billion cubic meters	0.0%
2-3.5 billion cubic meters	1.0%
3.5-5 billion cubic meters	2.0%
Above 5 billion cubic meters	3.0%

We sell a large portion of our offshore China natural gas production in Hong Kong. The remaining offshore China natural gas production is sold to customers in mainland China. Of the 73.6 billion cubic feet of natural gas that we produced offshore China in the year ended December 31, 2002, 50.3 billion cubic feet was produced from the Yacheng 13-1 gas field in the Western South China Sea. This field is governed by a production sharing contract we entered into with BP and Kufpec. We hold a 51% participating interest in this field. In December 1992, Castle Peak Power in Hong Kong signed a long-term gas supply contract under which it agreed to buy from the partners approximately 102.4 billion cubic feet of natural gas per year on a take-or-pay basis until 2015. Gas prices are quoted and paid in U.S. dollars. The payments are made in U.S. dollars on a monthly basis and are reconciled annually. Castle Peak Power purchased approximately 62.3% of our total offshore China natural gas production for the year ended December 31, 2002. Castle Peak Power is a 60/40 joint venture between ExxonMobil Energy Limited and CLP Power Hong Kong Limited, a public utility company in Hong Kong. The remaining 37.7% of our total offshore China natural gas production in the year ended December 31, 2002 was sold to PRC customers, including Hainan Fertilizer, Hainan Power, Shanghai Gas, Jingxi Chemical, Xinao Gas, Tianjin Binhai Power and Tianjin Binhai Gas.

The price of gas sold to the PRC market is determined by negotiations between us and the buyers based on market conditions. Contracts typically consist of a base price with provisions for annual resets and adjustment formulas which depend on a basket of crude prices, inflation and various other factors.

Procurement of Services

We usually outsource work in connection with the acquisition and processing of seismic data, reservoir studies, well drilling services, wire logging and perforating services and well control and completion service to independent third parties or our CNOOC affiliates.

In the development stage, we normally employ independent third parties for mooring and oil tanker transportation services and both independent third parties and CNOOC affiliates for other services by entering into contracts with them. We conduct a bidding process to determine who we employ to construct platforms, terminals and pipelines, to drill production wells and to transport offshore production facilities. Both independent third parties and CNOOC affiliates participate in the bidding process. We are closely involved in the design and management of services by contractors and exercise extensive control over their performance, including their costs, schedule and quality.

Competition

Domestic Competition

The petroleum industry is highly competitive. We compete in the PRC and in international markets for both customers and capital to finance our exploration, development and production activities. Our principal competitors in the PRC market are PetroChina and Sinopec.

We price our crude oil on the basis of comparable crude oil prices in the international market. The majority of our customers for crude oil are refineries affiliated with Sinopec and PetroChina to which we have been selling crude oil, from time to time, since 1982. Based on our dealings with these refineries, we believe that we have established a stable business relationship with them. In 1998, the PRC government restructured PetroChina and Sinopec into vertically integrated companies with each having both upstream and downstream petroleum businesses and operations.

We are the dominant player in the oil and gas industry offshore China and are the only company authorized to engage in oil and gas exploration and production offshore China in cooperation with foreign parties. We may face increased competition in the future from other petroleum companies in obtaining new PRC offshore oil and gas properties, or, as a result of changes in current PRC laws or regulations permitting an expansion of existing companies' activities or new entrants into the industry.

As part of our business strategy, we intend to expand our natural gas business to meet rapidly increasing domestic demand. Our competitors in the PRC natural gas market are PetroChina and, to a lesser extent, Sinopec. Our principal competitor, PetroChina, is the largest supplier of natural gas in China in terms of volume of natural gas supplied. PetroChina's natural gas business benefits from strong market positions in Beijing, Tianjin, Hebei Province and northern China. We intend to develop related natural gas businesses in China's coastal provinces, where we may face competition from PetroChina and, to a lesser extent, Sinopec. We believe that our extensive natural gas resources base, the proximity of these resources to the markets in China, our relatively advanced technologies and our experienced management team will enable us to compete effectively in the domestic natural gas market.

Foreign Competition and the World Trade Organization

Imports of crude oil are subject to tariffs, import quotas, handling fees and other restrictions. The PRC government also restricts the availability of foreign exchange with which the imports must be purchased. The combination of tariffs, quotas and restrictions on foreign exchange has, to some extent, limited the competition from imported crude oil.

In line with the general progress of its economic reform programs, the PRC government has agreed to reduce import barriers as part of its WTO commitments. As a result of China joining the World Trade Organization as a full member on December 11, 2001, it is required to further reduce its import tariffs and other trade barriers over time, including with respect to certain categories of petroleum and crude oil. All import quotas and licenses for processed oil are expected to be eliminated by 2004. Notwithstanding China's WTO related concessions, crude and processed oil remain, for the time being, subject to restrictions on import rights and only certain designated state-owned enterprises may import crude and processed oil. Sinopec and PetroChina have received permission to import crude oil on their own. At present, there is no timetable for allowing foreign owned or foreign invested entities to import crude or processed oil into the PRC.

The PRC government recently underwent substantial reform. No assurance can be given that the reorganization will not have a significant effect on the implementation of China's WTO commitments.

PRC Fiscal Regimes for Offshore Crude Oil and Natural Gas Activities

We conduct exploration and production operations either independently or jointly with foreign partners under our production sharing contracts. The PRC government has established different fiscal regimes for crude oil and natural gas production from our independent operations and from our production sharing contracts.

Royalties paid to the PRC government are based on our gross production from both independent operations and oil and gas fields under production sharing contracts. The amount of the royalties varies up to 12.5% based on the annual production of the relevant property. The PRC government has provided companies such as ours with a royalty exemption for up to one million tons, or seven million BOE per year, for our crude oil production and for up to 70.6 billion cubic feet, or 11.8 million BOE per year, for our natural gas production. The limits in these exemptions apply to our total production from both independent properties and properties under production sharing contracts. In addition, we pay production taxes to the PRC government equal to 5% of our crude oil and gas produced independently and 5% of our crude oil and gas produced under production sharing contracts.

Under our production sharing contracts, production of crude oil and gas is allocated among us, the foreign partners and the PRC government according to a formula contained in the contracts. Under this formula, a percentage of production under our production sharing contracts is allocated to the PRC government as its share oil. For more information about the allocation of production under the production sharing contracts, see "—Production Sharing Contracts—Offshore China—Production Sharing Formula."

The PRC government recently underwent substantial reform. No assurance can be given that the fiscal regime outlined above will not change significantly in the future.

Production Sharing Contracts

Offshore China

When exploration and production operations offshore China are conducted through a production sharing contract, the operator of the oil or gas field must submit a detailed evaluation report and an overall development plan to CNOOC upon discovery of petroleum reserves. The overall development plan must also be submitted to a joint management committee established under the production sharing contract. After CNOOC confirms the overall development plan, CNOOC submits it to the State Development and Planning Commission for approval. After receiving the governmental approval, the parties to the production sharing contract may begin the commercial development of the petroleum field.

As part of the reorganization in 1999, CNOOC transferred all of its economic interests and obligations under its existing production sharing contracts to us and our subsidiaries. As of December 31, 2002, we had 22 production sharing contracts in the production and development stage, and 11 contracts in the exploration stage.

Under PRC law, the negotiation of a production sharing contract is a function that only a state-owned national company, such as CNOOC, may perform. This function cannot be transferred to us because we are a pure commercial entity. Since the reorganization, under the terms of its undertaking with us, CNOOC, after entering into production sharing contracts with international oil and gas companies, is required to assign immediately to us all of its economic interests and obligations under the production sharing contracts. For further details, see "Relationship with CNOOC and Certain Related Party Transactions."

New production sharing contracts are entered into between CNOOC and foreign partners primarily through bidding organized by CNOOC and, to a lesser extent, through direct negotiation.

Bidding Process

The bidding process typically involves the following steps:

- CNOOC, with the PRC government's approval, determines which blocks are open for bidding and prepares geological information packages and bidding documentation for these blocks;
- CNOOC invites foreign enterprises to bid;

- potential bidders are required to provide information, including estimates of minimum work commitments, exploration costs and percentage of share oil payable to the PRC government; and

- CNOOC evaluates each bid and negotiates a production sharing contract with the successful bidder.

Under CNOOC's undertaking with us, we may participate with CNOOC in all negotiations of new production sharing contracts.

The term of a production sharing contract typically lasts for less than 30 years and has three distinct phases:

- *Exploration.* The exploration period generally lasts for seven consecutive years depending on the size of the contract area, and may be extended with the consent of CNOOC. During this period, exploratory and appraisal work on the exploration block is conducted in order to discover petroleum and to enable the parties to determine the commercial viability of any petroleum discovery.

- *Development.* The development period begins on the date that the overall development plan, which outlines the recoverable reserves and schedule for developing the discovered petroleum reserves, is approved by the relevant PRC regulatory authorities. The development phase ends when the design, construction, installation, drilling and related research work for the realization of petroleum production have been completed.

- *Production.* The production period begins when commercial operations start and usually lasts for 15 years. The production period may be extended upon approval of the PRC government.

Minimum Work Commitment

Under production sharing contracts that involve exploration activities, the foreign partners must complete a minimum amount of work during the exploration period, generally including:

- drilling a minimum number of exploration wells;

- producing a fixed amount of seismic data; and

- incurring a minimum amount of exploration expenditures.

Foreign partners are required to bear all exploration costs during the exploration period. However, such exploration costs can be recovered according to the production sharing formula after commercial discoveries are made and production begins. During the exploration period, foreign partners are required to return 25% of the contract area, excluding the development and production area, to CNOOC at the end of each of the third year and fifth year of the exploration period. At the end of the exploration period, all areas, excluding the development areas, production areas and areas under evaluation, must be returned to CNOOC.

Participating Interests

Under production sharing contracts, CNOOC has the right to take up to a 51% participating interest in any oil or gas field discovered in the contract area and may exercise this right after the foreign partners have made commercially viable discoveries. The foreign partners retain the remaining participating interests.

Production Sharing Formula

A chart illustrating the production sharing formula under our production sharing contracts is shown below.

Percentage of annual gross production	Allocation
5.0%	Production tax payable to the PRC government
0.0% - 12.5%(1)	Royalty oil payable to the PRC government
50.0% - 62.5%(1)	Cost recovery oil allocated according to the following priority: • recovery of current year operating costs by us and foreign partner(s); • recovery of earlier exploration costs by foreign partner(s); • recovery of development costs by us and foreign partner(s) based on participating interests;(3) and • any excess, distributed according to each partner's participating interest.(3)
32.5%(2)	Remainder oil allocated according to the following formula: • (1-X) multiplied by 32.5% represents share oil payable to the PRC government; and • X multiplied by 32.5% represents remainder oil distributed according to each partner's participating interest.(3)

(1) Assumes annual gross production of more than four million metric tons, approximately 30 million barrels of oil. For lower amounts of production, the royalty rate will be lower and the cost recovery will be greater than 50.0% by the amount that the royalty rate is less than 12.5%.
(2) The ratio "X" is agreed in each production sharing contract based on commercial considerations and ranges from 8% to 100%.
(3) See "—Principal Oil and Gas Regions" for our participating interest percentage in each production sharing contract.

The first 5.0% of the annual gross production is paid to the PRC government as production tax. The PRC government is also entitled to a royalty payment equal to the next 0% - 12.5% of the annual gross production based on the following sliding scale:

Annual gross production of oil(1)	Royalty rate
Less than 1 million tons	0.0%
1-1.5 million tons	4.0%
1.5-2.0 million tons	6.0%
2.0-3.0 million tons	8.0%
3.0-4.0 million tons	10.0%
Above 4 million tons	12.5%

(1) The sliding scale royalty for natural gas reaches a maximum at 3.0%.

Depending on the percentage of the PRC government's royalty payment, an amount equal to the next 50.0% to 62.5% of the annual gross production is allocated to the partners for cost recovery purposes. This amount is allocated according to the following priority schedule:

- recovery of operating costs incurred by the partners during the year;

- recovery of exploration costs, excluding interest accrued thereon, incurred but not yet recovered by foreign partners during the exploration period; and

- recovery of development investments incurred but not yet recovered, and interest accrued in the current year, according to each partner's participating interest.

The remaining 32.5% of the annual gross production, which is referred to as the remainder oil, is distributed to each of the PRC government, us and the foreign partners according to a "ratio X" agreed to by CNOOC and the foreign partners in the production sharing contract. An amount of oil and gas equal to the product of the remainder oil and one minus the "ratio X" is first distributed to the PRC government as share oil. The balance of the remainder oil, which is referred to as the allocable remainder oil, is then distributed to us and the foreign partners based on each party's participating interest.

We pay an estimated production tax and royalty to the PRC government each time we ship crude oil production, or on a monthly basis for natural gas production. At the end of each annual period, we calculate the production tax and royalty payable for the year and file this information with the PRC tax bureau. We make adjustments for any overpayment or underpayment of production tax and royalty at the end of the year.

The foreign partners have the right to either take possession of their crude oil for sale in the international market, or sell such crude oil to us for resale in the PRC market.

Management and Operator

Under each production sharing contract, a party will be designated as an operator to undertake the execution of the production sharing contract which includes:

- preparing work programs and budgets;

- procuring equipment and materials relating to operations;

- establishing insurance programs; and

- issuing cash-call notices to the parties to the production sharing contract to raise funds.

A joint management committee, which usually consists of six or eight persons, is set up under each production sharing contract to perform supervisory functions, and each of us and the foreign partners as a group has the right to appoint an equal number of representatives to form the joint management committee. The chairman of the joint management committee is the chief representative designated by us and the vice chairman is the chief representative designated by the foreign partners as a group. The joint management committee has the authority to make decisions on matters including:

- reviewing and approving operational and budgetary plans;

- determining the commercial viability of each petroleum discovery;

- reviewing and adopting the overall development plan; and

- approving significant procurements and expenditures, and insurance coverage.

Daily operations of a property subject to the respective production sharing contract are carried out by the designated operator. The operator is typically responsible for determining and executing operational and budgetary plans and all routine operational matters. Upon discovery of petroleum reserves, the operator is required to submit a detailed overall development plan to the joint management committee.

After the foreign partner has fully recovered its exploration and development costs under production sharing contracts in which the foreign partner is the operator, we have the exclusive right to take over the operation of the particular oil or gas field. With the consent of the foreign partner, we may also take over the operation before the foreign partner has fully recovered its exploration and development costs.

Ownership of Data and Assets

All data, records, samples, vouchers and other original information obtained by foreign partners in the process of exploring, developing and producing offshore petroleum become the property of CNOOC as a state-owned national oil company under PRC law. Through CNOOC, we have unlimited and unrestricted access to the data.

Our foreign partners and us have joint ownership in all of the assets purchased, installed or constructed under the production sharing contract until either:

- the foreign partners have fully recovered their development costs, or

- upon the expiration of the production sharing contract.

After that, as a state-owned national oil company under PRC law, CNOOC will assume ownership of all of the assets under the production sharing contracts, our foreign partners and us retain the exclusive right to use the assets during the production period.

Abandonment Costs

Any party to our production sharing contracts must give prior written notice to the other party or parties if it plans to abandon production of the oil or gas field within the contracted area. If the other party or parties agrees to abandon production from the oil or gas field, all parties pay abandonment costs in proportion to their respective percentage of participating interests in the field. If we decide not to abandon production upon notice from a foreign partner, all of such foreign partner's rights and obligations under the production sharing contract in respect of the oil or gas field, including the responsibilities for payment of abandonment costs, terminate automatically. We bear the abandonment costs if we decide to abandon production after an initial decision to proceed with production. In 2002, we incurred abandonment costs of approximately Rmb 204.0 million.

Production Tax

The PRC production tax rate on the oil and natural gas produced under production sharing contracts is currently 5%.

Overseas

In addition to our production sharing arrangements in the PRC, we also have interests in production sharing contracts and a technical assistance contract in Indonesia, including interests in the Malacca Strait, interests from an acquisition we completed in April 2002 and interests in the Tangguh LNG Project we acquired in January 2003.

Indonesian oil and gas activities are currently governed by Pertamina, the Indonesian state-owned oil and gas company founded in 1968. Under Indonesian law, Pertamina is currently the sole entity authorized to manage Indonesia's oil and gas resources on behalf of the Indonesian government and is empowered to enter into agreements with foreign and domestic companies. Pertamina is expected to become a limited liability company in 2003 pursuant to legislation enacted in 2001.

Pertamina enters into production sharing arrangements with private energy companies whereby such companies explore and develop oil and gas in specified areas in exchange for a percentage interest in the production from the fields in the applicable production sharing area. These production sharing arrangements are mainly governed by production sharing contracts, as well as by technical assistance contracts, each of which is described further below. Upon entering into a production sharing arrangement, the operator commits to spending a specified sum of capital to implement an agreed work program.

Production sharing arrangements in Indonesia are based on the following principles:

- contractors are responsible for all investments (exploration, development and production);

- a contractor's investment and production costs are recovered against production;

- the profit split between the Indonesian government and contractors is based on production after the cost recovery portion;

- ownership of tangible assets remains with the Indonesian government; and

- overall management control lies with Pertamina on behalf of the Indonesian government.

An original production sharing contract is awarded to explore for and to establish commercial hydrocarbon reserves in a specified area prior to commercial production. The contract is awarded for a number of years depending on the contract terms, subject to discovery of commercial quantities of oil and gas within a certain period. The term of the exploration period can generally be extended by agreement between the contractor and Pertamina. The contractor is generally required to relinquish specified percentages of the contract area by specified dates unless such designated areas correspond to the surface area of any field in which oil and gas has been discovered.

Pertamina is typically responsible for managing all production sharing contract operations, assuming and discharging the contractor from all taxes (other than Indonesian corporate taxes, taxes on interest, dividends and royalties and others as set forth in the production sharing contract), obtaining approvals and permits needed by the project and approving the contractor's work program and budget. The responsibilities of a contractor under a production sharing contract generally include advancing necessary funds, furnishing technical aid and preparing and executing the work program and budget. In return, the contractor may freely lift, dispose of and export its share of crude oil and retain the proceeds obtained from its share.

The contractor generally has the right to recover all finding and developing costs, as well as operating costs, in each production sharing contract against available revenues generated after deduction of first tranche oil and gas, or FTP. Under FTP terms, the parties are entitled to take and receive an annually agreed percentage of production from each production zone or formation each year, prior to any deduction for recovery of operating costs, investment credits and handling of production. FTP for each year is generally shared between the Indonesian government and the contractor in accordance with the standard sharing splits. The balance is available for cost recovery. Post-cost recovery, the Indonesian government is entitled to a specified profit share of crude oil production and of natural gas production. Under each production sharing arrangement, the contractor is obligated to pay Indonesian corporate taxes on its specified profit share at the Indonesian corporate tax rate in effect at the time the agreement is executed.

Production sharing contracts in Indonesia have long included a provision known as the domestic market obligation, or DMO, under which a contractor must sell a specified percentage of its crude oil to the local market at a reduced price. After the first five years of a field's production, the contractor is required to supply, the lesser of (i) 25% of the contractor's before-tax share of total crude oil production or (ii) the contractor's share of profit oil. This reduced price varies from contract to contract and is calculated at the point of export.

The new Oil and Gas Law, which came into force on November 23, 2001, stipulates a gas DMO, under which the contractor must sell up to 25% of its gas entitlement to the domestic market, although it is not clear at what price this gas must be sold. Production sharing contract parties have stated that they would prefer that this price be determined on the open market, and that it be recognized that if there are pre-existing gas sale agreements, or if the project produces LNG for export, the obligation to sell gas into the local market may not be feasible.

Technical assistance contracts are awarded when a field has prior or existing production. The oil or gas production is divided into non-shareable and shareable portions. The non-shareable portion represents the expected production from the field at the time the technical assistance contract is signed and is retained by Pertamina. The shareable portion represents the additional production resulting from the operator's investment in the field and is split in the same way as for an original production sharing contract as described above.

Geophysical Survey Agreements

Historically, we conducted our exploration operations through geophysical survey agreements with leading international oil and gas companies as well as independently and through production sharing contracts. As of December 31, 2002, we were not a party to any geophysical survey agreements, but may enter such agreements in the future.

Geophysical survey agreements are designed for foreign petroleum companies to conduct certain geophysical exploration before they decide whether to enter into production sharing contract negotiations with CNOOC. Geophysical survey agreements usually have a term of less than two years. International oil and gas companies must complete all of the work confirmed by both parties in the agreements and bear all the costs and expenses. If a foreign partner decides to enter into a production sharing contract with CNOOC, the costs and expenses that the foreign partner incurs in conducting geophysical survey may be recovered by the foreign partner in the production period subject to our confirmation. CNOOC has the sole ownership of all data and information obtained by the foreign partner during the geophysical survey, and, through CNOOC, we have access to all such data.

Under PRC law, the negotiation of a geophysical survey agreement is a function that only a state-owned national company, such as CNOOC, can perform. As part of its reorganization in 1999, CNOOC transferred to us all its commercial rights under a geophysical survey agreement, which has since been completed. In the future, CNOOC has agreed to assign to us all of its commercial rights under any geophysical survey agreements it enters into with international oil and gas companies.

Operating Hazards and Uninsured Risks

Our operations are subject to hazards and risks inherent in the drilling, production and transportation of crude oil and natural gas, including pipeline ruptures and spills, fires, explosions, encountering formations with abnormal pressures, blowouts, cratering and natural disasters, any of which can result in loss of hydrocarbons, environmental pollution and other damage to our properties and the properties of operators under production sharing contracts. In addition, certain of our crude oil and natural gas operations are located in areas that are subject to tropical weather disturbances, some of which can be severe enough to cause substantial damage to facilities and interrupt production.

As protection against operating hazards, we maintain insurance coverage against some, but not all, potential losses, including the loss of wells, blowouts, pipeline leakage or other damage, certain costs of pollution control and physical damages on certain assets. Our insurance coverage includes oil and gas field properties and construction insurance, marine hull insurance, protection and indemnity insurance, drilling equipment insurance, marine cargo insurance and third party and comprehensive general liability insurance. We also carry business interruption insurance for Pinghu Field. In Indonesia, the operators of the production sharing contracts in which we participate are required by local law to purchase insurance policies customarily taken out by international petroleum companies. As of December 31, 2002, we maintained approximately Rmb 34 billion in insurance coverage and paid an annual insurance premium of approximately Rmb 243 million to maintain that coverage. We believe that our level of insurance is adequate and customary for the PRC petroleum industry and international practices. However, we may not have sufficient coverage for some of the risks we face, either because insurance is not available or because of high premium costs. See “Risk Factors—Risks relating to our business—Exploration, development and production risks and natural disasters affect our operations and could result in losses that are not covered by insurance.”

For the year ended December 31, 2002, the amount of our total losses not covered by insurance was approximately Rmb 107 million.

Research and Development

During each of the three years ended December 31, 2000, 2001 and 2002, we used research and development services provided by CNOOC-affiliates, including China Offshore Oil Research Centre, as well as other international entities. We are developing more efficient and effective approaches to explore for new reserves. Our research efforts have focused on:

- advanced resolution enhancement technology;
- building up exploration and development data bases to improve the efficiency of our research efforts; and
- consolidating multi-discipline data to optimize the selection of exploration sites.

We are also studying various ways of utilizing our existing reserves including:

- building more accurate reservoir models;
- re-processing existing seismic and log data to locate potential areas near existing fields to be integrated into existing production facilities; and
- researching ways to reduce development risks for marginal fields and to group fields into joint developments to share common facilities.

During the three years ended December 31, 2000, 2001 and 2002, we spent approximately Rmb 104 million, Rmb 109 million and Rmb 110 million, respectively, on general research and development activities.

For further information regarding our agreement with the China Offshore Oil Research Center, see “Relationship with CNOOC and Certain Related Party Transactions—Related Party Transactions—Categories of Connected Transactions—Research and development services.”

Environmental Regulation

Our operations in China are required to comply with various PRC environmental laws and regulations administered by the central and local government environmental protection bureaus. We are also subject to the environmental rules introduced by the local PRC governments in whose jurisdictions our onshore logistical support facilities are located. The State Environmental Protection Bureau sets national environmental protection standards and local environmental protection bureaus may set stricter local standards.

The relevant environment protection bureau must approve or review each stage of a project. We must file an environmental impact statement or, in some cases, an environmental impact assessment outline before an approval can be issued. The filing must demonstrate that the project conforms to applicable environmental standards. The relevant environmental protection bureau generally issues approvals and permits for projects using modern pollution control measurement technology.

The PRC national and local environmental laws and regulations impose fees for the discharge of waste substances above prescribed levels, require the payment of fines for serious violations and provide that the PRC national and local governments may at their own discretion close or suspend any facility which fails to comply with orders requiring it to cease or cure operations causing environmental damage.

For the three year period ended December 31, 2002, we experienced a total of two incidents of crude oil discharge with a total volume of approximately 240 barrels being wrongfully discharged and spilled offshore, for which fines in an aggregate amount of Rmb 31,900 (US$3,853) were imposed. None of the incidents nor the aggregate amount of such fines had a material adverse effect on our business or results of operations.

The PRC environmental laws do not currently require offshore petroleum developers to pay abandonment costs. Our financial statements include provisions for costs associated with the dismantlement of oil and gas fields during the years ended December 31, 2000, 2001 and 2002 of approximately Rmb 104 million, Rmb 90 million and Rmb 126 million, respectively.

Environmental protection and prevention costs and expenses in connection with the operation of offshore petroleum exploitation are covered under each individual production sharing contract. Environmental protection and prevention costs and expenses represented approximately 1.425% of our average operating costs relating to projects constructed offshore China during the three years ended December 31, 2002. Each platform has its own environmental protection and safety staff responsible for monitoring and operating the environmental protection equipment. However, no assurance can be given that the PRC government will not impose new or stricter regulations which would require additional environmental protection expenditures.

We are not currently involved in any environmental claims and believes that our environmental protection systems and facilities are adequate for us to comply with applicable national and local environmental protection regulations.

Legal Proceedings

We are not a defendant in any material litigation, claim or arbitration, and know of no pending or threatened proceeding which would have a material adverse effect on our financial condition.

Patents and Trademarks

We own or have licenses to use two trademarks which are of value in the conduct of our business. CNOOC is the owner of the "CNOOC" trademark. Under two non-exclusive license agreements between CNOOC and us, we have obtained the right to use this trademark for a nominal consideration.

Real Properties

Our corporate headquarters is located in Hong Kong. We also lease several other properties from CNOOC in China and Singapore. The rental payments under these lease agreements are determined with reference to market rates. For further details regarding the terms of these leases, see "Relationship with CNOOC and Certain Related Party Transactions—Connected Transactions—Categories of Related Party Transactions—Lease agreement in respect of the Nanshan Terminal," and "—Lease and property management services."

We own the following property interests in the PRC:

- land, various buildings and structures at Xingcheng JZ 20-2 Natural Gas Separating Plant, Dongyao Village, Shuangsu Township, Xingcheng City, Liaoning Province;

- land, various buildings and structures located at Boxi Processing Plant, South of Jintang Subway, Tanggu District, Tianjin City;

- land, various buildings and structures at Weizhou Terminal Processing Plant, Weizhou Island, Weizhou Town, Beihai City, Guangxi Zhuang Autonomous Region; and

- a parcel of land at Suizhong 36-1 Base, Xiaolihuang Village, Gaoling Town, Suizhong County, Liaoning Province.

Employees and Employee Benefits

During the years ended December 31, 2000, 2001 and 2002, we employed 1,007 persons, 1,081 persons and 2,047 persons, respectively. Our number of employees increased significantly in 2002 due to the acquisition of our interests in oil and gas projects in Indonesia during that year. Of the 2,047 employees we employed as of December 31, 2002, approximately 81.8% were involved in petroleum exploration, development and production activities, approximately 10.9% were involved in accounts and finance work and the remainder were senior management, coordinators of production sharing contracts and safety and environmental supervisors. Workers for the operation of the oil and gas fields, maintenance personnel and ancillary service workers are hired on a contract basis.

We have a trade union that:

- protects employees' rights;

- organizes educational programs;

- assists in the fulfillment of economic objectives;

- encourages employee participation in management decisions; and

- assists in mediating disputes between us and individual employees.

We have not been subjected to any strikes or other labor disturbances and believe that relations with our employees are good.

The total remuneration of employees includes salary, bonuses and allowances. Bonus for any given period is based primarily on individual and our performance. Employees also receive subsidized housing, health benefits and other miscellaneous subsidies.

We have implemented an occupational health and safety program similar to that employed by other international oil and gas companies. Under this program, we closely monitor and record health and safety incidents and promptly report them to government agencies and organizations. On March 15, 2000, we finalized and implemented our occupational health and safety program. We believe this program is broadly in line with the United States government's Occupational Safety & Health Administration guidelines.

All full-time employees in the PRC are covered by a government-regulated pension. The PRC government is responsible for the pension of these retired employees. We are required to contribute monthly an average of approximately 12% to 22.5% of our employees' basic salaries, with each employee contributing 4% to 7% of his or her base salary for retirement. The contributions vary from region to region.

Our Indonesian subsidiaries employ approximately 1,000 employees, including approximately 30 managerial staff and technicians. We provide employee benefits to expatriate staff that we believe to be in line with customary international practices. Our non-expatriate employees in Indonesia enjoy welfare benefits mandated by Indonesia labor laws.

For further details regarding retirement benefits, see note 31 to our consolidated financial statements beginning on page F-1.

Health, Safety and Environmental Policy

We place much importance on our health, safety and environmental, or HSE, policy. In 2002, we implemented an overall HSE management system in each of our production divisions offshore China and also established an HSE policy for our overseas operations. The HSE policy for our operations offshore China focuses on increasing our employees' awareness of health, safety and environmental issues in the workplace. We regularly organize training courses and conduct environmental and safety drills. We also closely monitor weather forecasts and track hazardous weather conditions that may affect our production facilities.

The HSE policy for our overseas operations includes setting annual safety targets, conducting year-end evaluations, creating emergency contact lists, recording incidents accurately and reviewing management performance in this area.

In 2002, we established a "System for Determining Accountability in the Event of a Major Production Accident," and implemented an "Evaluation System for Health, Safety and Environmental Protection." We also launched a "Safety Activity of the Month" program and, together with our production sharing contract partners, hired a foreign professional to conduct safety inspects on the helicopters used in our operations offshore China.

Human Resources Development

As an oil and gas exploration and development company operating in highly competitive markets, our success depends in large part on our employees' abilities. We devote significant resources to training our technical employees. During 2002, we held 388 training workshops, which were attended by 8,482 participants. We are also dedicated to developing the skills of our senior management. In 2002, we partnered with the New York University Leonard N. Stern School of Business to organize a financial training workshop for our senior management. In addition, we organized an industry specific training program with Oklahoma State University, and a management workshop for our senior managers with the China-Europe International Business School.

MANAGEMENT

Directors and Executive Officers

In accordance with Hong Kong law and our articles of association, our affairs are managed by our board of directors. The board of directors has nine members, including four independent non-executive directors.

Our current directors and senior officers are as follows:

Name	Age as of December 31, 2002	Position
Liucheng Wei.............	56	Chairman of the Board of Directors and Chief Executive Officer
Chengyu Fu	51	Director
Longsheng Jiang.........	57	Director
Shouwei Zhou............	51	Director and President
Han Luo.....................	49	Director
Chak Kwong So	58	Independent Non-executive Director
Sung Hong Chiu.........	56	Independent Non-executive Director
Kenneth Courtis..........	57	Independent Non-executive Director
Erwin Schurtenberger .	63	Independent Non-executive Director
Ke Ru	59	Executive Vice President
Yunshi Cao	57	Senior Vice President, Company Secretary and General Counsel
Mark Qiu	39	Chief Financial Officer and Senior Vice President
Hua Yang	41	Senior Vice President
Wei Chen	45	Senior Vice President

Mr. Kenneth Courtis and Dr. Erwin Schurtenberger, two of our independent non-executive directors, were appointed in November 2002. Mr. Longsheng Jiang and Mr. Han Luo were appointed in December 2000. All other directors, including other independent non-executive directors, were appointed in September 1999.

We have a management team with extensive experience in the oil and gas industry. As a result of our cooperation with international oil and gas companies, the management team and staff have had the opportunity to work closely with foreign partners both within and outside China. Such opportunities, in conjunction with management exchange programs with foreign partners, have provided valuable training to our personnel in international management practices. A description of the business experience and present position of each director and executive officer is provided below. Our principal executive offices are located at 65th Floor, Bank of China Tower, One Garden Road, Central, Hong Kong.

Directors

Liucheng Wei received a B.S. degree from China Petroleum Institute and a graduate degree in Business Administration from the Chinese Academy of Social Sciences. He is a senior economist and has over 30 years' experience in the oil industry in the PRC. He was appointed as Chairman of the Board of Directors and Chief Executive Officer of our company in September 1999. Mr. Wei is also the President of CNOOC, a position he has held since November 1998. From 1993 to 1998, he served as Vice President of CNOOC. He joined CNOOC in 1982.

Chengyu Fu received a B.S. degree from Northeast Petroleum Institute in China and a master's degree in petroleum engineering from the University of Southern California in the United States. He has over 28 years' experience in the petroleum industry in the PRC. He was appointed as director in September 1999 and previously served as our Chief Operating Officer and President. He currently is a director and the Chief Executive Officer and Chairman of China Oilfield Services Limited, another majority-owned subsidiary of CNOOC. Mr. Fu is also a Vice President of CNOOC. In 1999, Mr. Fu was the General Manager of China Offshore Oil Eastern South China Sea Corporation, a subsidiary of CNOOC. From 1995 to 1999, he served as Vice President and General Manager of Xijiang Operations of ConocoPhillips China Inc. From 1994 to 1995, he served as Deputy General Manager of China Offshore Oil Eastern South China Sea Corporation. He joined CNOOC in 1982.

Longsheng Jiang received a B.S. degree from Beijing Petroleum Institute in China. He has over 31 years' experience in the oil and gas industry in the PRC. He was appointed as our director in December 2000. From 1982 to 1994, Mr. Jiang served as chief engineer of China Offshore Oil Western South China Sea Corporation. From 1995 to 1998, he was the general manager of China Offshore Oil Southern Drilling Company. Mr. Jiang is a Vice President of CNOOC, a position he has held since 1998. He joined CNOOC in 1982.

Shouwei Zhou received a Ph.D. degree from Southwest China Petroleum Institute and is a senior engineer. He was appointed as our director and Executive Vice President in September 1999 and as President in August 2002. Mr. Zhou is also a Vice President of CNOOC. From 1994 to 1999, Mr. Zhou was the Deputy Manager of China Offshore Oil Bohai Corporation, a subsidiary of CNOOC, and has been the President of China Offshore Oil Bohai Corporation since 1999. He joined CNOOC in 1982.

Han Luo received a doctor's degree from China Petroleum University. He has over 26 years' experience in the oil industry in the PRC. He was appointed as our director in December 2000. From 1993 to 1998, Mr. Luo served as Vice President of China Offshore Oil Eastern South China Sea Corporation and concurrently the chief representative of CNOOC in the CACT operating group, and executive Vice President of China Offshore Oil East China Sea Corporation. In 1999, he was the general manager of CNOOC China-Shanghai Branch. Mr. Luo is a Vice President of CNOOC, a position he has held since 2000. He joined CNOOC in 1982.

Independent Non-executive Directors

Chak Kwong So is the Chairman of the board of directors and chief executive of the MTR Corporation Limited. He has been a Non-Executive Director of The Hongkong and Shanghai Banking Corporation Limited since January 2000. Mr. So began his career with the Hong Kong government. He joined the private sector in 1978, serving in various posts in the securities, finance and property industries. Mr. So also served as Executive Director of the Hong Kong Trade Development Council from 1985 to 1992. Mr. So is the President of the Chartered Institute of Logistics and Transport. He is also a Vice President of the International Association of Public Transport and is the Chairman of its Asia-Pacific Division. He also serves on a number of other committees and organizations, including the Hong Kong/European Union Business Cooperation Committee, Independent Commission Against Corruption—Operations Review Committee, the Employers' Federation of Hong Kong, the Hong Kong Management Association and the Community Chest of Hong Kong.

Sung Hong Chiu received an LL.B. degree from the University of Sydney. He is admitted as a solicitor of the Supreme Court of New South Wales and the High Court of Australia. He has over 26 years' experience in legal practice and is a director of a listed company in Australia. Mr. Chiu is the founding member of the Board of Trustees of the Australian Nursing Home Foundation and served as the General Secretary of the Australian Chinese Community Association of New South Wales.

Kenneth Courtis is Managing Director of Goldman Sachs and Vice Chairman of Goldman Sachs Asia. He specializes in economics and strategy throughout the Asia-Pacific region as well as in Europe and North America. After graduating with honors from Glendon College in Toronto, Mr. Courtis received an M.A. in international economics from Sussex University, England, an M.B.A. in finance and strategy from the European Institute of Business Administration and a Ph.D. degree from the Institute of Economic and Political Studies in Paris. Prior to joining Goldman Sachs, he served as Chief Asia Economist and Strategist for Deutsche Bank.

Erwin Schurtenberger has served as the Ambassador of Switzerland to the People's Republic of China, the Democratic People's Republic of Korea, the Republic of Mongolia and the Republic of Iraq. He joined the Swiss Foreign Services in 1969. He has also been an independent business advisor to various European multinationals, American groups and humanitarian aid organizations such as Credit Suisse Financial Services, Novartis and Bunge. Dr. Schurtenberger currently serves on the board of directors of Robert Bosch RBint., Buhler Group Switzerland, Firmenich, Sire Holding, CIBA China and Winterthur Insurances (Asia). He is also a senior advisor to the China Training Center for Senior Personnel Management Officials. Dr. Schurtenberger received a Ph.D. degree in economics and was trained in political science and philosophy.

Company Secretary

Yunshi Cao is our Company Secretary, General Counsel and a Senior Vice President. He is also the General Counsel and the Director of the Legal Department of CNOOC, a position he has held since 1999. He joined CNOOC in 1982. Mr. Cao is a senior economist and licensed lawyer in the PRC. He has extensive experience in production sharing contracts and over 30 years' experience in the oil industry. He received a B.S. degree from the China Petroleum Institute and studied law at Columbia University School of Law.

Senior Management

Ke Ru serves as an Executive Vice President of our company and is responsible for our offshore petroleum exploration. Mr. Ru is a geologist, graduated from China Petroleum Institute and was a Visiting Scholar at the University of Oklahoma. He has over 30 years' experience in exploration, geophysical and geological research in China. He joined CNOOC in 1982 and was President of the Research Institute of China Offshore Oil Western South China Sea Corporation and Chief Geologist of CNOOC.

Mark Qiu serves as our Chief Financial Officer and a Senior Vice President. Prior to joining us, Dr. Qiu worked at Salomon Smith Barney and last served as the Head of Oil and Gas Investment Banking Group Asia. Prior to that, Dr. Qiu served as a Vice President at ARCO China Inc., a subsidiary of Atlantic Richfield Corporation (ARCO) and later as a Corporate Federal Government Relations Director of ARCO in Washington D.C. He was a Sloan Fellow and received an MBA degree from Massachusetts Institute of Technology and a doctoral and master degree in Decision Sciences from the University of Texas at Arlington. Dr. Qiu joined CNOOC in 2001.

Hua Yang is a Senior Vice President of our company and President of CNOOC International Limited. He is a senior engineer and is responsible for our overseas operations. He received his B.S. degree from China Petroleum Institute. He has over 20 years' experience in petroleum exploration and production. Mr. Yang joined CNOOC in 1982 and was Acting Director of the Overseas Development Department of CNOOC.

Wei Chen is a Senior Vice President and General Manager of our Administration Department. He is a senior engineer and is responsible for our administration, foreign affairs, human resources and material procurement. He received his B.S. degree from China Petroleum University and holds an M.B.A. degree from Tsinghua University. He has over 20 years' experience in petroleum exploration and production. Mr.

Chen joined CNOOC in 1984 and previously served as the Deputy Manager for the development department of the CNOOC Research Centre, the Deputy Manager of the Overseas Research Department, the Manager of the Information Department, the Deputy Director of the Research Centre and the General Manager of our Human Resources Department.

Audit and Other Committees

The audit committee consists of two independent non-executive directors. Its primary duties are to review and supervise the financial reporting process and our internal control system.

We have established a compensation committee. It consists of three independent non-executive directors. The primary duties of the compensation committee are to manage share option schemes and to formulate our remuneration policy.

International Advisory Board

On October 29, 2001, we announced the establishment of an International Advisory Board with globally well-respected political figures and corporate leaders as members. The purpose of the International Advisory Board is to provide the management with strategic advice on world events and macro issues that may impact our development. Kenneth Courtis and Erwin Schurtenberger, two of our independent non-executive directors, were members of the International Advisory Board prior to their election to the board of directors in November 2002. On March 20, 2003, we announced that Peter Sutherland and Cornelius Herkstroter have joined our International Advisory Board to fill the vacancies created by the departures of Mr. Curtis and Mr. Schurtenberger.

Set forth below is information on the current members of our International Advisory Board.

Name	Biographical Information
Cornelius Herkstroter	Former Chairman of the Committee of Managing Directors of the Royal Dutch Shell Group of Companies and President of Royal Dutch Petroleum Company. He spent his entire career in the mineral and resources industry, primarily with Royal Dutch Shell. He holds various board and advisory positions with several global corporations and organizations.
Henry A. Kissinger	56th Secretary of State of the United States and former Assistant to the President for National Security Affairs. Born in Germany in May 1923, he received his Ph.D. degree from Harvard University in 1954.
Simon Murray	Former Executive Chairman of Asia Pacific for the Deutsche Bank Group. He was the founder of Davenham Investments, a project advisory company. He became the Group Managing Director of Hutchison Whampoa in 1984. He is currently a Director of a number of companies that include Hutchison Whampoa, Cheung Kong Holdings, Tommy Hilfiger in the United States and Vivendi Universal in France.
Edward S. Steinfeld	Assistant professor at the MIT Sloan School of Management. He received both his undergraduate and doctoral training at Harvard University. A China specialist, he has conducted extensive firm-level research in China.
Peter Sutherland	Chairman and Managing Director of Goldman Sachs International and non-executive Chairman of BP plc. He served as Director General of the World Trade Organization from 1993 to 1995 and is a distinguished leader in world trade and commerce. He holds various board and advisory positions with several global corporations and organizations.

Share Option Scheme

On June 6, 2002, we adopted a new share option scheme to comply with new requirements issued by the Hong Kong Stock Exchange. Our new share option scheme provides for the grant of options to our employees, including non-executive directors. Under this share option scheme, the compensation committee of our board of directors may from time to time propose to the board of directors to award a specific member of share options to particular employees. Options granted under this scheme are exercisable in accordance with the following vesting schedule:

- one-third of the shares underlying the option vest on the first anniversary of the date of the grant;

- one-third of the shares underlying the option vest on the second anniversary of the date of the grant; and

- one-third of the shares underlying the option vest on the third anniversary of the date of the grant.

The option period may commence on any day after the option is granted, but must end within 10 years from the date of the grant. The maximum number of shares to be issued under our share option scheme may not exceed 10% of our issued share capital as of June 6, 2002. If we increase our share capital, our shareholders in a general meeting may increase the maximum number of shares that may be issued under our share option scheme provided such increase does not exceed 10% of our issued share capital as of the date of such increase. The total number of shares that may be issued upon exercise of all outstanding options, however, may not exceed 30% of our issued share capital under any circumstances.

Unless separately approved by our shareholders in a general meeting with the relevant participant and his or her associates abstaining from voting, the maximum number of shares in respect of which options may be granted to any participant together with any shares issued in respect of options which have been exercised by that participant and any shares which would be issued upon the exercise of the outstanding options granted to that participant in any 12 month period up to the date of the latest grant may not exceed 1% of our issued share capital.

Under the new share option scheme, the consideration payable by a participant for the grant of an option is HK$1.00. The exercise price for our share options is determined by our board of directors at the grant date, but may not be set below a minimum price which is the highest of:

- the closing price of our shares on the Hong Kong Stock Exchange as stated in its quotation sheets on the date of the grant of the options;

- the average closing price of our shares on the Hong Kong Stock Exchange as stated in its quotation sheets for the five trading days immediately preceding the date of the grant of the options; or

- the nominal value of one share.

Any grant of share options to a connected person (as defined in the Hong Kong Stock Exchange listing rules) must be approved by our independent non-executive directors (excluding any independent non-executive director who may be the recipient of the options).

On March 12, 2001, our board of directors, under a pre-global offering share option scheme adopted on February 4, 2001, granted options in 4,620,000 shares to directors and senior management at an exercise price of HK$5.95 per share. The options granted under this scheme are exercisable in accordance with the following vesting schedule:

- 50% of the shares underlying the option vest 18 months after the date of the grant; and
- 50% of the shares underlying the option vest 30 months after the date of the grant.

On August 27, 2001, under the original share option scheme that was adopted shortly after our initial public offering, our board of directors granted options in 8,820,000 shares to directors and senior management at an exercise price of HK$6.16 per share. The vesting schedule for these options is the same as the vesting schedule under our current share option scheme. On February 24, 2003, our board of directors granted options in 8,410,000 shares to members of our senior management at an exercise price HK$10.54 per share.

For further details about our share option scheme, see notes 29 and 37(ii) to our consolidated financial statements beginning on page F-1.

RELATIONSHIP WITH CNOOC AND CERTAIN RELATED PARTY TRANSACTIONS

Ownership by CNOOC

CNOOC indirectly owned or controlled an aggregate of approximately 70.6% of our shares as of March 31, 2003. Accordingly, it is able to exercise all the rights of a controlling shareholder, including electing the directors and voting to amend our articles of association. Although CNOOC retains a controlling interest in us, our board of directors remains responsible for the management of our business.

The PRC government established CNOOC as the state-owned offshore petroleum company of China in 1982 under the Regulation of the People's Republic of China on Exploitation of Offshore Petroleum Resources in Cooperation with Foreign Enterprises, whereby CNOOC assumed overall responsibility for the administration and development of PRC offshore petroleum operations with foreign oil and gas companies. Prior to March 2003, CNOOC was regulated and supervised by the State Economic and Trade Commission. Since March 2003, the PRC government has undergone substantial reform. The State Economic and Trade Commission has been succeeded by the newly established State Development and Reform Commission.

Prior to CNOOC's internal business reorganization, which took effect as of October 1, 1999, CNOOC and its various subsidiaries and affiliates performed commercial and administrative functions, including:

- exercising the exclusive right to cooperate with foreign partners in offshore petroleum exploration, development, production and sales activities, and taking up to a 51% participating interest in production sharing contracts;
- organizing international bidding for offshore petroleum exploitation;
- conducting independent exploration, development, production and sales activities in independently operated oil and gas fields offshore China;
- awarding projects to and signing bilateral contracts with foreign partners for offshore petroleum exploitation;
- reviewing and confirming appraisal reports and overall development plans required under production sharing contracts; and
- obtaining from the PRC government all approvals, permits, licenses, consents and special policies necessary under production sharing contracts.

Reorganization

We were incorporated with limited liability on August 20, 1999 in Hong Kong under the Companies Ordinance. Our business registration number in Hong Kong is 685974. Under section three of our memorandum of association, we have the capacity and the rights, powers and privileges of a natural person and in addition and without limit, we may do anything which we are permitted to do by any enactment or rule of law.

Under the reorganization in 1999, CNOOC transferred all of its then current operational and commercial interests in its offshore petroleum business to us. As a result, we and our subsidiaries are the only vehicle through which CNOOC engages in petroleum exploration, development, production and sales activities both within and outside China.

The assets and liabilities primarily relating to the offshore petroleum business that were transferred to us in the reorganization included:

- 37 production sharing contracts and one geophysical survey agreement;

- eight independent development and production projects;
- a 30% interest in Shanghai Petroleum and Natural Gas Company Limited;
- the land use rights to terminal facilities in Nanhai, Weizhou and the western part of the Bohai Bay; and
- loans from, and swap agreements with, various PRC and foreign banks.

In addition, CNOOC transferred 917 employees to us to facilitate the transfer of the oil and natural gas businesses previously operated by CNOOC.

CNOOC has retained its commercial interests in operations and projects not related to oil and gas exploration and production, including:

- a petrochemical project in Huizhou, Guangdong Province;
- a fertilizer plant in Hainan Province; and
- a liquefied natural gas project in Guangdong Province.

CNOOC also retained all of its administrative functions, which it performed prior to the reorganization, including:

- organizing international bidding for offshore petroleum exploitation;
- awarding projects to and signing bilateral contracts with foreign partners for offshore petroleum exploitation;
- approving any extension of the period for the completion of the appraisal work on petroleum discovery under the production sharing contracts; and
- submitting the overall development plans, reports of the oil and gas fields and the environmental impact statements related to the production sharing contracts to the PRC governmental authorities.

Undertakings

CNOOC has undertaken to us that:

- we will enjoy the exclusive right to exercise all of CNOOC's commercial and operational rights under the PRC laws and regulations relating to the exploration, development, production and sales of the PRC offshore oil and natural gas;
- it will transfer to us all of CNOOC's rights and obligations under any new production sharing contracts and geophysical exploration operations, except those relating to CNOOC's administrative functions;
- neither CNOOC nor any of its affiliates will engage or be interested, directly or indirectly, in oil and natural gas exploration, development, production and sales in or outside the PRC;
- we will be able to participate jointly with CNOOC in negotiating new production sharing contracts and to set out our views to CNOOC on the proposed terms of new production sharing contracts;
- we will have unlimited and unrestricted access to all data, records, samples and other original data owned by CNOOC relating to oil and natural gas resources;

- we will have an option, for which no consideration will be payable by us to CNOOC, to make any investment in liquefied natural gas projects that CNOOC has invested or proposes to invest, and CNOOC will at its own expense help us to procure all necessary government approvals needed for our participation in these projects; and

- we will have an option, for which no consideration will be payable by us to CNOOC, to participate in other businesses related to natural gas in which CNOOC has invested or proposes to invest, and CNOOC will at its own expense procure all necessary government approvals needed for our participation in such business.

The undertakings from CNOOC will cease to have any effect:

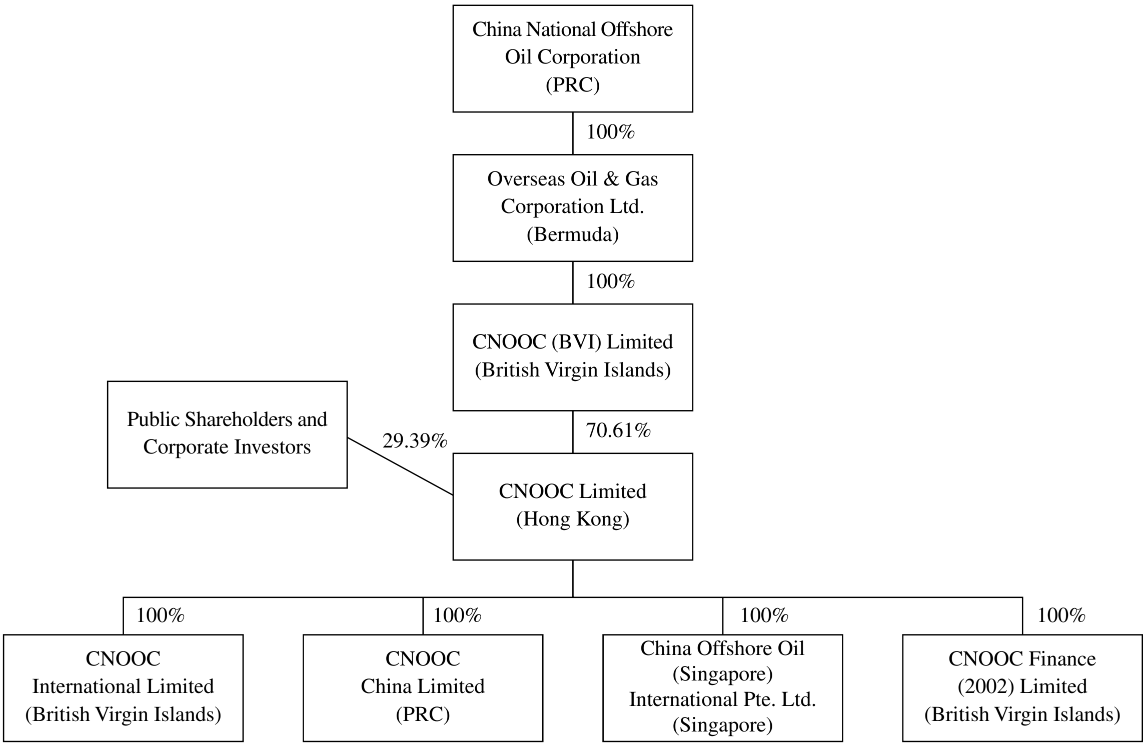
- if we become a wholly owned subsidiary of CNOOC;

- if our securities cease to be listed on any stock exchange or automated trading system; or

- 12 months after CNOOC or any other PRC government-controlled entity ceases to be our controlling shareholder.

Corporate Structure

The following chart sets forth our corporate structure as of December 31, 2002.



The issuer was incorporated in the British Virgin Islands on April 2, 2003 and is not included in the chart above. The issuer is our 100% wholly owned finance subsidiary. See "The Issuer."

Related Party Transactions

We regularly enter into transactions with related parties, including CNOOC and its subsidiaries. Since CNOOC indirectly owns an aggregate of approximately 70.6% of our issued share capital, some of these transactions constitute connected transactions under the Hong Kong Stock Exchange listing rules and are regulated by the Hong Kong Stock Exchange.

Under the Hong Kong Stock Exchange listing rules, each connected transaction normally would require full disclosure and the prior approval of our independent shareholders. However, since the connected transactions are carried out in the ordinary and usual course of business and occur on a regular basis on normal commercial terms and on terms that are fair and reasonable as far as our shareholders are concerned, the Hong Kong Stock Exchange has allowed us to apply for a waiver from strict compliance with the listing rules to engage in these transactions. The waiver typically categorizes and limits the value of our various connected transactions.

We originally obtained a waiver from the Hong Kong Stock Exchange on April 3, 2001, shortly after our shares were listed on the Hong Kong Stock Exchange. This waiver expired on December 31, 2002, and we obtained a new waiver from the Hong Kong Stock Exchange on January 7, 2003. The new waiver covers the period from January 1, 2003 to December 31, 2005.

The Hong Kong Stock Exchange required us to obtain the approval of our independent shareholders for the proposed connected transactions before it would grant us the new waiver. As an interested shareholder, CNOOC abstained from the shareholder vote on the proposed connected transactions. We appointed an independent board committee to advise the independent shareholders on whether the terms of the proposed connected transactions were in our interest and were fair and reasonable so far as the independent shareholders were concerned. An independent financial advisor, Cazenove Asia Limited, advised the independent board committee on the terms of the connected transactions. Our independent shareholders approved the proposed connected transactions at an extraordinary general meeting on December 23, 2002.

Categories of Connected Transactions

Our ongoing connected transactions fall into the following eight categories:

- Contracts with foreign petroleum companies;
- Trademark license agreements;
- Lease agreement in respect of the Nanshan terminal;
- Provision of materials, utilities and ancillary services;
- Technical services;
- Research and development services;
- Lease and property management services; and
- Sales of crude oil, condensate oil and liquefied petroleum gas.

Contracts with foreign petroleum companies. As part of our restructuring, and in preparation for our initial public offering, CNOOC transferred to us all of its rights and obligations under all existing and any future production sharing contracts with various international oil and gas companies. As required by PRC law, CNOOC retained certain administrative functions and remains and will remain a party to the production sharing contracts. PRC law requires a State-run entity, such as CNOOC, to negotiate and conclude an initial production sharing contract with a foreign partner offshore China. New production sharing contracts continue to be entered into between CNOOC and foreign partners, primarily through bidding organized by CNOOC and, to a lesser extent, through direct negotiation.

Trademark license agreements. CNOOC has licensed to us two "CNOOC" trademarks under non-exclusive license agreements that will expire on September 8, 2008. We paid a nominal amount of Rmb 1,000 for each of the trademarks. The registrations for the two trademarks will expire on December 6, 2008 and April 20, 2009, respectively. CNOOC has undertaken that so long as it is our controlling shareholder, it will renew the trademark registrations to enable us to continue using them without any additional consideration.

Lease agreement in respect of the Nanshan Terminal. Under an agreement dated September 9, 1999, CNOOC has granted us the right to use the Nanshan Terminal, Yacheng 13-1, free-of-charge for a period of 20 years. We use the property to process natural gas.

Provision of materials, utilities and ancillary services. Various CNOOC subsidiaries provide us with the use of certain facilities and ancillary services and products, including:

- materials for offshore oil and gas production (including cement, diesel oil, mud, fuels, barite and paint);
- oil and gas production labor services;
- warehousing and storage;
- road transportation services;
- telecommunication and network services;
- wharf services;
- construction services, including the construction of roads, piers, buildings, plants and embankment;
- major equipment maintenance and repair works;
- medical, child care and social welfare services;
- water, electricity and heat supply;
- security and fire services; technical training; accommodation;
- repair and maintenance of buildings; and
- catering services.

Under agreements between these CNOOC subsidiaries and us, the facilities and ancillary products and services are provided at:

(i) state-prescribed prices; or

(ii) where there is no state-prescribed price, market prices, including the local or national market prices; or

(iii) when neither (i) nor (ii) is applicable, the cost to CNOOC's associates of providing the relevant materials, utilities and ancillary services, including the cost of sourcing or purchasing from third parties, plus a margin of not more than 5%, before any applicable taxes.

The prices, volumes and other terms of the agreements are reviewed by the parties annually. If any of the terms are amended, the parties must enter into a supplemental agreement no later than 60 days prior to the end of the financial year preceding the financial year in which the amendment takes effect. If the parties fail to reach an agreement by then, the existing terms of the supply agreement will continue to apply until the parties agree on the terms of the supplemental agreement. We have undertaken to the Hong Kong Stock Exchange that we will comply with the provisions of the listing rules with respect to any supplemental agreements.

For the three years ended December 31, 2002, the amounts we paid to CNOOC subsidiaries for these services were approximately Rmb 793 million, Rmb 815 million and Rmb 789 million, respectively, representing 3.3%, 3.9% and 3.0%, respectively, of our total revenues.

Technical services. Various CNOOC subsidiaries, including China Oilfield Services Limited and CNOOC Offshore Oil Engineering Company Limited, provide us with technical and labor services for its offshore oil and gas production activities, including:

- offshore drilling;
- ship tugging, oil tanker transportation and security services;
- well surveys, well logging, well cementing and other related technical services;
- collection of geophysical data, ocean geological prospecting, and data processing;
- platform fabrication service and maintenance; and
- design, construction, installation and test of offshore and onshore production facilities.

For the three years ended December 31, 2002, the amounts we paid to CNOOC subsidiaries for these services were approximately Rmb 2,038 million, Rmb 2,367 million and Rmb 3,280 million, respectively, representing 8.4%, 11.4% and 12.4%, respectively, of our total revenue. We generally conduct an open bidding process to select these services providers and the charges for these services are based on arm's-length negotiations between the parties and reflect considerations such as volume of sales, length of contracts, overall customer relationship and other market factors.

Research and development services. Various CNOOC subsidiaries and affiliates, including the China Offshore Oil Research Centre (the "Centre"), provide us with research and development services, including:

- geophysical exploration services;
- seismic data processing;
- comprehensive exploration research services; and
- information technology services.

We pay the Centre an annual fee of Rmb 110 million for general research and development services. We occasionally also hire the Centre through an open bidding process for specific research and development projects. For specific projects during the three years ended December 31, 2002, we paid the Centre approximately Rmb 52 million, Rmb 50 million and Rmb 57 million, respectively, representing approximately 0.2%, 0.2% and 0.2%, respectively, of our total revenues.

Lease and property management services. We have entered into lease and property management agreements with CNOOC and its subsidiaries for premises located in Beijing, Tianjin, Zhanjiang, Shanghai and Shenzhen in the PRC and in Singapore. Most of the premises are necessary for our operations, and the agreements are based on normal commercial terms. For the three years ended December 31, 2002, the aggregate rentals and management fees payable by us to CNOOC and its subsidiaries were approximately Rmb 49 million, Rmb 46 million and Rmb 54 million, respectively.

Sales of crude oil, condensate oil and liquefied petroleum gas. We sell crude oil, condensate oil and liquefied petroleum gas to CNOOC affiliates that engage in the downstream petroleum business. The prices for these products are based on prices in the international market. For the three years ended December 31, 2002, CNOOC subsidiaries paid us approximately Rmb 508 million, Rmb 1,814 million and Rmb 4,362 million, respectively, representing approximately 2.1%, 8.7% and 16.5% of our total revenues for the respective periods.

Waiver Conditions

The new waiver granted to us by the Hong Kong Stock Exchange contains the following typical conditions:

i. in relation to the ongoing connected transactions referred to in the paragraphs headed "Contracts with foreign petroleum companies," "Trademark license agreements" and "Lease agreement in respect of the Nanshan Terminal" the transactions, and the respective agreements (if any) governing such transactions, must be on terms that are fair and reasonable so far as our shareholders are concerned and in relation to the ongoing connected transactions referred to in the paragraphs headed "Provision of materials, utilities and ancillary services," "Technical services," "Research and development services," "Lease and property management services" and "Sales of crude oil, condensate oil and liquefied petroleum gas" the transactions, and the respective agreements (if any) governing such transactions must be:

   a. entered into by us in our ordinary and usual course of business;

   b. either on normal commercial terms or, where there is no available comparison, on terms no less favorable than those available to or from independent third parties; and

   c. on terms that are fair and reasonable so far as our shareholders are concerned;

ii. brief details of the ongoing connected transactions in each year as required by Rule 14.25(1)(A) to (D) of the Hong Kong Stock Exchange listing rules (i.e., the date or period of the transaction, the parties thereto and a description of their connected relationship, a brief description of the transaction and the purpose of the transaction, the total consideration and the terms, and the nature and the extent of the interest of the connected person in the transaction), must be disclosed in our annual report and accounts for the relevant year;

iii. our independent non-executive directors must review annually the transactions and confirm, in our annual report and accounts for the year in question, that such transactions have been conducted in the manner stated in (i) above and, where applicable, within the annual limit stated in (v) below;

iv. our auditors must carry out review procedures annually in relation to the connected transactions and must confirm in writing whether the transactions:

a. received the approval of our board of directors;

b. have been entered into in accordance with the pricing policies as stated in our financial statements; and

c. have been entered into in accordance with the terms of the agreement governing the transactions or, where there is no agreement, on terms that are not less favorable than terms available to or from independent third parties.

For the purpose of the above review by our auditors, CNOOC has undertaken to us that it will provide the auditors with access to its relevant accounting records;

v. the aggregate annual volume of transactions shall not exceed the proposed annual limits set out in the following table:

Transaction	**Annual Limit**	**Basis for Determining the Annual Limits**
Materials, utilities and ancillary services supply agreements	10% of our audited consolidated total revenues in the preceding financial year	Under our initial waiver, the annual limit for this category was 3.91% of our total revenues. The new annual limit is based on past transaction amounts and future projections. We believe that new projects warrant the additional flexibility.
Technical services	In respect of the three financial years ending December 31, 2005, Rmb 5,853 million, Rmb 7,338 million and Rmb 4,880 million, respectively	Our original waiver from the Hong Kong Stock Exchange limited this category of connected transactions to Rmb 2,367 million for the year ended December 31, 2002. The new annual limits take into consideration continued expansion of existing oilfields and the development of two new oilfields in the Bohai Bay, which are expected to enter production by the end of year 2004.
Research and development services for particular projects	In respect of the three financial years ending December 31, 2005, Rmb 141 million, Rmb 148 million and Rmb 153 million, respectively	Under our initial waiver, the limit for this category was Rmb 52 million per year. The new annual limits are based on the amounts in prior years and a projection of our future needs for such services.

Transaction	Annual Limit	Basis for Determining the Annual Limits
Sales of crude oil, condensate oil and liquefied petroleum gas	In respect of the three financial years ending December 31, 2005, 42%, 56% and 82%, respectively, of our audited consolidated total revenues in the preceding financial year	Our original waiver from the Hong Kong Stock Exchange limited this category of transactions to Rmb 1,950 million (representing 18% of our audited consolidated revenues for the year ended December 31, 2002). The new annual limits are based on the amount of past sales and expected increases in this category because of the ongoing development of existing oilfields and the development of two new oilfields in the Bohai Bay. The increases also reflect our anticipated need to use CNOOC's refining processes for heavy crude oil from new developments and the possibility that we may sell an increasing proportion of our oil and gas to CNOOC because of generally lower transportation costs.
General research and development services agreement	Rmb 110 million	The annual limit for this category of connected transactions is the same as the limit under the previous waiver from the Hong Kong Stock Exchange and takes into consideration our anticipated need for these services.
Lease and management services	Rmb 78 million	Under our initial waiver, the maximum amount of this category was Rmb 49 million. The new waiver amount is based on possible future expansion and the unavailability of alternative providers.

The proposed increase in the annual limits for the transactions is primarily a result of the continued expansion in our business scope and operations, including the ongoing development of existing oilfields and the development of two new oilfields in the Bohai Bay. The proposed annual limits for the transactions take into consideration the two new oilfields in the Bohai Bay; and

vi. we will undertake that if any of the terms of the agreements or arrangements referred to above are altered or if we enter into any new agreements with any connected persons (within the meaning of the Hong Kong Stock Exchange listing rules) in the future or if the limits stated in (v) above are exceeded, we will comply with the standard disclosure and shareholder approval provisions in the Hong Kong Stock Exchange listing rules unless we apply for and obtain a separate waiver from the Hong Kong Stock Exchange.

In addition to these connected transactions, from time to time we place cash deposits with CNOOC Finance Corporation Limited, or CNOOC Finance. CNOOC Finance is a wholly owned subsidiary of CNOOC and operates as a non-bank finance company under the supervision of the People's Bank of China. The interest rates offered by CNOOC Finance are regulated by the People's Bank of China. As of December 31, 2002, we had cash and cash equivalents and time deposits aggregating Rmb 2,740 million placed with CNOOC Finance. Our interest income from deposits placed with CNOOC Finance during the year 2002 was approximately Rmb 3.5 million.

For further information regarding related party transactions, see note 27 to our consolidated financial statements beginning on page F-1.

DESCRIPTION OF THE NOTES AND GUARANTEES

The notes will be issued pursuant to two indentures, each to be dated as of May 21, 2003 among us, as guarantor, the issuer and The Bank of New York, as trustee (the "Trustee"). A copy of each of the indentures will be available for inspection at the registered office of the Trustee and, for so long as the related series of notes are listed on the Luxembourg Stock Exchange, at the office of Dexia Banque Internationale à Luxembourg S.A., the issuer's current listing, paying and transfer agent in Luxembourg. The holders of a series of the notes will be bound by, and be deemed to have notice of, all the provisions of the related indenture. The following summaries of certain provisions of the notes and the indentures are subject to, and are qualified in their entirety by reference to, the detailed provisions of the notes and the indentures. Terms and expressions used in this section and not otherwise defined shall have the meanings given to such terms in the notes and the indentures.

General

The 2013 notes will be issued in an initial aggregate principal amount of US$200,000,000 and will mature on May 21, 2013, while the 2033 notes will be issued in an initial aggregate principal amount of US$300,000,000 and will mature on May 21, 2033, unless either the 2013 notes or the 2033 notes are redeemed earlier pursuant to the respective terms thereof and of the respective indenture. At maturity, the notes are payable at 100% of the principal amount thereof plus accrued interest thereon. The 2013 notes will bear interest at the rate of 4.125% per annum and the 2033 notes will bear interest at the rate of 5.500% per annum. Interest on both series of notes will accrue from May 21, 2003 or from the most recent Interest Payment Date (as defined below) to which interest has been paid or provided for payable semiannually in arrears on May 21 and November 21 in each year (each, an "Interest Payment Date"), commencing on November 21, 2003, to the persons in whose names the notes are registered at the close of business on the preceding May 6 and November 6, respectively (each an "Interest Record Date"). In any case where the date of maturity of the principal of or interest on the notes or the date fixed for redemption of the notes is not a Business Day, then payment of principal or interest shall be made on the next succeeding Business Day, with the same force and effect as if made on the date of maturity or the date fixed for redemption, as the case may be, and no interest shall accrue for the period after such date. Interest shall be calculated on the basis of a 360-day year consisting of twelve 30-day months. The notes will not be entitled to the benefit of any sinking fund. The notes shall be denominated in principal amounts of US$1,000 and in integral multiples of US$1,000 in excess thereof.

The notes will be the direct, unconditional, unsubordinated and unsecured obligations of the issuer, and rank *pari passu* with all other unsecured and unsubordinated obligations of the issuer (other than obligations preferred by applicable law) and senior in priority of payment and in all other respects to all other Indebtedness of the issuer that is designated as subordinate or junior in right of payment to the notes.

The notes are unconditionally guaranteed as to the payment of the principal and interest in respect thereof and all other amounts payable under the notes by the issuer as evidenced by the guarantee set forth in the respective indenture. Each guarantee is our direct, unconditional, unsubordinated and unsecured obligation and will rank *pari passu* with all of our other unsecured and unsubordinated obligations (other than obligations preferred by applicable law) and senior in priority of payment and in all other respects to all our other Indebtedness that is designated as subordinate or junior in right of payment to the guarantee.

The principal of, interest on, and all other amounts payable under, the notes will be payable, and the notes may be exchanged or transferred, at the office or agency of the issuer in the Borough of Manhattan, The City of New York (which initially will be the corporate trust office of the Trustee at 101 Barclay Street, 21st Floor West, New York, N.Y. 10286, U.S.A.) and at the offices of Dexia Banque Internationale à Luxembourg S.A., the issuer's current listing, paying and transfer agent in Luxembourg (currently located at 69, route d'Esch, L-2953, Luxembourg). The principal of and interest on the notes will be made by wire transfer or otherwise in immediately available funds and payable in U.S. dollars or in such other coin or currency of the United States of America as of the time of payment is legal tender for the payment of public and private debts. Payments of interest and principal with respect to interests in the global notes will be credited to the respective accounts of the holders of such interests with DTC or its participants, including Euroclear and Clearstream, Luxembourg. See "—Notes; Delivery and Form."

Application has been made to list the notes on the Luxembourg Stock Exchange. For so long as the notes are listed on the Luxembourg Stock Exchange, and the rules of the Luxembourg Stock Exchange so require, the issuer will appoint and maintain a paying agent and a transfer agent in Luxembourg who shall initially be Dexia Banque Internationale à Luxembourg S.A.

Guarantees

Under the indentures, we will irrevocably and unconditionally guarantee the due and punctual payment of the principal of and interest on, and all other amounts payable under (including any Additional Amounts payable in respect of), the notes when and as the same shall become due and payable, whether on the Stated Maturity (as defined in the respective indenture), upon acceleration, by call for redemption or otherwise. We have (i) agreed that our obligations under the guarantees will be as if we were principal obligors and not merely surety, and will be enforceable irrespective of any invalidity, irregularity or unenforceability of the notes or the indentures and (ii) waived our right to require the Trustee to pursue or exhaust its legal or equitable remedies against the issuer prior to exercising its rights under the guarantees. The guarantees will not be discharged with respect to any note except by payment in full of the principal thereof, interest thereon and all other amounts payable thereunder (including any Additional Amounts payable in respect thereof). Moreover, if at any time any amount paid under a note is rescinded or must otherwise be restored, the rights of the holder of the note under the guarantee will be reinstated with respect to such payment as though such payment had not been made. All payments under the guarantees will be made in U.S. dollars.

Further Issues

The 2013 notes will be issued in an initial aggregate principal amount of US$200,000,000, and the 2033 notes will be issued in an initial aggregate principal amount of US$300,000,000. We and the issuer may, however, from time to time, without the consent of the holders of the notes, create and issue pursuant to the indentures, additional notes of a series having the same terms and conditions under the respective indenture as the previously outstanding notes in all respects (or in all respects except for the date for and amount of the first payment of interest thereon) so that the same shall be consolidated and form a single series with the previously outstanding notes of that series.

Additional Amounts

All payments of principal and interest in respect of the notes or the guarantees will be made without withholding or deduction for, or on account of, any present or future taxes, duties, assessments or governmental charges of whatever nature ("Taxes") imposed or levied by or on behalf of the British Virgin Islands, Hong Kong, the PRC or any political subdivision, territory or possession thereof, any authority therein having power to tax, any area subject to its jurisdiction or any jurisdiction from or through which payment is made (each a "Relevant Taxing Jurisdiction") unless such Taxes are required by law to be withheld or deducted. If any deduction or withholding for any present or future Taxes of the applicable Relevant Taxing Jurisdiction shall at any time be so required, we or the issuer, as the case may be, shall pay such additional amounts ("Additional Amounts") as will result (after deduction of such taxes, duties, assessments or governmental charges and any additional taxes, duties, assessments or governmental charges payable in respect of such Additional Amounts) in receipt by each holder of any note of such amounts as would have been received by such holder with respect to such note or guarantee, as applicable, had no such withholding or deduction been required; provided, however, that no Additional Amounts shall be payable for or on account of:

(a) any such Taxes which would not have been imposed but for

(i) the existence of any present or former connection between such holder (or a beneficial holder of a note) and the applicable Relevant Taxing Jurisdiction (including, without limitation, such holder (or a beneficial holder of a note) being or having been a domiciliary, national or resident thereof, being or having been present or engaged in trade or business therein or having or having had a permanent establishment therein) other than the holding or ownership of a note, the collection of principal of and interest on, or the enforcement of, a note or guarantee or being or having been a beneficiary of a guarantee; or

(ii) the presentation of a note or guarantees (where presentation is required) for payment on a date more than 30 days after the date on which such payment became due and payable or the date on which payment thereof is duly provided for, whichever occurs later, except to the extent that such holder would have been entitled to such Additional Amounts if it had presented such note or guarantee for payment on any day within such period of 30 days; or

(b) any estate, inheritance, gift, sale, transfer, personal property or similar tax, assessment or other similar governmental charge; or

(c) any such Taxes withheld or deducted from any payment: (i) where such withholding or deduction is imposed on such payment to an individual and is required to be made pursuant to any European Union Directive on the taxation of savings implementing the conclusions of the ECOFIN Council meeting of November 26-27, 2000 or any law implementing or complying with, or introduced in order to conform to, such Directive or (ii) where such withholding or deduction could have been avoided by or on behalf of a holder by presenting the relevant note or guarantee to another paying agent in a Member State of the European Union; or

(d) any such Taxes payable otherwise than by deduction or withholding from payments under or with respect to any note or guarantee; or

(e) any such Taxes that are imposed or withheld by reason of the failure to comply by the holder or the beneficial owner of such note with a request by or on behalf of us or the issuer (sent to such holder or beneficial owner at least 30 days prior to the date compliance is required) (i) to provide information concerning the nationality, residence or identity of such holder or beneficial owner, or (ii) to make any declaration or other similar claim (to the extent such holder is entitled thereto) or satisfy any information or reporting requirements, which, in the case of (i) or (ii), is required or imposed by statute, treaty, regulation or administrative practice of the applicable Relevant Taxing Jurisdiction as a precondition to exemption from all or part of such Taxes; or

(f) any combination of items (a) through (e) above;

nor shall Additional Amounts be paid with respect to any payment of the principal of or any interest on any note or under the respective guarantee to any holder of a note who is a fiduciary or partnership or other than the sole beneficial owner of such payment to the extent that the settlor, beneficiary, partner or beneficial owner would not have been entitled to such Additional Amounts had it been the holder of such note.

Whenever there is mentioned, in any context, the payment of principal or interest in respect of any note or guarantee, such mention shall be deemed to include the payment of Additional Amounts provided for in the respective indenture to the extent that, in such context, Additional Amounts are, were or would be payable in respect thereof pursuant to the indenture.

Optional Tax Redemption

Each series of notes may be redeemed, at the option of the issuer, as a whole but not in part, upon notice as described below, at a redemption price equal to 100% of the principal amount thereof, together with accrued interest to the date fixed for redemption, if any, if, (i) as a result of any change in, or amendment to, the laws (or any regulations or rulings promulgated thereunder) of a Relevant Taxing Jurisdiction affecting taxation, or any change in official position regarding application or interpretation of such laws, regulations or rulings (including a holding by a court of competent jurisdiction), which change, amendment, application or interpretation is proposed and becomes effective on or after the date of the respective indenture, on the occasion of the next payment of principal or interest in respect of the notes, we or the issuer, as the case may be, would be obligated to pay Additional Amounts with respect to that series and (ii) such obligation cannot be avoided by us or the issuer, as the case may be, taking reasonable measures. Prior to the giving of any notice of redemption of the notes pursuant to the foregoing, the issuer shall deliver to the Trustee a notice of such redemption election, an opinion of independent legal counsel of recognized standing issued to the issuer to the effect that we or the issuer, as the case may be, have, or would, become obligated to pay such Additional Amounts as described in clause (i) as the result of such change, amendment, application or interpretation and an Officer's Certificate (as defined in the indentures) of the issuer, stating that such amendment, change, application or interpretation has occurred, describing the facts leading thereto and stating that such requirement cannot be avoided by us or the issuer, as the case may be, taking reasonable measures. The notes are not otherwise subject to redemption at our or the issuer's option.

Notice of redemption of the notes as provided above shall be given not less than 30 nor more than 60 days prior to the date fixed for redemption. Notice having been given, the notes of such series shall become due and payable on the date fixed for redemption and will be paid at the redemption price, together with accrued interest to the date fixed for redemption, at the place or places of payment and in the manner specified in the notice. From and after the date fixed for redemption, if moneys for the redemption of such notes shall have been made available as provided in the respective indenture for redemption on the date fixed for redemption, the notes shall cease to bear interest, and the only right of the holders of the notes shall be to receive payment of the redemption price and interest accrued to the date fixed for redemption.

Modification and Waiver

The indentures contain provisions permitting us, the issuer and the Trustee, without the consent of the holders of notes, to execute supplemental indentures for certain enumerated purposes, including any amendment solely to conform the indentures to this offering memorandum (as amended and supplemented) and, with the consent of the holders of not less than a majority in aggregate principal amount of the applicable series of notes then outstanding under the respective indenture, to change or modify in any manner the rights of the holders of the notes, provided that no such modification or amendment may, without the consent of the holder of each such note affected thereby, among other things:

(i) change the stated maturity of the notes;

(ii) reduce the principal amount of or payments of interest on any such note;

(iii) change any obligation of us or the issuer to pay Additional Amounts;

(iv) change the currency or place of payment of the principal of or interest on such note;

(v) impair the right to institute suit for the enforcement of any payment due on or with respect to any such note;

(vi) reduce the above stated percentage of outstanding notes necessary to modify or amend the respective indenture;

(vii) reduce the percentage of the aggregate principal amount of outstanding notes necessary for waiver of compliance with certain provisions of the indentures or for waiver of certain defaults;

(viii) change, in any manner adverse to the interest of holders of the notes, the terms and provisions of the guarantees in respect of the due and punctual payment of principal of and interest on the notes; or

(ix) modify such provisions with respect to modification and waiver.

The holders of not less than a majority in aggregate principal amount of the notes then outstanding of a series may, on behalf of holders of all the notes of that series, waive compliance by us or the issuer with certain restrictive provisions of the respective indenture. The holders of not less than a majority in aggregate principal amount of the notes of a series may on behalf of all holders of notes waive any existing or past default under the respective indenture for the notes, except a continuing default in the payment of principal of, or interest on, any note then outstanding or in respect of a covenant or provision which under such indenture cannot be modified or amended without the consent of the holder of each note then outstanding affected thereby. Any such waivers will be conclusive and binding on all holders of the notes of a series, whether or not they have given consent to such waivers, and on all future holders of such notes, whether or not notation of such waivers is made upon such notes. Any instrument given by or on behalf of any holder of a note in connection with any consent to any such waiver will be irrevocable once given and will be conclusive and binding on all subsequent holders of such note.

Limitation on Liens

The indentures provide that we will not, and will not permit the issuer or any Principal Subsidiary to, create, incur, assume or permit to exist any Lien upon any of its property or assets, now owned or hereafter acquired, to secure any Indebtedness of us or such Principal Subsidiary (or any guarantees or indemnity in respect thereof) without, in any such case, making effective provision whereby the notes and the guarantees will be secured either at least equally and ratably with such Indebtedness or by such other Lien as shall have been approved by the holders of the notes as provided in the indentures, for so long as such Indebtedness will be so secured, unless, after giving effect thereto, the aggregate outstanding principal amount of all such secured Indebtedness (including the Attributable Value of the Sale and Leaseback Transactions set forth below) entered into after the date of the indentures does not exceed 50% of our Adjusted Consolidated Net Worth.

The foregoing restriction will not apply to:

(i) any Lien which is in existence prior to the date of the indentures and any replacement thereof created in connection with the refinancing (together with interest, fees and other charges attributable thereto) of the Indebtedness originally secured (but the principal amount secured by any such Lien may not be increased);

(ii) any Lien arising or already arisen automatically by operation of law which is promptly discharged or disputed in good faith by appropriate proceedings; provided that any reserve or other appropriate provision required by Hong Kong GAAP shall have been made therefor;

(iii) any Lien over goods (or any documents relating thereto) arising either in favor of a bank issuing a form of documentary credit in connection with the purchase of such goods or by way of retention of title by the supplier of such goods where such goods are supplied on credit, subject to such retention of title, and in both cases where such goods are acquired in the ordinary course of business;

(iv) any right of set-off or combination of accounts arising in favor of any bank or financial institution as a result of the day-to-day operation of banking arrangements;

(v) any Lien either over any asset acquired after the date of the indentures which is in existence at the time of such acquisition or in respect of the obligations of any Person which becomes our Subsidiary after the date of the indentures which is in existence at the date on which it becomes our Subsidiary and in both cases any replacement thereof created in connection with the refinancing (together with interest, fees and other charges attributable thereto) of the Indebtedness originally secured (but the principal amount secured by any such Lien may not be increased); *provided* that any such Lien was not incurred in anticipation of such acquisition or of such company becoming our Subsidiary;

(vi) any Lien created on any property or asset acquired, leased or developed (including improved, constructed, altered or repaired) after the date of the indentures; *provided, however*, that (a) any such Lien shall be confined to the property or asset acquired, leased or developed (including improved, constructed, altered or repaired); (b) the principal amount of the debt encumbered by such Lien shall not exceed the cost of the acquisition or development of such property or asset or any improvement thereto (including any construction, repair or alteration) or thereon and (c) any such Lien shall be created concurrently with or within one year following the acquisition, lease or development (including construction, improvement, repair or alteration) of such property or asset;

(vii) any Lien pursuant to any order of attachment, execution, enforcement, distraint or similar legal process arising in connection with court proceedings; provided that such process is effectively stayed, discharged or otherwise set aside within 30 days;

(viii) any Lien created or outstanding in favor of us or any of our Subsidiaries;

(ix) any easement, right-of-way, zoning and similar restriction and other similar charge or encumbrance not interfering with the ordinary course of business of us and our Principal Subsidiaries;

(x) any lease, sublease, license and sublicense granted to any third party and any Lien pursuant to farm-in and farm-out agreements, operating agreements, development agreements and any other agreements, which are customary in the oil and gas industry and in the ordinary course of our business and any Principal Subsidiary;

(xi) any Lien on any property or asset to secure all or part of the cost of exploration, drilling, development, production, gathering, processing, marketing of such property or asset or to secure Indebtedness incurred to provide funds for any such purpose;

(xii) any Lien over any property or asset to secure Indebtedness incurred in connection with the construction, installation or financing of pollution control, abatement or remediation facilities;

(xiii) any Lien arising in connection with industrial revenue, development or similar bonds or other indebtedness or means of project financing (not to exceed the value of the project financed and limited to the project financed);

(xiv) any Lien in favor of any government or any subdivision thereof, securing the obligations of us or any of our Principal Subsidiaries under any contract or payment owed to such governmental entity pursuant to applicable laws, rules, regulations or statutes;

(xv) any Lien over any property or asset securing Indebtedness of us or any of our Principal Subsidiaries guaranteed by any international finance agency, including the World Bank and the International Finance Corporation, or any subdivision, department or division thereof;

(xvi) any right arising in connection with the sale or other transfer of crude oil, natural gas or other petroleum hydrocarbons in place for a period of time until, or in an amount such that, the transferee will realize therefrom a specified amount (however determined) of such crude oil, natural gas or other petroleum hydrocarbons or a specified amount of money, or the sale or other transfer of any other interest in property of the character commonly referred to as a production payment or overriding royalty;

(xvii) any Lien created in connection with any sale/leaseback transaction, subject to the limitation set forth below under "—Limitation on Sale and Leaseback Transactions;"

(xviii) any renewal or extension of any of the Liens described in the foregoing clauses which is limited to the original property or asset covered thereby; or

(xix) any Lien in respect of Indebtedness of us or any of our Subsidiaries with respect to which we or such Subsidiary have paid money or deposited money or securities with a fiscal agent, trustee or depository to pay or discharge in full the obligations of us and our Subsidiary in respect thereof (other than the obligation that such money or securities so paid or deposited, and the proceeds therefrom, be sufficient to pay or discharge such obligations in full).

Limitation on Sale and Leaseback Transactions

The indentures provide that we shall not, and shall not cause or permit any Principal Subsidiary to, enter into any Sale and Leaseback Transaction with any Person (not including any Principal Subsidiary) for a period, including renewals, in excess of three years of any Principal Property which has been owned by us or a Principal Subsidiary for more than six months unless either:

(i) we or such Principal Subsidiary would be permitted under the "—Limitation on Liens" covenant to create, incur or permit to exist a Lien on the Principal Property to secure Indebtedness (without equally and ratably securing the notes with such Indebtedness) at least equal in amount to the Attributable Value of the Sale and Leaseback Transactions; or

(ii) we or such Principal Subsidiary, within 120 days after such sale or transfer, (x) apply, in the case of a sale or transfer for cash, an amount equal to the net proceeds thereof or, in the case of a sale or transfer otherwise than for cash, an amount equal to the fair market value of the Principal Property so leased (as determined in good faith by any two members of our Board of Directors or the Board of Directors of such Principal Subsidiary) to (A) the retirement of Indebtedness of us or such Principal Subsidiary ranking prior to or on parity with the notes, incurred or assumed by us or such Principal Subsidiary, which by its terms matures at, or is extendible or renewable at the option of the obligor to, a date more than 12 months after the date of incurring or assuming such Indebtedness; provided, however, that in connection with such application, we or such Principal Subsidiary will retire such Indebtedness and will cause the related commitment (if any) to be permanently reduced in an amount equal to the principal amount of such Indebtedness so voluntarily retired by us or such Principal Subsidiary; or (B) the purchase of other property which will constitute a Principal Property having a fair market value (as determined in good faith by any two members of our Board of Directors or the Board of Directors of such Principal Subsidiary) at least equal to the fair market value of the Principal Property leased in such Sale and Leaseback Transaction; or (y) deposits, in the case of a sale or transfer for cash, an amount equal to the net proceeds thereof into an escrow account which is used solely for the purpose of providing for our or such Principal Subsidiary's obligations under the Sale and Leaseback Transaction.

"Attributable Value" means, at the time of determination, the lesser of (i) the fair market value of the Principal Property subject to the Sale and Leaseback Transaction (as determined in good faith by any two members of our Board of Directors) and (ii) the present value (discounted at a rate equal to the rate of interest on the notes, compounded semiannually) of the total amount of rent required to be paid under such lease during the remaining term thereof, including any period for which such lease has been extended. Such rental payments shall not include amounts payable by or on behalf of the lessee on account of maintenance and repairs, insurance, taxes, assessments, water rates and similar charges.

"Principal Property" means any real property owned at the date of the indentures or thereafter acquired by us or a Principal Subsidiary, the gross book value (including related land and improvements thereon and all machinery and equipment included therein) of which, on the date as of which the determination is being made, exceeds 2% of our Consolidated Total Assets.

"Sale and Leaseback Transaction" means any transaction or series of related transactions pursuant to which we or any Principal Subsidiary sell or transfer any Principal Property to any Person with the intention of taking back a lease of such Principal Property pursuant to which the rental payments are calculated to amortize the purchase price of such Principal Property substantially over the useful life thereof and such Principal Property is in fact so leased. For purposes of this definition, a Sale and Leaseback Transaction shall not include any transaction relating to farm-in and farm-out agreements, operating agreements, development agreements, and any other similar arrangements which are customary in the oil and gas industry or in the ordinary course of business of us and any Principal Subsidiary.

Consolidation, Merger and Sale of Assets

The indentures provide that neither we nor the issuer may consolidate with or merge into any other Person in a transaction in which we or the issuer, as the case may be, are not the surviving entity, or convey, transfer or lease our properties and assets substantially as an entirety to any Person unless:

(i) any Person formed by such consolidation or into which we or the issuer, as the case may be, are merged or to whom we or the issuer, as the case may be, have conveyed, transferred or leased our properties and assets substantially as an entirety is a corporation, partnership, trust or other entity validly existing under the laws of the jurisdiction of its organization and such Person expressly assumes by an indenture supplemental to the indentures all the obligations of us or the issuer under the indentures, the notes or the guarantees, as the case may be;

(ii) immediately after giving effect to the transaction, no Event of Default, and no event which, after notice or lapse of time or both, would become an Event of Default, shall have occurred and be continuing;

(iii) any such Person not organized and validly existing under the laws of (or any such Person resident for tax purposes in a jurisdiction other than) Hong Kong (in the case of us) or the British Virgin Islands (in the case of the issuer) shall expressly agree in a supplemental indenture that all payments pursuant to the notes in respect of principal of or interest on the notes or on the guarantees shall be made without withholding or deduction for or on account of, any present or future taxes, duties, assessments or governmental charges of whatever nature imposed or levied by or on behalf of the jurisdiction of organization (or residence for tax purposes) of such Person, any political subdivision, territory or possession thereof, any taxing authority therein or any area subject to its jurisdiction, unless such taxes, duties, assessments or governmental charges are required by such jurisdiction or any such subdivision, territory, possession, area or authority to be withheld or deducted, in which case such Person will pay such additional amounts of, or in respect of, principal and interest ("Successor Additional Amounts") as will result (after deduction of such taxes, duties, assessments or governmental charges and any additional taxes, duties, assessments or governmental charges payable in respect of such Successor Additional Amounts) in the payment to the holder of a note of the amounts which would have been payable pursuant to the notes had no such withholding or deduction been required, subject to the same exceptions as apply with respect to the payment by us or the issuer of Additional Amounts in respect of the notes (inserting references to the taxing jurisdiction where appropriate), and *provided* that such successor Person shall not have the right to redeem the notes pursuant to other provisions described under "—Optional Tax Redemption" in respect of such Successor Additional Amounts;

(iv) such successor Person shall have delivered to the Trustee an opinion of independent legal counsel of recognized standing licensed to practice law in the United States to the effect that the holders of the notes will not recognize income, gain or loss for U.S. federal income tax purposes as a result of such transaction and will be subject to U.S. federal income tax on the same amounts and in the same manner and at the same times as would be the case as if the transaction had not occurred; and

(v) if, as a result of the transaction, any property or asset of us or any of our Subsidiaries would become subject to a Lien that would not be permitted under "—Limitation on Liens" above, we, the issuer or such successor Person take such steps as shall be necessary to secure the notes at least equally and ratably with the Indebtedness secured by such Lien or by such other Lien as shall have been approved by holders of the notes pursuant to the indentures.

Limitation on Issuer's Activities

For so long as the notes are outstanding, the issuer will conduct no business or any other activities other than the offering, sale or issuance of Indebtedness and the lending of the proceeds thereof to us and any other activities in connection therewith. Upon any merger of the issuer into us or of us into the issuer, this covenant will no longer apply.

In addition, we will maintain 100% equity ownership of the issuer during the period that any note remains outstanding.

Events of Default

Each of the following shall constitute an Event of Default under the respective indenture for each series of notes:

(i) failure to pay principal of any note of the series within two Business Days after the due date for such payment;

(ii) failure to pay interest on any note of the series within 30 days after the due date for such payment;

(iii) failure to perform any other covenant or agreement of us or the issuer in the respective indenture, and such failure continues for 60 days after there has been given, by registered or certified mail, to us or the issuer, as the case may be, by the Trustee or by the holders of at least 25% in aggregate principal amount of the notes of the series then outstanding (with a copy to the Trustee) a written notice specifying such failure and requiring it to be remedied and stating that such notice is a "Notice of Default" under the indenture;

(iv) the guarantees shall cease to be in full force or effect or we shall deny or disaffirm our obligations under the guarantees;

(v) (a) failure to pay upon final maturity (after giving effect to the expiration of any applicable grace period therefor) the principal of any Indebtedness of us, the issuer or any Principal Subsidiary, (b) acceleration of the maturity of any Indebtedness of us, the issuer or any Principal Subsidiary following a default by us, the issuer, or such Principal Subsidiary, if such Indebtedness is not discharged, or such acceleration is not annulled, within 10 days after receipt by the Trustee of the written notice from us or the issuer as provided in the respective indenture, or (c) failure to pay any amount payable by us, the issuer or any Principal Subsidiary under any guarantee or indemnity in respect of any Indebtedness of any other Person if such obligation is not discharged or otherwise satisfied within 10 days after receipt of written notice as provided in the respective indenture; *provided, however*, that no such event set forth in clause (a), (b) or (c) shall constitute an Event of Default unless the aggregate outstanding Indebtedness to which all such events relate exceeds US$30,000,000 (or its equivalent in any other currency); and

(vi) certain events in bankruptcy, insolvency or reorganization in respect of us, the issuer or any Principal Subsidiary as provided in the respective indenture.

If an Event of Default (other than an Event of Default described in clause (vi) above) with respect to the notes shall occur and be continuing, either the Trustee or the holders of at least 25% in aggregate principal amount of the notes of a series then outstanding by notice as provided in the respective indenture may declare the principal amount of such notes and any accrued and unpaid interest thereon to be due and payable immediately. If an Event of Default in clause (vi) above with respect to the notes shall occur, the unpaid principal amount of all the notes and any accrued and unpaid interest thereon will automatically, and without any action by the Trustee or any holder of notes, become immediately due and payable. After any such acceleration but before a judgment or decree based on acceleration has been obtained, the holders of at least a majority in aggregate principal amount of the notes then outstanding may, under certain circumstances, rescind and annul such acceleration if all Events of Default, other than the nonpayment of accelerated principal, have been cured or waived as provided in the respective indenture. For information as to waiver of defaults, see "—Modification and Waiver." See also "—Notices" below.

Subject to the provisions of the indentures relating to the duties of the Trustee in case an Event of Default shall occur and be continuing, the Trustee will be under no obligation to exercise any of its rights or powers under the indentures at the request or direction of any of the holders of notes unless such holders shall have offered to the Trustee security or indemnity satisfactory to the Trustee. Subject to certain provisions, including those requiring security or indemnification of the Trustee, the holders of a majority in aggregate principal amount of the notes of a series then outstanding will have the right to direct the time, method and place of conducting any proceeding for any remedy available to the Trustee or exercising any trust or power conferred on the Trustee with respect to the notes. No holder of any notes will have any right to institute any proceeding, judicial or otherwise, with respect to the indentures, or for the appointment of a receiver or a trustee, or for any other remedy thereunder unless (i) such holder has previously given to the Trustee written notice of a continuing Event of Default with respect to the notes, (ii) the holders of at least 25% in aggregate principal amount of the notes of a series then outstanding have made written request, and such holder or holders have offered to the Trustee indemnity satisfactory to the Trustee, to institute such proceeding as trustee and (iii) the Trustee has failed to institute such proceeding, and has not received from the holders of a majority in aggregate principal amount of the notes then outstanding a direction inconsistent with such request, within 60 days after such notice, request and offer. However, such limitations do not apply to a suit instituted by a holder of a note for the enforcement of the right to receive payment of the principal of or interest on such note on or after the applicable due date specified in such note.

Neither we nor any of our Subsidiaries will, directly or indirectly, pay or cause to be paid any consideration, whether by way of interest, fee or otherwise, to any holder of any notes for or as an inducement to any consent, waiver or amendment of any of the terms or provisions of the indenture or the notes unless such consideration is offered to be paid or agreed to be paid to all holders of the notes that consent, waive or agree to amend in the time frame set forth in the solicitation documents relating to such consent, waiver or agreement.

Certain Definitions

Set forth below are definitions of certain of the terms used herein. Additional terms are defined elsewhere above or in the indentures.

"*Adjusted Consolidated Net Worth*" means the sum of our (a) shareholders' equity as determined under Hong Kong GAAP and (b) Subordinated Indebtedness.

"*Business Day*" means a day in The City of New York and the applicable place of payment other than a Saturday, Sunday or a day on which banking institutions are authorized or obligated by law or executive order to remain closed.

"*Capital Stock*" means any and all shares, interests (including joint venture interests), participations or other equivalents (however designated) of capital stock of a corporation or any and all equivalent ownership interests in a Person (other than a corporation).

"*Consolidated Total Assets*" means the consolidated total assets of us and our Subsidiaries as shown on our most recent audited consolidated balance sheet.

"*Indebtedness*" of any Person means, at any date, without duplication, (i) any outstanding indebtedness for or in respect of money borrowed (including bonds, debentures, notes or other similar instruments, whether or not listed) that is evidenced by any agreement or instrument, excluding trade payables, (ii) all noncontingent obligations of such Person to reimburse any bank or other Person in respect of amounts paid under a letter of credit or similar instrument, and (iii) all Indebtedness of others guaranteed by such Person; provided, however, that, for the purpose of determining the amount of our Indebtedness outstanding at any relevant time, the amount included as our Indebtedness in respect of finance leases shall be the net amount from time to time properly characterized as "obligations under finance leases" in accordance with the Hong Kong GAAP.

"*Lien*" means any mortgage, charge, pledge, lien, encumbrance, hypothecation, title retention, security interest or security arrangement of any kind.

"*Person*" means any individual, corporation, partnership, joint venture, association, joint stock company, trust, unincorporated organization, government or any agency or political subdivision thereof or any other entity.

"*Principal Subsidiary*" at any time shall mean one of our Subsidiaries

(i) as to which one or more of the following conditions is/are satisfied:

   (a) its net profit or (in the case of one of our Subsidiaries which has Subsidiaries) consolidated net profit attributable to us (in each case before taxation and exceptional items) is at least 5% of our consolidated net profit (before taxation and exceptional items); or

   (b) its net assets or (in the case of one of our Subsidiaries which has Subsidiaries) consolidated net assets attributable to us (in each case after deducting minority interests in Subsidiaries) are at least 5% of our consolidated net assets (after deducting minority interests in Subsidiaries);

   all as calculated by reference to the then latest audited financial statements (consolidated or, as the case may be, unconsolidated) of our Subsidiary and our then latest consolidated financial statements; or

(ii) to which is transferred all or substantially all of the assets of our Subsidiary which immediately prior to the transfer was a Principal Subsidiary, provided that, with effect from such transfer, the Subsidiary which so transfers its assets and undertakings shall cease to be a Principal Subsidiary (but without prejudice to paragraph (i) above) and our Subsidiary to which the assets are so transferred shall become a Principal Subsidiary.

A certificate of our auditors as to whether or not our Subsidiary is a Principal Subsidiary shall be conclusive and binding on all parties in the absence of manifest error.

"*Subsidiary*" means, as applied to any Person, any corporation or other entity of which a majority of the outstanding Voting Shares is, at the time, directly or indirectly, owned by such Person.

"*Subordinated Indebtedness*" means our Indebtedness (including perpetual debt, which we are not required to repay) which (i) has a final maturity and a weighted average life to maturity longer than the remaining life to maturity of the notes and (ii) is issued or assumed pursuant to, or evidenced by, an indenture or other instrument containing provisions for the subordination of such Indebtedness to the notes including (x) a provision that in the event of our bankruptcy, insolvency or other similar proceeding, the holders of the notes shall be entitled to receive payment in full in cash of all principal, Additional Amounts and interest on the notes (including all interest arising after the commencement of such proceeding whether or not an allowed claim in such proceeding) before the holder or holders of any such Subordinated Indebtedness shall be entitled to receive any payment of principal, interest or premium thereon, (y) a provision that, if an Event of Default has occurred and is continuing under the indentures for the notes, the holder or holders of any such Subordinated Indebtedness shall not be entitled to payment of any principal, interest or premium in respect thereof unless or until such Event of Default shall have been cured or waived or shall have ceased to exist, and (z) a provision that the holder or holders of such Subordinated Indebtedness may not accelerate the maturity thereof as a result of any default relating thereto so long as any note is outstanding.

"*Voting Shares*" means, with respect to any Person, the Capital Stock having the general voting power under ordinary circumstances to vote on the election of the members of the board of directors or other governing body of such Person (irrespective of whether or not at the time stock of any other class or classes shall have or might have voting power by reason of the happening of any contingency).

Defeasance and Discharge

The indentures provide that, upon the conditions set forth therein, we and the issuer may each be discharged from all our obligations with respect to notes of a series (except for certain obligations to exchange or register the transfer of notes, to replace stolen, lost or mutilated notes, to maintain paying agencies and to hold moneys for payment in trust) upon the deposit in trust for the benefit of the holders of such notes of money in U.S. dollars or U.S. Government Obligations (as defined in the indentures), or both, which, through the payment of principal and interest thereon in accordance with their terms, will provide money in an amount sufficient to pay the principal of and interest on the notes (and any Additional Amounts in respect thereof) in accordance with the terms of the indentures and the notes. Such defeasance or discharge may occur only if, among other things, we and the issuer have delivered to the Trustee an opinion of independent legal counsel of recognized standing licensed to practice law in the United States to the effect that holders of the notes will not recognize income, gain or loss for U.S. federal income tax purposes as a result of such deposit, defeasance or discharge and will be subject to U.S. federal income tax on the same amounts, in the same manner and at the same times as would have been the case if such deposit, defeasance or discharge had not occurred, which opinion of counsel must be based on a ruling received by us or the issuer from the U.S. Internal Revenue Service or a published ruling of the U.S. Internal Revenue Service or other changes in applicable U.S. federal income tax law.

Unclaimed Payments

Any moneys deposited with or paid to the Trustee or any paying agent of the notes, or then held by the issuer, in trust, for the payment of the principal of or interest on (or any Additional Amount payable in respect of) any note and not applied but remaining unclaimed for two years after the date upon which such principal or interest shall have become due and payable, shall, upon the request of us or the issuer be repaid to us or the issuer, as the case may be, by the Trustee or such paying agent or (if then held by the issuer) be discharged from such trust, unless otherwise required by mandatory provisions of applicable escheat or abandoned or unclaimed property law, and the holder of such note shall, unless otherwise required by mandatory provisions of applicable escheat or abandoned or unclaimed property laws, thereafter look only to us or the issuer for any payment which such holder may be entitled to collect, and all liability of the Trustee or any paying agent of the notes with respect to such moneys shall thereupon cease.

Concerning the Trustee

Pursuant to the indentures, the Trustee will be designated by the issuer as the initial Paying Agent, Transfer Agent and Registrar for the notes. The Corporate Trust Office of the Trustee is currently located at 101 Barclay Street, 21st Floor West, New York, N.Y. 10286, U.S.A.

The indentures provide that the Trustee, except during the continuance of an Event of Default, undertakes to perform such duties and only such duties as are specifically set forth in the indentures. If an Event of Default has occurred and is continuing, the Trustee will use the same degree of care and skill in its exercise of the rights and powers vested in it by the indentures as a prudent person would exercise under the circumstances in the conduct of such person's own affairs. The indentures also provide that the Trustee and any paying or other agent of the notes, in their individual or any other capacity, may become the owner or pledgee of notes with the same rights it would have if it were not the Trustee or such agent and may otherwise deal with us and the issuer and receive, collect, hold and retain collections from us and the issuer with the same rights it would have if it were not the Trustee or such agent; *provided, however*, that all moneys received by the Trustee shall, until used or applied as provided in the indentures, be held in trust thereunder for the purposes for which they were received and need not be segregated from other funds except to the extent required by law.

Indemnification for Judgment Currency Fluctuations

To the fullest extent permitted by law, the obligations of us or the issuer to any holder of notes under the indentures or the notes, as the case may be, shall, notwithstanding any judgment in a currency (the "Judgment Currency") other than U.S. dollars (the "Agreement Currency"), be discharged only to the extent that on the day following receipt by such holder or the Trustee, as the case may be, of any amount in the Judgment Currency, such holder or the Trustee, as the case may be, may in accordance with normal banking procedures purchase the Agreement Currency with the Judgment Currency. If the amount of the Agreement Currency so purchased is less than the amount originally to be paid to such holder or the Trustee, as the case may be, in the Agreement Currency, we and the issuer agree, as a separate obligation and notwithstanding such judgment, to pay the difference and if the amount of the Agreement Currency so purchased exceeds the amount originally to be paid to such holder, such holder or the Trustee, as the case may be, agrees to pay to or for the account of us or the issuer, as the case may be, such excess, *provided* that such holder or the Trustee, as the case may be, shall not have any obligation to pay any such excess as long as a Default by us or the issuer in its obligations under the indentures or the notes has occurred and is continuing, in which case such excess may be applied by such holder or the Trustee, as the case may be, to such obligations.

Notices

Notices to holders of notes will be mailed to them (or the first named of joint holders) by first class mail (or, if first class mail is unavailable, by airmail) at their respective addresses in the register and will be deemed to have been given on the fourth Business Day after the date of mailing.

So long as the notes are listed on the Luxembourg Stock Exchange and the rules of the Luxembourg Stock Exchange so require, all notices to holders of the notes will also be published in a daily newspaper of general circulation in Luxembourg. It is expected that such publication will be made in the *Luxemburger Wort*. If publication as aforesaid is not practicable, notice will be validly given if made in accordance with the rules of the Luxembourg Stock Exchange.

Governing Law and Consent to Jurisdiction

The notes, the guarantees and the indentures are governed by and will be construed in accordance with the laws of the State of New York. We and the issuer have each agreed that any action arising out of or based upon the indentures, the guarantees or the notes may be instituted in any U.S. federal or New

York State court located in the Borough of Manhattan, The City of New York, and we and the issuer have each irrevocably submitted to the nonexclusive jurisdiction of any such court in any such action. We and the issuer have each appointed CT Corporation System as our respective agent upon which process may be served in any such action.

We and the issuer have each agreed that, to the extent that we have or may become entitled to any sovereign or other immunity, we will waive such immunity in respect of our obligations under the indentures.

Certain Information Requirements

So long as the notes remain outstanding and are "restricted securities" within the meaning of Rule 144(a)(3) under the U.S. Securities Act, we will furnish, upon the request of any holder of a beneficial interest in a note, such information as is specified in paragraph (d)(4) of Rule 144A under the U.S. Securities Act, to such holder or beneficial owner or to a prospective purchaser of such note or interest therein who is a Qualified Institutional Buyer, or a QIB, within the meaning of Rule 144A, in order to permit compliance by such holder or beneficial owner with Rule 144A in connection with the resale of such note or beneficial interest therein in reliance on Rule 144A unless, at the time of such request, we are subject to the reporting requirements of Section 13 or 15(d) of the U.S. Exchange Act, or are included in the list of foreign private issuers that claim exemption from the registration requirements of Section 12(g) of the U.S. Securities Exchange Act (and therefore are required to furnish the U.S. Securities and Exchange Commission certain information pursuant to Rule 12g3-2(b) under the U.S. Exchange Act).

Notes; Delivery and Form

The statements set forth herein include summaries of certain rules and operating procedures of DTC, Euroclear and Clearstream, Luxembourg which will affect transfers of interests in the global notes.

The notes sold in offshore transactions in reliance on Regulation S under the U.S. Securities Act will be initially in the form of one or more Regulation S global notes, fully registered without interest coupons, which will be deposited with The Bank of New York, as custodian for DTC (in such capacity, the "Custodian") and registered in the name of Cede & Co., as nominee of DTC, for the accounts of Euroclear and Clearstream, Luxembourg, as participants in DTC.

The notes sold to QIBs in reliance on Rule 144A under the U.S. Securities Act will be issued initially in the form of one or more Rule 144A global notes, fully registered without interest coupons, which will be deposited with the Custodian for DTC and registered in the name of Cede & Co., as nominee of DTC.

The notes will be issued in denominations of US$1,000 and in integral multiples of US$1,000 above that amount.

The notes (including beneficial interests in the global notes) will be subject to certain restrictions on transfer set forth therein and in the indentures and will bear a legend regarding such restrictions as set forth under "Transfer Restrictions." Under certain circumstances, transfers may be made only upon receipt by the Trustee of a written certification (in the form(s) provided in the indentures).

Until 40 days after the later of the commencement of the offering and the closing date (as defined in the purchase agreement with respect to the notes), beneficial interests in a Regulation S global note may be held only through Euroclear or Clearstream, Luxembourg unless delivery is made through the related Rule 144A global note in accordance with the certification requirements described in this paragraph. Prior to the 40th day after the later of the commencement of the offering and the closing date, a beneficial interest in a Regulation S global note may be transferred within the United States to a person who takes delivery in the form of an interest in the related Rule 144A global note only if the transferor, and any person acting on its behalf, reasonably believes that the transferee is a QIB, and upon receipt by the Trustee of a written certification (in the form(s) provided in the indentures) (a) from the transferee to the effect that such transferee (i) is a QIB purchasing for its own account (or for the account of one or more QIBs over which account it exercises sole investment discretion) and (ii) agrees to comply with the restrictions on transfer set forth under "Transfer Restrictions," and (b) from the transferor to the effect that the transfer was made to a person whom the transferor reasonably believes is a QIB acquiring for its own account or the account of a QIB and that the transferor has informed the transferee that the transfer is being made in reliance on Rule 144A. After the 40th day after the later of commencement of the offering and the closing date (but not earlier), investors may also hold interests in a Regulation S global note through organizations other than Euroclear or Clearstream, Luxembourg that are either Participants (as hereinafter defined) or Euroclear Participants (as hereinafter defined) or Clearstream Participants (as hereinafter defined).

Beneficial interests in a Rule 144A global note may be transferred to a person who takes delivery in the form of an interest in a Rule 144A global note without any written certification from the transferor or the transferee. Beneficial interests in a Rule 144A global note may be transferred to a person who takes delivery in the form of an interest in a Regulation S global note only upon receipt by the Trustee of written certifications (in the form(s) provided in the indentures) from the transferor to the effect that such transfer is being made to a non-U.S. person as defined in Rule 904 of Regulation S or pursuant to Rule 144 under the U.S. Securities Act (if available). If such transfer occurs on or prior to the 40th day after the later of the commencement of the offering and the closing date, the interest transferred will be held immediately thereafter through Euroclear or Clearstream, Luxembourg.

Any beneficial interest in one of the global notes that is transferred to an entity who takes delivery in the form of an interest in the other global note will, upon transfer, cease to be an interest in such global note and become an interest in the other global note and, accordingly, will thereafter be subject to all transfer restrictions, if any, and other procedures applicable to beneficial interests in such other global note for as long as it remains such an interest.

Investors may hold their interests in the global notes directly through DTC, Clearstream, Luxembourg or Euroclear, as the case may be, if they are participants in such systems, or indirectly through organizations which are participants in such systems. Clearstream, Luxembourg and Euroclear will hold interests in the Regulation S global notes on behalf of their participants through customers' securities accounts in their respective names on the books of their respective depositaries, which are participants in DTC.

Transfers between participants in DTC (the "Participants") will be effected in the ordinary way in accordance with DTC rules. Transfers between participants in Clearstream, Luxembourg and Euroclear ("Clearstream Participants" and "Euroclear Participants," respectively) will be effected in the ordinary way in accordance with their respective rules and operating procedures.

Persons who are not Participants may beneficially own interests in the global notes held by DTC only through Participants or Indirect Participants (an defined below) (including Euroclear and Clearstream, Luxembourg). So long as Cede & Co., as the nominee of DTC, is the registered owner of the global notes, Cede & Co., for all purposes will be considered the sole holder of such notes.

Payment of interest on and principal of the global notes will be made to Cede & Co., the nominee for DTC, as the registered owner of the global notes by wire transfer of immediately available funds. None of us, the issuer nor the Trustee will have any responsibility or liability for any aspect of the records relating to or payments made on account of beneficial ownership interests in the global notes or for maintaining, supervising or reviewing any records relating to such beneficial ownership interest.

The issuer has been informed by DTC that, upon receipt of any payment of interest on or the redemption price of the global notes, DTC will credit Participants' accounts with payments in amounts proportionate to their respective beneficial interests in the global notes as shown on the records of DTC. Payments of interest on and principal of the notes held through Clearstream, Luxembourg or Euroclear will be credited to the cash accounts of Clearstream Participants or Euroclear Participants, as the case may be, in accordance with the relevant system's rules and procedures. Payments by Participants to owners of beneficial interests in the global notes held through such Participants will be the responsibility of such Participants, as is the case with securities held by broker-dealers, either directly or through nominees, for the accounts of customers and registered in "street name."

Because DTC can only act on behalf of Participants, who in turn act on behalf of Indirect Participants and certain banks, the ability of a person having a beneficial interest in the global notes to pledge such interest to persons or entities that do not participate in the DTC system, or to otherwise take actions in respect of such interest, may be affected by the lack of a physical certificate.

So long as the notes are represented by global notes and such global notes are held on behalf of DTC or any other clearing system, such clearing system or its nominee will be considered the sole holder of the notes represented by the applicable global notes for all purposes under the indentures, including, without limitation, obtaining consents and waivers thereunder, and none of us, the issuer or the Trustee shall be affected by any notice to the contrary. None of us, the Trustee or the issuer shall have any responsibility or obligation with respect to the accuracy of any records maintained by any clearing system or any Participant of such clearing system. The clearing systems will take actions on behalf of their Participants (and any such Participants will take actions on behalf of any Indirect Participants) in accordance with their standard procedures. To the extent that any clearing system acts upon the direction of the holders of the beneficial interests in the applicable global note and such beneficial holders give conflicting instructions, the applicable clearing system may take conflicting actions in accordance with such instructions.

DTC has advised the issuer that it will take any action permitted to be taken by a holder of notes (including, without limitation, the presentation of notes for exchange) only at the direction of one or more Participants and only in respect of the principal amount of the notes represented by the global note as to which such Participant or Participants has or have given such direction.

Clearstream, Luxembourg or Euroclear, as the case may be, will take any action permitted to be taken by a holder of notes (including, without limitation, the presentation of notes for exchange) on behalf of a Clearstream Participant or a Euroclear Participant only in accordance with its relevant rules and procedures and subject to its ability to effect such actions through DTC.

DTC has advised the issuer as follows:

DTC is a limited purpose trust company organized under the laws of the State of New York, a member of the Federal Reserve System, a "clearing corporation" within the meaning of the Uniform Commercial Code and a "Clearing Agency" registered pursuant to the provisions of Section 17A of the U.S. Securities Exchange Act. DTC was created to hold securities for its Participants and facilitate the clearance and settlement of securities transactions between Participants through electronic book-entry changes in accounts of its Participants, thereby eliminating the need for the physical movement of certificates. Participants include securities brokers and dealers, banks, trust companies and clearing corporations and may include certain other organizations. Indirect access to the DTC system is available to others such as banks, brokers, dealers and trust companies that clear through or maintain a custodial relationship with a Participant, either directly or indirectly ("Indirect Participants").

Although DTC, Clearstream, Luxembourg and Euroclear have agreed to the foregoing procedures in order to facilitate transfers of interests in the global notes among participants of DTC, Clearstream, Luxembourg and Euroclear, they are under no obligation to perform or continue to perform such procedures, and such procedures may be discontinued at any time. None of us, the issuer or the Trustee will have any responsibility for the performance by DTC, Clearstream, Luxembourg and Euroclear, or their respective Participants or Indirect Participants, of their respective obligations under the rules and procedures governing their operations.

Individual Notes

If DTC is at any time unwilling or unable to continue as depositary and a successor depositary is not appointed by the issuer within 90 days or if there shall have occurred and be continuing an Event of Default (as described above) with respect to the notes, the issuer will issue individual notes in certificated, fully registered form in exchange for the global notes.

Subject to the transfer restrictions set forth on the individual notes in certificated form, the holder of such individual notes in certificated form may transfer or exchange such notes by surrendering them at the Corporate Trust Office of the Trustee or at the office of the transfer agent in Luxembourg. Prior to any proposed transfer of individual notes in certificated form (other than pursuant to an effective registration statement), the holder may be required to provide certifications and other documentation relating to the manner of such transfer and submit such certifications and other documentation to the Trustee as described under "Notes; Delivery and Form" above. Upon the transfer, exchange or replacement of individual notes in certificated form not bearing the legend referred to under "Transfer Restrictions," the Trustee will deliver individual notes in certificated form that do not bear the legend. Upon the transfer, exchange or replacement of individual notes in certificated form bearing the legend, or upon specific request for removal of the legend on an individual note in certificated form, the Trustee will deliver only individual notes in certificated form that bear such legend or shall refuse to remove such legend, as the case may be, unless there is delivered to us or the issuer such satisfactory evidence, which may include an opinion of counsel, as may reasonably be required by us or the issuer that neither the legend nor the restrictions on transfer set forth therein are required to ensure compliance with the provisions of the U.S. Securities Act.

TAXATION

The statements herein regarding taxation are based on the laws in force as of the date of this offering memorandum and are subject to any changes in law occurring after such date, which changes could be made on a retroactive basis. The following summary does not purport to be a comprehensive description of all of the tax considerations that may be relevant to a decision of a prospective purchaser to acquire or dispose of the notes and does not purport to deal with the tax consequences applicable to all categories of investors, some of which (such as dealers in securities or commodities) may be subject to special rules. You are advised to consult your own tax advisors concerning the overall tax consequences of the purchase, ownership and disposition of the notes.

U.S. Federal Income Taxation

The following summary describes certain U.S. federal income tax consequences of the purchase, ownership and disposition of notes as of the date hereof. Except where noted, it deals only with notes held as capital assets by persons that are the initial purchasers and does not deal with special situations, such as those of dealers in securities or currencies, traders in securities that elect to mark to market, financial institutions, insurance companies, regulated investment companies, persons holding notes as part of a hedging or conversion transaction or a straddle, tax-exempt investors, or persons whose "functional currency" is not the U.S. dollar. Furthermore, the discussion below is based upon the provisions of the Internal Revenue Code of 1986, as amended (the "Code"), and regulations, rulings and judicial decisions thereunder as of the date hereof, and such authorities may be repealed, revoked or modified (possibly with retroactive effect) so as to result in U.S. federal income tax consequences different from those discussed below. **Persons considering the purchase, ownership or disposition of notes should consult their own tax advisors concerning the application of the U.S. federal income tax laws to their particular situations as well as any tax consequences arising under the laws of any state, local, foreign or other jurisdiction.**

As used under this heading, a "U.S. Holder" is a beneficial owner of a note that, for U.S. federal income tax purposes, is (i) a citizen or resident of the United States, (ii) a corporation or partnership created or organized in or under the laws of the United States or of any state thereof, or the District of Columbia, (iii) an estate the income of which is subject to U.S. federal income taxation regardless of its source, or (iv) a trust meeting certain requirements. A "Non-U.S. Holder" is a beneficial owner of a note that is not a U.S. Holder.

Based on the advice of counsel, the issuer intends to treat the notes as debt for U.S. federal income tax purposes. The notes are expected to be issued without "original issue discount." Accordingly, a U.S. Holder will generally recognize ordinary income with respect to interest payments on the notes when such interest is accrued or received, in accordance with his normal method of accounting for U.S. federal income tax purposes. Capital gain or loss will generally be recognized upon the sale, exchange or redemption of the notes. Any such gain will generally be treated as U.S. source income for U.S. foreign tax credit purposes.

Interest received on the notes will be treated as foreign source income for U.S. foreign tax credit purposes. If a U.S. Holder is required to pay foreign tax on any payments received on the notes (including any withholding taxes paid), the holder may be eligible for a credit on its U.S. federal income tax return for foreign taxes paid. Prospective investors should consult their own tax advisors about the availability and limitations of foreign tax credits.

A Non-U.S. Holder will generally not be subject to U.S. federal income or withholding taxes on payments of interest on the notes. A Non-U.S. Holder will generally not be subject to U.S. federal income or withholding tax on any gain realized on the sale or exchange of a note unless the Non-U.S. Holder is an individual present in the United States for 183 days or more in the taxable year and certain other conditions are met.

The issuer will be required to file information returns with the U.S. Internal Revenue Service (the "IRS") reporting payments made to certain U.S. Holders on the notes. In addition, certain U.S. Holders may be subject to U.S. backup withholding taxes in respect of such payments if such a holder does not provide its taxpayer identification number to the issuer or if the IRS notifies the issuer that such a holder is subject to backup withholding due to a failure to report certain interest or dividend income. Certain U.S. Holders may also be subject to information reporting and backup withholding requirements with respect to proceeds from a sale of the notes. Non-U.S. Holders may be required to comply with applicable certification procedures to establish that they are not U.S. persons in order to avoid the application of U.S. information reporting requirements and backup withholding tax.

Backup withholding is not an additional tax. Any amounts withheld under the backup withholding rules may be refunded or credited against the holder's U.S. federal income tax liability, provided that the required information is furnished to the IRS.

British Virgin Islands

The following summary contains a description of the principal tax laws of the British Virgin Islands, as in effect on the date hereof, and is subject to any change in the tax laws of the British Virgin Islands that may come into effect after such date (which may have retroactive effect).

As of the date of this offering memorandum the issuer is exempt from all provisions of the Income Tax Act of the British Virgin Islands, including with respect to all dividends, interests, rents, royalties, compensation and other amounts payable by the issuer to persons who are not persons resident in the British Virgin Islands. Capital gains realized with respect to any shares, debt obligations or other securities of the issuer by persons who are not persons resident in the British Virgin Islands are also exempt from all provisions of the Income Tax Act of the British Virgin Islands. No estate, inheritance, succession or gift tax, rate, duty, levy or other charge is payable by persons who are not persons resident in the British Virgin Islands with respect to any shares, debt obligations or other securities of the issuer.

Hong Kong

The following summary contains a description of the principal tax laws of Hong Kong, as in effect on the date hereof, and is subject to any change in the tax laws of Hong Kong that may come into effect after such date (which may have retroactive effect).

No Hong Kong tax will be required to be withheld from payments of principal or interest on the notes or payments by us in respect thereof under the guarantees.

Interest on the notes is not subject to Hong Kong profits tax, except where the notes are subscribed for by or are held by a financial institution as part of its business carried on in Hong Kong.

Hong Kong profits tax is not chargeable on profit arising on the sale or disposal of the notes, except where such transactions are or form part of a trade, profession or business carried on in Hong Kong.

Proposed European Union Savings Directive

On March 19, 2003, the European Union Council of Economic and Finance Ministers discussed the adoption of a new directive regarding the taxation of savings income. It is proposed that European Union member states will be required to provide to the tax authorities of another member state details of payments of interest or other similar income paid by a person within its jurisdiction to an individual resident in that other member state; provided, however, Austria, Belgium and Luxembourg will instead apply a withholding system for a transitional period in relation to such payments. The directive, which is proposed to come into force on January 1, 2005, is not yet final, and may be subject to further amendment and clarification.

PLAN OF DISTRIBUTION

The issuer intends to offer the notes through the initial purchasers named below (the "Initial Purchasers"). Subject to the terms and conditions contained in a purchase agreement among us, the issuer and the Initial Purchasers, the issuer has agreed to sell to the Initial Purchasers, and each of the Initial Purchasers, severally and not jointly, has agreed to purchase from the issuer, the principal amount of the notes listed opposite its name below.

Initial Purchasers	Principal Amount of 2013 notes	Principal Amount of 2033 notes
Credit Suisse First Boston (Europe) Limited	US$85,500,000	US$128,250,000
Merrill Lynch, Pierce, Fenner & Smith Incorporated	85,500,000	128,250,000
Goldman Sachs (Asia) L.L.C.	20,000,000	30,000,000
Cazenove Asia Limited.	8,000,000	12,000,000
CITIC Capital Markets Limited	100,000	150,000
China Construction Bank	100,000	150,000
BOCI Capital Limited	100,000	150,000
Industrial and Commercial Bank of China (Asia) Limited	100,000	150,000
Barclays Bank PLC	100,000	150,000
ICEA Securities Limited	100,000	150,000
Nomura International (Hong Kong) Limited	100,000	150,000
Daiwa Securities SMBC Hong Kong Limited	100,000	150,000
Société Générale Asia Limited	100,000	150,000
The Hongkong and Shanghai Banking Corporation Limited	100,000	150,000
Total	US$200,000,000	US$300,000,000

The purchase agreement provides that the obligations of the Initial Purchasers to pay for and accept delivery of the notes are subject to the approval of certain legal matters by their counsel, including the validity of the notes, and other conditions contained in the purchase agreement such as the receipt by the Initial Purchasers of officers' certificates and legal opinions. The Initial Purchasers reserve the right to withdraw, cancel or modify offers to investors and to reject orders in whole or in part.

We and the issuer have agreed to indemnify the Initial Purchasers against certain liabilities or to contribute to payments that the Initial Purchasers may be required to make in respect of those liabilities. The Initial Purchasers have agreed to pay certain expenses of the issuer in connection with the offering of the notes.

Commissions and Discounts

The Initial Purchasers have advised us and the issuer that they propose initially to offer the notes to investors at the prices listed on the cover page of this offering memorandum and to dealers at such prices less a concession not in excess of 0.30% of the principal amount of the notes for the 2013 notes and 0.50% of the principal amount of the notes for the 2033 notes. After the initial offering, the prices to investors, concessions and discounts may be changed.

The Notes Are Not Being Registered

The Initial Purchasers, either directly or through their respective selling agents, propose to offer the notes for resale in transactions not requiring registration under the U.S. Securities Act or applicable state securities laws, including sales pursuant to Rule 144A and Regulation S. The Initial Purchasers will not offer or sell the notes except:

- to persons they reasonably believe to be qualified institutional buyers in the United States, or

- pursuant to offers and sales to non-U.S. persons that occur outside the United States within the meaning of Regulation S.

Each Initial Purchaser has severally acknowledged and agreed that, except as permitted by the preceding paragraph, it will not offer or sell any notes (i) as part of their distribution at any time, and (ii) otherwise until 40 days after the later of the date upon which the offering of the notes commences and the closing date, within the United States or to, or for the account or benefit of, U.S. persons. Each Initial Purchaser has agreed that, at or prior to confirmation of a sale of notes (other than a sale of notes pursuant to Rule 144A), it will have sent to each distributor, dealer or person receiving a selling concession, fee or other remuneration that purchases notes from or through it during the restricted period, a confirmation or notice setting forth the restrictions on offers and sales of notes within the United States or to, or for the account or benefit of, U.S. persons.

In addition, until 40 days after the later of the commencement of this offering and the closing date, an offer or sale of the notes within the United States by a dealer (whether or not participating in this offering) may violate the registration requirements of the U.S. Securities Act if such offer or sale is made otherwise than in accordance with Rule 144A under the U.S. Securities Act or pursuant to another exemption from registration under the U.S. Securities Act.

Each purchaser of the notes will be deemed to have made acknowledgments, representations and agreements as described under "Transfer Restrictions."

No Sale of Similar Securities

We and the issuer have agreed in the purchase agreement that, for a period of 90 days after the date of delivery of the notes, we will not, without the prior written consent of the Initial Purchasers, offer, sell, contract to sell or otherwise dispose of any debt securities issued by us or our affiliates that are substantially similar to the notes, including any convertible debt securities or exchangeable debt securities.

UK Selling Restrictions

Each Initial Purchaser has agreed that:

- it has not offered or sold and, prior to the expiry of the period of six months from the date of issue of the notes, it will not offer or sell any notes to persons in the United Kingdom except to persons whose ordinary activities involve them in acquiring, holding, managing or disposing of investments (as principal or agent) for the purposes of their businesses or otherwise in circumstances which have not resulted and will not result in an offer to the public in the United Kingdom within the meaning of the Public Offers of Securities Regulations 1995 (as amended);

- it has complied and will comply with all applicable provisions of the Financial Services and Markets Act 2000 (the "FSMA") with respect to anything done by it in relation to the notes in, from or otherwise involving the United Kingdom; and

- it has only communicated or caused to be communicated and will only communicate or cause to be communicated any invitation or inducement to engage in investment activity (within the meaning of Section 21 of the FSMA) received by it in connection with the issue or sale of the notes in circumstances in which Section 21(1) of the FSMA does not apply to the issuer.

Hong Kong Selling Restrictions

Each Initial Purchaser has agreed that:

- it has not offered or sold and will not offer or sell in Hong Kong, by means of any document, any notes, other than to persons whose ordinary business is to buy or sell shares or debentures, whether as principal or agent, or in circumstances which do not constitute an offer to the public within the meaning of the Companies Ordinance (Cap. 32) of Hong Kong; and

- it has not issued and will not issue any advertisement, invitation or document relating to the notes, whether in Hong Kong or elsewhere, which is directed at, or the contents of which are likely to be accessed or read by, the public in Hong Kong (except if permitted to do so under the securities laws of Hong Kong) other than with respect to notes which are or are intended to be disposed of only to persons outside Hong Kong or only to "professional investors" within the meaning of the Securities and Futures Ordinance (Cap. 571) of Hong Kong and any rules made thereunder.

Singapore Selling Restrictions

Each Initial Purchaser has agreed that it has not offered or sold, and will not offer or sell, any notes nor has it made and nor will it make, any notes the subject of an invitation for subscription or purchase and it has not circulated or distributed, and it will not circulate or distribute, this offering memorandum or any other document or material in connection with the offer or sale, or invitation for subscription or purchase of such notes, whether directly or indirectly, to the public or any member of the public in Singapore other than (i) to an institutional investor or other person specified in Section 274 of the Securities and Futures Act, Chapter 289 of Singapore (the "Securities and Futures Act") (ii) to a sophisticated investor, and in accordance with the conditions, specified in Section 275 of the Securities and Futures Act or (iii) otherwise pursuant to, and in accordance with the conditions of, any other applicable provision of the Securities and Futures Act.

Japan Selling Restrictions

Each Initial Purchaser has agreed that it has not offered or sold, and will not offer or sell, directly or indirectly, any of the notes in Japan or to any resident of Japan or to any persons for reoffering or resale, directly or indirectly, in Japan or to any resident of Japan, except (x) pursuant to an exemption from the registration requirements of the Securities and Exchange Law of Japan available thereunder and (y) in compliance with the other relevant requirements of Japanese law.

The Netherlands Selling Restrictions

The notes may not be offered, sold, transferred or delivered in or from The Netherlands, as part of their initial distribution or as part of any reoffering, and neither the offering memorandum nor any other document in respect of the offering may be distributed or circulated in The Netherlands, other than to individuals or legal entities which include, but are not limited to, banks, brokers, dealers, institutional investors and undertakings with a treasury department, who or which trade or invest in securities in the conduct of a business or profession.

Italy Selling Restrictions

The offering of the notes has not been cleared by CONSOB (the Italian Securities Exchange Commission) pursuant to Italian securities legislation and, accordingly, no notes may be offered, sold or delivered, nor may copies of the offering memorandum or of any other document relating to the notes be distributed in the Republic of Italy, except:

(i) to professional investors ("operatori qualificati"), as defined in Article 31, second paragraph, of CONSOB Regulation No. 11522 of July 1, 1998, as amended; or

(ii) in circumstances which are exempted from the rules on solicitation of investments pursuant to Article 100 of Legislative Decree No. 58 of February 24, 1998 (the "Financial Services Act") and Article 33, first paragraph, of CONSOB Regulation No. 11971 of May 14, 1999, as amended.

Any offer, sale or delivery of the notes or distribution of copies of the offering memorandum or any other document relating to the notes in the Republic of Italy under (i) or (ii) above must be:

(a) made by an investment firm, bank or financial intermediary permitted to conduct such activities in the Republic of Italy in accordance with the Financial Services Act and Legislative Decree No. 385 of September 1, 1993 (the "Banking Act"), as amended;

(b) in compliance with Article 129 of the Banking Act and the implementing guidelines of the Bank of Italy pursuant to which the issue or the offer of securities in the Republic of Italy may need to be preceded and followed by an appropriate notice to be filed with the Bank of Italy depending, inter alia, on the aggregate value of the securities issued or offered in the Republic of Italy and their characteristics; and

(c) in compliance with any other applicable notification requirement or limitation which may be imposed by CONSOB or the Bank of Italy.

In any case the notes shall not be placed, sold and/or offered either in the primary or in the secondary market to retail individuals residing in Italy.

British Virgin Islands Selling Restrictions

Each Initial Purchaser has agreed that it has not made and will not make any invitation to the public in the British Virgin Islands to subscribe for any of the notes, whether directly or indirectly.

Price Stabilization and Short Positions

In connection with the offering, Merrill Lynch, Pierce, Fenner and Smith Incorporated or any of its affiliates, on behalf of the Initial Purchasers, may engage in transactions that stabilize the market price of the notes. Such transactions consist of bids or purchases to peg, fix or maintain the price of the notes. If the Initial Purchasers create a short position in the notes in connection with the offering, i.e., if they sell more notes than are listed on the cover page of this offering memorandum, the Initial Purchasers may reduce that short position by purchasing notes in the open market. Purchases of a security to stabilize the price or to reduce a short position may cause the price of the security to be higher than it might be in the absence of these purchases.

None of us, the issuer or any of the Initial Purchasers makes any representation or prediction as to the direction or magnitude of any effect that the transactions described above may have on the price of the notes. In addition, none of us, the issuer or any of the Initial Purchasers makes any representation that the Initial Purchasers will engage in these transactions or that these transactions, once commenced, will not be discontinued without notice.

Listing

An application has been made to list the notes on the Luxembourg Stock Exchange. No assurance can be given as to the liquidity of, or trading market for, the notes.

Other Relationships

The Initial Purchasers and their respective affiliates have engaged in, and may in the future engage in, investment banking and other commercial dealings in the ordinary cause of business with us.

TRANSFER RESTRICTIONS

Because of the following restrictions, purchasers are advised to consult legal counsel prior to making any offer, sale, resale, pledge or other transfer of the notes.

Each purchaser of the notes will be deemed to have represented and agreed as follows (terms used in this paragraph that are defined in Rule 144A or in Regulation S are used herein as defined therein):

1. it is not an "affiliate" (as defined in Rule 144 under the U.S. Securities Act) of us or the issuer or acting on behalf of us or the issuer and (A) (i) is a qualified institutional buyer, (ii) is aware that the sale of the notes to it is being made in reliance on Rule 144A, and (iii) is acquiring such notes for its own account or the account of a qualified institutional buyer, or (B) (i) is outside the United States and (ii) is not a U.S. person;

2. it acknowledges that the notes and the guarantees have not been and will not be registered under the U.S. Securities Act or with any securities regulatory authority of any jurisdiction and may not be offered or sold within the United States except as set forth below;

3. it understands and agrees that if in the future it decides to resell, pledge or otherwise transfer any notes or any beneficial interests in any notes other than a Regulation S global note, such notes may be resold, pledged, or transferred only by an initial investor (i) to us or the issuer or any subsidiary thereof, (ii) to a person whom the seller reasonably believes is a qualified institutional buyer that purchases for its own account or for the account of a qualified institutional buyer in a transaction meeting the requirements of Rule 144A, (iii) in an offshore transaction meeting the requirements of Rule 904 of Regulation S under the U.S. Securities Act, (iv) pursuant to an exemption from registration under the U.S. Securities Act provided by Rule 144 under the U.S. Securities Act or (v) pursuant to an effective registration statement under the U.S. Securities Act, and in each of such cases, in accordance with any applicable securities laws of any state of the United States and any other jurisdiction;

4. it agrees to, and each subsequent holder is required to, notify any purchaser of the notes from it of the resale restrictions referred to in clause 3 above, if then applicable;

5. it understands and agrees that (A) notes initially offered in the United States to qualified institutional buyers will be represented by Rule 144A global notes, and (B) notes offered outside the United States in reliance on Regulation S will be represented by Regulation S global notes;

6. it understands that the notes will bear a legend to the following effect unless otherwise agreed to by us and the issuer:

   THIS NOTE HAS NOT BEEN REGISTERED UNDER THE U.S. SECURITIES ACT OF 1933, AS AMENDED (THE "SECURITIES ACT"), AND, ACCORDINGLY, MAY NOT BE OFFERED OR SOLD WITHIN THE UNITED STATES OR TO, OR FOR THE ACCOUNT OR BENEFIT OF, U.S. PERSONS EXCEPT AS SET FORTH IN THE FOLLOWING SENTENCE. BY ITS ACQUISITION HEREOF, THE HOLDER (1) REPRESENTS THAT IT IS A "QUALIFIED INSTITUTIONAL BUYER" (AS DEFINED IN RULE 144A UNDER THE SECURITIES ACT) OR IT IS NOT A U.S. PERSON AND IS ACQUIRING THIS NOTE IN AN OFFSHORE TRANSACTION IN COMPLIANCE WITH REGULATION S UNDER THE SECURITIES ACT, (2) AGREES THAT IT WILL NOT, WITHIN THE TIME PERIOD REFERRED TO IN RULE 144(K) UNDER THE SECURITIES ACT AS IN EFFECT WITH RESPECT TO SUCH TRANSFER, RESELL OR OTHERWISE TRANSFER THIS NOTE EXCEPT (A) TO THE ISSUER, THE COMPANY OR ANY SUBSIDIARY THEREOF, (B) INSIDE THE UNITED STATES TO A QUALIFIED INSTITUTIONAL BUYER IN COMPLIANCE WITH RULE 144A UNDER THE SECURITIES ACT, (C) OUTSIDE THE UNITED STATES IN AN OFFSHORE TRANSACTION IN COMPLIANCE

WITH RULE 904 UNDER THE SECURITIES ACT, (D) PURSUANT TO THE EXEMPTION FROM REGISTRATION PROVIDED BY RULE 144 UNDER THE SECURITIES ACT (IF AVAILABLE) OR (E) PURSUANT TO AN EFFECTIVE REGISTRATION STATEMENT UNDER THE SECURITIES ACT, AND (3) AGREES THAT IT WILL DELIVER TO EACH PERSON TO WHOM THIS NOTE IS TRANSFERRED A NOTICE SUBSTANTIALLY TO THE EFFECT OF THIS LEGEND. AS USED HEREIN, THE TERMS "OFFSHORE TRANSACTION," "UNITED STATES" AND "U.S. PERSON" HAVE THE MEANINGS GIVEN TO THEM BY REGULATION S UNDER THE SECURITIES ACT. THE INDENTURE CONTAINS A PROVISION REQUIRING THE TRUSTEE TO REFUSE TO REGISTER ANY TRANSFER OF THIS NOTE IN VIOLATION OF THE FOREGOING RESTRICTIONS.

7. it acknowledges that we, the issuer and the Initial Purchasers and others will rely upon the truth and accuracy of the foregoing acknowledgments, representation and agreements and agrees that, if any of such acknowledgments, representations or warranties deemed to have been made by virtue of its purchase of notes are no longer accurate, it shall promptly notify us and the issuer, and if it is acquiring any notes as a fiduciary or agent for one or more accounts, it represents that it has sole investment discretion with respect to each such account and that it has full power to make the foregoing acknowledgments, representations and agreements on behalf of each such account.

For further discussion of the requirements (including the presentation of transfer certificates) under the indentures to effect exchanges of transfer of interests in global notes and of notes in certificated form, see "Description of the Notes and Guarantees—Notes; Delivery and Form."

RATINGS

The notes have been rated Baa1 with positive outlook by Moody's Investors Service and "BBB" by Standard & Poor's Ratings Services. The credit ratings accorded the notes are not a recommendation to purchase, hold or sell the notes inasmuch as such ratings do not comment as to market price or suitability for a particular investor. There can be no assurance that the ratings will remain in effect for any given period or that the ratings will not be revised by the rating agencies in the future if, in their judgment, circumstances so warrant.

LEGAL MATTERS

Certain legal matters with respect to the notes will be passed upon for us and the issuer by Sidley Austin Brown & Wood, Hong Kong and New York, as to Hong Kong and New York law and Conyers Dill & Pearman as to British Virgin Islands law, and for the initial purchasers by Skadden, Arps, Slate, Meagher & Flom LLP, New York, New York as to certain matters of New York law. Certain legal matters under PRC law will be passed upon for us and the issuer by Commerce & Finance Law Office, Beijing, China.

INDEPENDENT PUBLIC ACCOUNTANTS

The financial statements as of December 31, 2000 and 2001 and for each of the years in the two-year period ended December 31, 2001, included in this offering memorandum, have been audited by Arthur Andersen & Co, independent public accountants. See "Risk Factors—Risks relating to our business—You may not be able to assert claims against Arthur Andersen, our independent public accountants for periods prior to December 31, 2001, nor may you be able to assert claims against our current independent public accountants for financial statements previously audited by Arthur Andersen" and "Management's Discussion and Analysis of Financial Condition and Results of Operations—Change of Accountants." The financial statements as of and for the year ended December 31, 2002 included in this offering memorandum have been audited by Ernst & Young, independent public accountants, as stated in their reports appearing herein.

EXPERTS

The summary report of Ryder Scott Company, L.P., independent petroleum engineering consultants, a copy of which appears as Appendix A, has been included in this offering memorandum in reliance on the authority of such firm as experts in estimating proved oil and gas reserves. Ryder Scott Company has given and not withdrawn its written consent to the issue of this offering memorandum with the inclusion in it of its reports in the form and context in which they are included.

GENERAL INFORMATION

1. The offering of the notes and the guarantees were authorized and approved by the sole director of the issuer on May 9, 2003 and our board of directors on March 27, 2003. All consents, approvals, authorization or other orders required under the prevailing laws of the British Virgin Islands and Hong Kong have been given or obtained for the offer, issue and sale of the notes and the guarantees.

2. Application has been made to list the notes on the Luxembourg Stock Exchange. The legal notice relating to the issue of the notes and the guarantees, the memorandum and articles of association of the issuer and the memorandum and articles of association of our company will be registered prior to the listing with the Registrar of the District Court in Luxembourg *(Greffier en Chef du Tribunal d'Arrondissement de et à Luxembourg)*, where such documents are available for inspection and where copies thereof can be obtained upon request. As long as the notes are listed on the Luxembourg Stock Exchange, we and the issuer will maintain a paying agent and a transfer agent in Luxembourg.

3. For so long as the notes are listed on the Luxembourg Stock Exchange, copies of the memorandum and articles of association of the issuer, the memorandum and articles of association of our company, the approval of the board of directors of the issuer and of our company and the indentures will be available for inspection at the office of the paying and transfer agent in Luxembourg.

4. As a company incorporated in Hong Kong and with our shares listed on the Hong Kong Stock Exchange, we are required to send to each of our shareholders and other holders of our listed securities a copy of our annual report containing, among other items, our audited consolidated financial statements and our audited unconsolidated balance sheet not less than 21 days before the date of our annual general meeting and in any event not more than four months after the date upon which the financial period ended. We are also required to send to each of our shareholders and other holders of our listed securities a copy of our interim report, which should be reviewed by our auditors or audit committee, containing our unaudited consolidated balance sheet, income statement, cash flow statement and a statement of movements in equity for the first six months of each financial year, each with comparative figures for the corresponding prior period, not later than three months after the end of that six-month period. We do not publish audited interim consolidated or unconsolidated financial statements. For so long as any of the notes are outstanding, copies of the English version of our annual and interim reports containing these financial statements may be obtained at the specified offices of the paying agents, including the paying agent in Luxembourg. If the issuer publishes financial statements in the future, such statements will be made available in Luxembourg.

5. For so long as the notes are listed on the Luxembourg Stock Exchange, the issuer will publish all notices to holders of notes in a newspaper of general circulation in Luxembourg, currently expected to be the *Luxembourg Wort* in Luxembourg.

6. According to Chapter VI, Article 3, point A/II/2 of the Rules and Regulations of the Luxembourg Stock Exchange, the notes shall be freely transferable and therefore no transaction made on the Luxembourg Stock Exchange shall be cancelled.

7. Since December 31, 2002, the date of our latest audited consolidated financial statements included herein and except as disclosed herein, there has been no material adverse change in our financial position or prospects. Since the incorporation of the issuer on April 2, 2003, there has been no material adverse change in the financial position of the issuer.

8. None of us, the issuer or any of our subsidiaries is involved in any litigation or arbitration proceedings relating to claims or amounts which are material in the context of the offering of the notes and the guarantees and, so far as we or the issuer are aware, no such litigation or arbitration proceedings are pending or threatened.

9. The purchase agreement dated May 14, 2003, which is governed by the laws of the State of New York, the indentures to be dated on or about May 21, 2003, each of the notes to be dated on or about May 21, 2003, and the guarantees to be dated on or about May 21, 2003, which will all be governed by the laws of the State of New York, will be made available for inspection in Luxembourg.

10. The notes have been accepted for clearance through Euroclear and Clearstream, Luxembourg. The following table sets forth the Common Codes, the ISIN numbers and the CUSIP (CINS) numbers for the notes.

	2013 Regulation S global notes	**2033 Regulation S global notes**	**2013 Rule 144A global notes**	**2033 Rule 144A global notes**
Common Code	16904953	16905046	16904899	16904996
ISIN	USG21886AA70	USG21886AB53	US12615TAA60	US12615TAB44
CUSIP	G21886 AA 7	G21886 AB 5	12615T AA 6	12615T AB 4

CERTAIN OIL AND GAS TERMS

Unless the context indicates otherwise, references to:

- "adjusted finding and development cost per BOE" means, for a given period, the sum of (a) total finding costs incurred divided by the sum of discoveries, extensions, and revisions of prior estimates of net proved reserves and (b) the sum of (i) total development costs and (ii) the amount of expected future development costs of proved undeveloped reserves divided by the sum of (iii) proved undeveloped reserves and (iv) the sum of undeveloped reserves converted to developed reserves. This measure is used to account for expected future development costs for existing reserves in addition to finding and development costs already incurred.

- "API gravity" means the American Petroleum Institute's scale for specific gravity for liquid hydrocarbons, measured in degrees. The lower the API gravity, the heavier the liquid and, generally, the lower its commercial value. For example, asphalt has an API gravity of eight degrees, West Texas Intermediate, a benchmark crude oil, has an API of 40 degrees, and gasoline has an API gravity of 50 degrees.

- "appraisal well" means an exploration well drilled after a successful wildcat well to gain more information on a newly discovered oil or gas reserve.

- "condensate" means light hydrocarbon liquids separated from natural gas in the field through condensation when natural gas is exposed to surface temperature and pressure. This group generally includes slightly heavier hydrocarbons than natural gas liquids, such as pentane. It is combined with crude oil production and reserve figures.

- "crude oil" means crude oil and liquids, including condensate, natural gas liquids and liquefied petroleum gas.

- "development cost" means, for a given period, costs incurred to obtain access to proved reserves and to provide facilities for extracting, treating, gathering and storing the oil and gas.

- "dry hole" means an exploration well that is not commercial (i.e., economically feasible to develop). Dry hole costs include the full costs for such drilling and are charged as an expense.

- "exploration well" means a wildcat or appraisal well.

- "finding and development cost per BOE" means, for a given period, the sum of total finding and development cost incurred, divided by the sum of discoveries, extensions, and revisions of prior estimates of net proved reserves.

- "finding cost" means, for a given period, costs incurred in identifying areas that may warrant examination and in examining specific areas that are considered to have prospects of containing oil and gas reserves, including costs of drilling exploration wells.

- "lifting cost" means, for a given period, costs incurred to operate and maintain wells and related equipment and facilities, including applicable operating costs of support equipment and facilities and other costs of operating and maintaining those wells and related equipment and facilities, plus production taxes. Also known as production cost.

- "natural gas liquids" means light hydrocarbons that can be extracted in liquid form from natural gas through special separation plants. This group includes typically lighter liquid hydrocarbons than condensate, such as butane, propane and ethane. It is combined with crude oil production but not with crude oil reserve figures.

- “net wells” means a party’s working interest in wells under a production sharing contract.
- “offshore” means areas under water with a depth of five meters or greater.
- “onshore” means areas of land and areas under water with a depth of less than five meters.
- “proved developed reserves” means proved reserves of oil and natural gas that can be expected to be recovered through existing wells with existing equipment and operating methods.
- “proved reserves” means estimated quantities of crude oil and natural gas that geological and engineering data demonstrate with reasonable certainty to be recoverable in future years from known reservoirs under existing economic and operating conditions, i.e., prices and costs as of the date the estimate is made.
- “proved undeveloped reserves” means proved reserves that are expected to be recovered from new wells in undrilled areas, or from existing wells where significant expenditure is required for completion.
- “reserve replacement ratio” means, for a given year, gross additions to proved reserves divided by production during the year.
- “reserve-to-production ratio” means the ratio of proved reserves to annual production of crude oil or, with respect to natural gas, to wellhead production excluding flared gas.
- “seismic data” means data recorded in either two-dimensional (2D) or three-dimensional (3D) form from sound wave reflections off of subsurface geology. This is used to understand and map geological structures for exploratory purposes to predict the location of undiscovered reserves.
- “success” means a discovery of oil or gas by an exploration well. Such an exploration well is a successful well and is also known as a discovery. A successful well is not necessarily commercial, which means there are enough hydrocarbon deposits discovered for economical recovery.
- “success rate” means the total number of successful wells divided by the total number of wells drilled in a given period. Success rate can be applied to wildcat wells or exploration wells in general.
- “wildcat well” means an exploration well drilled in an area or rock formation that has no known reserves or previous discoveries.

For a further definition of reserves, see “Appendix A—Summary Report of Ryder Scott Company, L.P.”

References to:

- bbls means barrels, which is equivalent to approximately 0.134 tons of oil (33 degrees API);
- mmbbls means million barrels;
- BOE means barrels-of-oil equivalent;
- BOE per day means barrels-of-oil equivalent per day;
- million BOE means million barrels-of-oil equivalent;
- mcf means thousand cubic feet;

- mmcf means million cubic feet;
- bcf means billion cubic feet, which is equivalent to approximately 283.2 million cubic meters;
- BTU means British Thermal Unit, a universal measurement of energy; and
- km means kilometers, which is equivalent to approximately 0.62 miles.

INDEX TO FINANCIAL STATEMENTS

REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

To the Shareholders of CNOOC Limited
(Incorporated in Hong Kong with limited liability)

We have audited the accompanying consolidated balance sheet of CNOOC Limited (the "Company") and its subsidiaries (the "Group") as of December 31, 2002, and the related consolidated statement of income, changes in equity and cash flows for the year then ended. These financial statements are the responsibility of the management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits. The financial statements of CNOOC Limited and its subsidiaries for the years ended December 31, 2000 and 2001 were audited by other auditors who have ceased operations and whose report dated March 27, 2002 expressed an unqualified opinion on those statements.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and auditing standards established by the Hong Kong Society of Accountants. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the 2002 consolidated financial statements referred to above present fairly, in all material respects, the financial position of CNOOC Limited and its subsidiaries as of December 31, 2002, and the results of their operations and their cash flows for the year then ended in conformity with accounting principles generally accepted in Hong Kong ("Hong Kong GAAP").

Hong Kong GAAP does not conform to generally accepted accounting principles in the United States of America. A description of the significant differences between those two generally accepted accounting principles and the effect of those differences on net income and shareholders' equity is set forth in Note 38 to the consolidated financial statements.

Ernst & Young
Certified Public Accountants

Hong Kong
March 27, 2003

The following report is a copy of the report previously issued by Arthur Andersen & Co in connection with CNOOC Limited's Form 20-F Annual Report for fiscal year 2001, as filed with the United States Securities and Exchange Commission, and has not been reissued by Arthur Andersen & Co for this offering.

REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

To the Shareholders of CNOOC Limited:

We have audited the accompanying consolidated balance sheets of CNOOC Limited (established in the Hong Kong Special Administrative Region, the People's Republic of China) and its subsidiaries as of December 31, 2001 and 2000, and the related consolidated statements of income, recognized gains and losses and cash flows for the years ended December 31, 2001, 2000 and 1999. These financial statements are the responsibility of the management of CNOOC Limited. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards in the United States of America and auditing standards established by the Hong Kong Society of Accountants. Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the accompanying consolidated financial statements referred to above present fairly, in all material respects, the financial positions of CNOOC Limited and its subsidiaries as of December 31, 2001 and 2000, and the results of their operations and cash flows for the years ended December 31, 2001, 2000 and 1999 in conformity with accounting principles generally accepted in Hong Kong ("Hong Kong GAAP").

Hong Kong GAAP does not conform to generally accepted accounting principles in the United States of America. A description of the significant differences between those two generally accepted accounting principles and the effect of those differences on net income and shareholders' equity is set forth in Note 36 to the consolidated financial statements.

ARTHUR ANDERSEN & CO
Certified Public Accountants

Hong Kong
March 27, 2002

CNOOC LIMITED AND ITS SUBSIDIARIES
CONSOLIDATED INCOME STATEMENTS
FOR THE YEARS ENDED DECEMBER 31, 2002, 2001, AND 2000

(All amounts expressed in thousands, except per share data)

	Notes	2000	2001	2002	2002
		RMB'000	RMB'000	RMB'000	US$'000
REVENUE					
Oil and gas sales	8, 27	18,819,323	17,560,788	23,779,294	2,871,895
Marketing revenues	9	5,126,015	2,537,032	2,377,469	287,134
Other income		278,580	721,737	217,052	26,214
		24,223,918	20,819,557	26,373,815	3,185,243
EXPENSES					
Operating expenses		(2,124,078)	(2,329,130)	(3,775,334)	(455,958)
Production taxes		(1,036,729)	(883,768)	(1,023,049)	(123,557)
Exploration expenses		(552,869)	(1,039,297)	(1,318,323)	(159,218)
Depreciation, depletion and amortisation		(2,577,882)	(2,566,920)	(4,019,532)	(485,451)
Dismantlement	28	(103,569)	(90,367)	(126,139)	(15,234)
Impairment losses related to property, plant and equipment	17	—	(99,675)	—	—
Crude oil and product purchases	9	(5,097,765)	(2,453,312)	(2,326,338)	(280,959)
Selling and administrative expenses	10	(456,002)	(615,389)	(1,006,540)	(121,563)
Other		(217,599)	(517,876)	(30,866)	(3,728)
		(12,166,493)	(10,595,734)	(13,626,121)	(1,645,668)
PROFIT FROM OPERATING ACTIVITIES		12,057,425	10,223,823	12,747,694	1,539,575
Interest income		236,624	317,706	147,870	17,859
Interest expenses	11	(475,004)	(116,634)	(294,792)	(35,603)
Exchange (loss)/gain, net		381,336	235,409	(113,814)	(13,746)
Investment income		—	220,650	193,277	23,343
Share of profit of an associate		218,326	89,963	165,387	19,974
Non-operating (loss)/income, net		(196,031)	34,941	(71,379)	(8,621)
PROFIT BEFORE TAX		12,222,676	11,005,858	12,774,243	1,542,781
Tax	14	(1,926,076)	(3,048,227)	(3,541,416)	(427,707)
NET PROFIT		10,296,600	7,957,631	9,232,827	1,115,074

The accompanying notes are an integral part of these financial statements.

CNOOC LIMITED AND ITS SUBSIDIARIES
CONSOLIDATED INCOME STATEMENTS (CONT'D)
FOR THE YEARS ENDED DECEMBER 31, 2002, 2001, AND 2000

(All amounts expressed in thousands, except per share data)

	Notes	2000	2001	2002	2002
		RMB'000	RMB'000	RMB'000	US$'000
DIVIDENDS					
Final	15	6,426,424	—	1,306,740	157,819
Interim	15	—	871,194	958,314	115,738
		6,426,424	871,194	2,265,054	273,557
EARNINGS PER SHARE					
Basic	16	RMB1.63	RMB1.00	RMB1.12	US$ 0.14
Diluted	16	RMB1.63	RMB1.00	RMB1.12	US$ 0.14
DIVIDEND PER SHARE					
Final	15	RMB0.98	N/A	RMB0.16	US$ 0.02
Interim	15	N/A	RMB0.11	RMB0.12	US$ 0.01
EARNINGS PER ADS					
Basic	16	RMB32.53	RMB20.04	RMB22.48	US$ 2.71
Diluted	16	RMB32.53	RMB20.04	RMB22.47	US$ 2.71

The accompanying notes are an integral part of these financial statements.

CNOOC LIMITED AND ITS SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
AS OF DECEMBER 31, 2002 AND 2001

(All amounts expressed in thousands)

	Notes	2001	2002	2002
		RMB'000	RMB'000	US$'000
NON-CURRENT ASSETS				
Property, plant and equipment, net	17	23,827,499	36,071,820	4,356,500
Investment in an associate	18	461,990	537,377	64,901
		24,289,489	36,609,197	4,421,401
CURRENT ASSETS				
Accounts receivable, net	19	1,194,180	3,063,266	369,960
Inventories and supplies	20	627,337	848,605	102,489
Due from related companies	27	176,519	453,290	54,745
Other current assets		692,595	1,060,955	128,135
Short-term investments	21	8,895,804	6,531,278	788,801
Time deposits with maturities over three months	27	2,050,000	4,690,000	566,425
Cash and cash equivalents	27	6,393,724	7,839,114	946,753
		20,030,159	24,486,508	2,957,308
TOTAL ASSETS		44,319,648	61,095,705	7,378,709
CURRENT LIABILITIES				
Accounts payable	22	591,624	2,659,743	321,225
Other payables and accrued liabilities	23	813,146	1,712,408	206,813
Current portion of long-term bank loans	24	1,231,840	297,518	35,932
Due to the parent company	26, 27	125,493	270,438	32,662
Due to related companies	27	157,823	231,592	27,970
Tax payable		1,471,750	1,962,765	237,049
		4,391,676	7,134,464	861,651
NON-CURRENT LIABILITIES				
Long-term bank loans	24	3,255,699	941,093	113,659
6.375% long-term guaranteed notes	25	—	4,071,184	491,689
Provision for dismantlement	28	1,598,130	2,239,320	270,449
Deferred tax liabilities	14	1,763,637	6,141,156	741,685
		6,617,466	13,392,753	1,617,482
CAPITAL AND RESERVES				
Issued capital	29	876,978	876,978	105,915
Reserves	30	32,433,528	39,691,510	4,793,661
		33,310,506	40,568,488	4,899,576
TOTAL EQUITY AND LIABILITIES		44,319,648	61,095,705	7,378,709

The accompanying notes are an integral part of these financial statements.

CNOOC LIMITED AND ITS SUBSIDIARIES
STATEMENTS OF CHANGES IN EQUITY
FOR THE YEARS ENDED DECEMBER 31, 2002, 2001, AND 2000

(All amounts expressed in thousands of Renminbi)

	Share capital	Share premium	Revaluation reserve	Cumulative translation reserve	Statutory reserve	Retained earnings	Total
Balances at January 1, 2000	642,000	7,124,955	170,598	—	100,874	345,813	8,384,240
Net profit for the year	—	—	—	—	—	10,296,600	10,296,600
Appropriation to statutory reserve	—	—	—	—	847,464	(847,464)	—
Dividends (Note 15)	—	—	—	—	—	(6,426,424)	(6,426,424)
Net proceeds from Private Placements	59,181	3,710,483	—	—	—	—	3,769,664
Surplus on revaluation of properties	—	—	104,073	—	—	—	104,073
Foreign currency translation differences	—	—	—	(6,350)	—	—	(6,350)
Net gain not recognised in the income statement	—	—	—	(6,350)	—	—	(6,350)
Balances at January 1, 2001	701,181	10,835,438	274,671	(6,350)	948,338	3,368,525	16,121,803
Issuance of ordinary shares	175,797	9,925,767	—	—	—	—	10,101,564
Net profit for the year	—	—	—	—	—	7,957,631	7,957,631
Appropriation to statutory reserve	—	—	—	—	587,022	(587,022)	—
Dividends (Note 15)	—	—	—	—	—	(871,194)	(871,194)
Foreign currency translation differences	—	—	—	702	—	—	702
Net gain not recognised in the income statement	—	—	—	702	—	—	702
Balances at January 1, 2002 as previously stated	876,978	20,761,205	274,671	(5,648)	1,535,360	9,867,940	33,310,506
Cumulative effect of change in accounting policy (Note 3)	—	—	—	—	—	298,157	298,157
Balances at January 1, 2002 as restated	876,978	20,761,205	274,671	(5,648)	1,535,360	10,166,097	33,608,663
Net profit for the year	—	—	—	—	—	9,232,827	9,232,827
Appropriation to statutory reserve	—	—	—	—	697,050	(697,050)	—
Dividends (Note 15)	—	—	—	—	—	(2,265,054)	(2,265,054)
Foreign currency translation differences	—	—	—	(7,948)	—	—	(7,948)
Net loss not recognised in the income statement	—	—	—	(7,948)	—	—	(7,948)
Balances at December 31, 2002	876,978	20,761,205	274,671	(13,596)	2,232,410	16,436,820	40,568,488

The accompanying notes are an integral part of these financial statements.

CNOOC LIMITED AND ITS SUBSIDIARIES
CONSOLIDATED CASH FLOW STATEMENTS
FOR THE YEARS ENDED DECEMBER 31, 2002, 2001, AND 2000

(All amounts expressed in thousands)

	Notes	2000	2001	2002	2002
		RMB'000	RMB'000	RMB'000	US$'000
OPERATING ACTIVITIES					
Cash generated from operations	32(a)	14,429,703	14,024,982	17,261,970	2,084,779
Income taxes paid		(880,080)	(2,611,450)	(3,013,279)	(363,923)
Income tax refund		—	—	167,065	20,177
Interest received		163,461	317,706	147,870	17,859
Dividends received		21,000	99,000	90,000	10,870
Short-term investment income received		—	53,641	79,679	9,623
Interest paid		(501,383)	(124,422)	(136,222)	(16,452)
Net cash from operating activities		13,232,701	11,759,457	14,597,083	1,762,933
INVESTING ACTIVITIES					
Additions of property, plant and equipment		(4,403,968)	(4,342,622)	(6,832,746)	(825,211)
Proceeds from disposals of property, plant and equipment		27,148	6,313	446	54
Acquisition of subsidiaries	32(b)	—	—	(4,734,174)	(571,760)
(Increase)/decrease in time deposits with maturities over three months		(3,424,512)	1,374,512	(2,640,000)	(318,841)
Additions of short-term investments		(300,000)	(8,699,312)	(3,399,413)	(410,557)
Disposals of short-term investments		—	308,506	5,882,305	710,423
Increase in amounts due from related companies		240,726	(13,831)	—	—
Net cash used in investing activities		(7,860,606)	(11,366,434)	(11,723,582)	(1,415,892)
FINANCING ACTIVITIES					
Issue of 6.375% long-term guaranteed notes		—	—	4,059,345	490,259
Net proceeds from Private Placement		3,769,664	—	—	—
Repayment of bank loans		(3,371,657)	(3,497,533)	(3,367,347)	(406,684)
Dividends paid		(4,074,466)	(4,268,517)	(2,265,054)	(273,557)
Increase/(decrease) in amount due to the parent company		47,256	(1,657,004)	144,945	17,505
Proceeds from issue of share capital		—	10,101,564	—	—
Proceeds from new bank loans		339,423	2,500,000	—	—
Increase in amounts due to related companies		(164,570)	25,564	—	—
Net cash (used in)/from financing activities		(3,454,350)	3,204,074	(1,428,111)	(172,477)
NET INCREASE IN CASH AND CASH EQUIVALENTS		1,917,745	3,597,097	1,445,390	174,564
Cash and cash equivalents at beginning of year		878,882	2,796,627	6,393,724	772,189
CASH AND CASH EQUIVALENTS AT END OF YEAR		2,796,627	6,393,724	7,839,114	946,753
ANALYSIS OF BALANCES OF CASH AND CASH EQUIVALENTS					
Cash and bank balances		2,796,627	6,393,724	7,839,114	946,753

The accompanying notes are an integral part of these financial statements.

(All amounts expressed in Renminbi unless otherwise stated)

1. CORPORATE INFORMATION

CNOOC Limited (the "Company") was incorporated in the Hong Kong Special Administrative Region ("Hong Kong"), the People's Republic of China (the "PRC") on August 20, 1999 to hold the interests in certain entities whereby creating a group comprising the Company and its subsidiaries. During the year, the Company and its subsidiaries (hereinafter collectively referred to as the "Group") were principally engaged in the exploration, development, production and sales of crude oil, natural gas and other petroleum.

In the opinion of directors, the ultimate holding company is China National Offshore Oil Corporation ("CNOOC"), a company established in the PRC.

As of December 31, 2002, we had direct or indirect interests in the following principal subsidiaries. All of these entities are private limited companies and were owned by the parent company upon their incorporation/establishment except for CNOOC International Limited and CNOOC Finance (2002) Limited which were owned by the Company upon its incorporation and nine subsidiaries which were newly acquired from Repsol-YPF, S.A. during the year.

Particulars of the principal subsidiaries are as follows:

Name	Place and date of incorporation/ registration and operations	Nominal value of issued ordinary share capital	Percentage of equity attributable to the Company	Principal activities
Directly held subsidiaries:				
CNOOC China Limited	Tianjin, the PRC September 15, 1999	RMB10 billion	100%	Offshore petroleum exploration, development, production and sales in the PRC
CNOOC International Limited	British Virgin Islands August 23, 1999	US$2	100%	Investment holding
China Offshore Oil (Singapore) International Pte., Ltd.	Singapore May 14, 1993	S$3 million	100%	Sales and marketing of petroleum outside of the PRC
CNOOC Finance (2002) Limited	British Virgin Islands January 24, 2002	US$1,000	100%	Bond issuance
Indirectly held subsidiaries*:				
Malacca Petroleum Limited	Bermuda November 2, 1995	US$12,000	100%	Investment holding
OOGC America, Inc.	State of Delaware, United States of America September 2, 1997	US$1,000	100%	Investment holding
OOGC Malacca Limited	Bermuda November 2, 1995	US$12,000	100%	Investment holding

(All amounts expressed in Renminbi unless otherwise stated)

1. CORPORATE INFORMATION (CONT'D)

Name	Place and date of incorporation/ registration and operations	Nominal value of issued ordinary share capital	Percentage of equity attributable to the Company	Principal activities
CNOOC Southeast Asia Limited	Bermuda May 16, 1997	US$12,000	100%	Investment holding
CNOOC ONWJ Ltd.	Labuan, F.T., Malaysia March 27, 2002	US$1	100%	Offshore petroleum exploration, development and production in Indonesia
CNOOC SES Ltd.	Labuan, F.T., Malaysia March 27, 2002	US$1	100%	Offshore petroleum exploration, development and production in Indonesia
CNOOC Poleng Ltd.	Labuan, F.T., Malaysia March 27, 2002	US$1	100%	Offshore petroleum exploration, development and production in Indonesia
CNOOC Madura Ltd.	Labuan, F.T., Malaysia March 27, 2002	US$1	100%	Offshore petroleum exploration, development and production in Indonesia
CNOOC Blora Ltd.	Labuan, F.T., Malaysia March 27, 2002	US$1	100%	Offshore petroleum exploration, development and production in Indonesia

* Indirectly held through CNOOC International Limited.

During the year, the Group acquired nine subsidiaries of Repsol-YPF, S.A. Subsequent to the acquisition, a restructuring was performed whereby all the assets and liabilities acquired from the subsidiaries of Repsol-YPF, S.A. were transferred to the newly established companies in Labuan, F.T., Malaysia. Further details of this acquisition are included in note 5 to the financial statements.

The above table lists the subsidiaries of the Company which, in the opinion of the directors, principally affected the results for the year or formed a substantial portion of the net assets of the Group. To give details of other subsidiaries would, in the opinion of the directors, result in particulars of excessive length.

(All amounts expressed in Renminbi unless otherwise stated)

2. IMPACT OF NEW AND REVISED STATEMENTS OF STANDARD ACCOUNTING PRACTICE (“SSAPS”)

The following recently-issued and revised SSAPs and related Interpretations are effective for the first time for the current year’s financial statements:

SSAP 1 (Revised)	:	“Presentation of financial statements”
SSAP 11 (Revised)	:	“Foreign currency translation”
SSAP 15 (Revised)	:	“Cash flow statements”
SSAP 34	:	“Employee benefits”
Interpretation 14	:	“Evaluating the substance of transactions involving the legal form of a lease”
Interpretation 15	:	“Business combinations — “Date of exchange” and fair value of equity instruments”
Interpretation 18	:	“Consolidation and equity method — Potential voting rights and allocation of ownership interests”

These SSAPs prescribe new accounting measurement and disclosure practices. The major effects on the Group’s accounting policies and on the amounts disclosed in these financial statements of adopting these SSAPs and Interpretations are summarised as follows:

SSAP 1 (Revised) prescribes the basis for the presentation of financial statements and sets out guidelines for their structure and minimum requirements for the content thereof. The principal impact of the revision to this SSAP is that a consolidated statement of changes in equity is now presented on page F-7 of the financial statements in place of the consolidated statement of recognised gains and losses that was previously required and in place of the Group reserves note.

SSAP 11 (Revised) prescribes the basis for the translation of foreign currency transactions and financial statements. The principal impact of the revision of this SSAP on the consolidated financial statements is that the income statement of overseas subsidiaries are now translated to Renminbi at the exchange rates at the dates of the transactions, or at an approximation thereto, whereas previously they were translated at the exchange rates at the balance sheet date. The adoption of the revised SSAP 11 has had no material effect on the financial statements.

SSAP 15 (Revised) prescribes the revised format for the cash flow statement. The principal impact of the revision of this SSAP is that the consolidated cash flow statement now presents cash flows under three headings, cash flows from operating, investing and financing activities, rather than the five headings previously required. In addition, cash flows from overseas subsidiaries arising during the year are now translated to Renminbi at the exchange rates at the dates of the transactions, or at an approximation thereto, whereas previously they were translated at the exchange rates at the balance sheet date.

SSAP 34 prescribes the principles to be applied for recognition, measurement and disclosures for employee short-term and long-term benefits. In addition, disclosures are now required in respect of the Company’s share option scheme, as detailed in Note 29 to the financial statements. These share option scheme disclosures are similar to the Listing Rules disclosures previously included in the Report of the Directors, which are now required to be included in the notes to the financial statements as a consequence of the SSAP. The SSAP requirements have not had a material effect on the amounts previously recorded in the financial statements, therefore no prior year adjustment has been required.

3. CHANGE IN ACCOUNTING POLICY

During the year, the Group changed its method of accounting for the provision for dismantlement to comply with SSAP 28 "Provisions, contingent liabilities and contingent assets." SSAP 28 requires a provision to be recorded for a present obligation whether that obligation is legal or constructive. The associated cost is capitalised and the liability is discounted and an accretion expense is recognised using the credit-adjusted risk-free interest rate in effect when the liability is initially recognised.

The effect of this change in accounting policy was to increase retained earnings and property, plant and equipment, as of January 1, 2002 by RMB 298,156,268 and RMB 736,848,177 respectively, and to increase the provision for dismantlement and deferred tax liabilities as of January 1, 2002 by RMB 310,910,651 and RMB 127,781,258 respectively. No adjustment was made to the prior year amounts as the impact on the financial statements for the year ended December 31, 2001 was not material.

4. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Basis of preparation

These financial statements have been prepared in accordance with Hong Kong Statements of Standard Accounting Practice, accounting principles generally accepted in Hong Kong ("Hong Kong GAAP") and the requirements of the Hong Kong Companies Ordinance. They have been prepared under the historical cost convention as modified by the revaluation of land and buildings and short-term investments. The significant differences between Hong Kong GAAP and generally accepted accounting principles in the United States of America ("US GAAP") are set forth in Note 38 to the financial statements.

Basis of consolidation

The consolidated financial statements include the financial statements of the Company and its subsidiaries for the year ended December 31, 2002. The results of subsidiaries acquired or disposed of during the year are consolidated from or to their effective dates of acquisition or disposal, respectively. All significant intercompany transactions and balances within the Group are eliminated on consolidation.

Impairment of assets

An assessment is made whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable, or when there is any indication that an impairment loss previously recognised for an asset in prior years may no longer exist or may have decreased. If any such indication exists, the asset's recoverable amount is estimated. An asset's recoverable amount is calculated as the higher of the asset's value in use or its net selling price.

An impairment loss is recognised only if the carrying amount of an asset exceeds its recoverable amount. An impairment loss is charged to the income statement in the period in which it arises, unless the asset is carried at a revalued amount, when the impairment loss is accounted for in accordance with the relevant accounting policy for that revalued asset.

A previously recognised impairment loss is reversed only if there has been a change in the estimates used to determine the recoverable amount of an asset, however not to an amount higher than the carrying amount that would have been determined (net of any depreciation/amortisation), had no impairment loss been recognised for the asset in prior years.

(All amounts expressed in Renminbi unless otherwise stated)

4. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONT'D)

Impairment of assets (cont'd)

A reversal of an impairment loss is credited to the income statement in the period in which it arises, unless the asset is carried at a revalued amount, when the reversal of the impairment loss is accounted for in accordance with the relevant accounting policy for that revalued asset.

Property, plant and equipment

Property, plant and equipment comprise oil and gas properties, land and buildings, and vehicles and office equipment.

(i) Oil and gas properties

For oil and gas properties, the successful efforts method of accounting is adopted. The Group capitalises initial acquisition costs of oil and gas properties. Impairment of initial acquisition costs is recognised based on exploratory experience and management judgement. Upon discovery of commercial reserves, acquisition costs are transferred to proved properties. The costs of drilling and equipping successful exploratory wells, all development costs, including those renewals and betterments which extend the economic life of the assets, and the borrowing costs arising from borrowings used to finance the development of oil and gas properties before they are substantially ready for production are capitalised. The costs of unsuccessful exploratory wells and all other exploration costs are treated as expenses when incurred.

Exploratory wells are evaluated for economic viability within one year of completion. Exploratory wells that discover potentially economic reserves in areas where major capital expenditures will be required before production would begin and when the major capital expenditure depends upon successful completion of further exploratory work remain capitalised and are reviewed periodically for impairment.

Productive oil and gas properties and other tangible and intangible costs of producing properties are amortised using the unit-of-production method on a property-by-property basis under which the ratio of produced oil and gas to the estimated remaining proved developed reserves is used to determine the depreciation, depletion and amortisation provision. Costs associated with significant development projects are not depleted until commercial production commences and the reserves related to those costs are excluded from the calculation of depletion.

Capitalised acquisition costs of proved properties are amortised by the unit-of-production method on a property-by-property basis computed based on the total estimated units of proved reserves.

The Group estimates future dismantlement costs for oil and gas properties with reference to the estimates provided from either internal or external engineers after taking into consideration the anticipated method of dismantlement required in accordance with current legislation and industry practices. The associated cost is capitalised and the liability is discounted and an accretion expense is recognised using the credit-adjusted risk-free interest rate in effect when the liability is initially recognised.

(All amounts expressed in Renminbi unless otherwise stated)

4. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONT'D)

Property, plant and equipment (cont'd)

(ii) Land and buildings

Land and buildings represent the onshore buildings and the land use rights which are stated at valuation less accumulated depreciation and accumulated impairment losses. Professional valuations are performed periodically with the last valuation performed on December 31, 2000. In the intervening years, the directors review the carrying value of land and buildings and adjustment is made where in the directors' opinion there has been a material change in value. Any increase in land and building valuation is credited to the revaluation reserves; any decrease is first offset against an increase in earlier valuation in respect of the same property and is thereafter charged to the income statement. Depreciation is calculated on the straight-line basis at annual rate estimated to write off valuation of each asset over its expected useful life, ranging from 30 to 50 years.

(iii) Vehicles and office equipment

Vehicles and office equipment are stated at cost less accumulated depreciation and impairment losses. The straight-line method is adopted to depreciate the cost less any estimated residual value of these assets over their expected useful life. The Group estimates the useful lives of vehicles and office equipment to be 5 years.

The useful lives of assets and method of depreciation, depletion and amortisation are reviewed periodically.

The gain or loss on disposal or retirement of property, plant and equipment recognised in the income statement is the difference between the net sales proceeds and the carrying amount of the relevant asset. Any revaluation reserve relating to the fixed asset is transferred to retained earnings as a reserve movement.

Subsidiaries

A subsidiary is a company in which the Company, directly or indirectly, controls more than half of its voting power or issued share capital or controls the composition of its board of directors.

The Company's interests in subsidiaries are stated at cost less any impairment losses.

Associates

An associate is a company, not being a subsidiary or a jointly-controlled entity, in which the Group has a long-term interest of generally not less than 20% of the equity voting rights and over which it is in a position to exercise significant influence.

The Group's share of the post-acquisition results and reserves of the associate is included in the consolidated income statement and consolidated reserves, respectively. The Group's proportionate interests in the associate are stated in the consolidated balance sheet at the Group's share of net assets under the equity method of accounting, less any impairment losses.

Trade and other receivables

Trade and other receivables are stated at their cost, after provision for doubtful accounts.

4. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONT'D)

Inventories and supplies

Inventories consist primarily of oil and supplies consist mainly of items for repair and maintenance of oil and gas properties. Inventories are stated at the lower of cost and net realisable value. Costs of inventories and supplies represent purchase or production cost of goods and are determined on a weighted average basis. Net realisable value is based on estimated selling prices less any estimated costs to be incurred to completion and disposal. Supplies are capitalised to property, plant and equipment when used for renewals and betterments of oil and gas properties and have resulted in an increase in the future economic values of oil and gas properties or are recognised as expenses when used.

Related parties

Parties are considered to be related if one party has the ability, directly or indirectly, to control the other party or exercise significant influence over the other party in making financial and operating decisions. Parties are also considered to be related if they are subject to common control or common significant influence. Related parties may be individuals or corporate entities.

Short-term investments

Short-term investments are investments in debt and equity securities not intended to be held on a continuing basis and are stated at their fair values at the balance sheet date, on an individual investment basis. The gains or losses arising from changes in the fair value of a security are credited or charged to the income statement in the period in which they arise.

Cash and cash equivalents

For the purpose of the consolidated cash flow statement, cash and cash equivalents comprise cash on hand and demand deposits, and short-term highly liquid investments which are readily convertible into known amounts of cash and which are subject to an insignificant risk of changes in value, and have a short maturity of generally within three months when acquired, less bank overdrafts which are payable on demand and form an integral part of the Group's cash management. For the purpose of the balance sheet, cash and cash equivalents comprise cash on hand and at banks, and term deposits with maturities of three months or less, and assets similar in nature to cash which are not restricted to use.

Provisions

A provision is recognised when a present obligation (legal or constructive) has arisen as a result of a past event and it is probable that a future outflow of resources will be required to settle the obligation, provided that a reliable estimate can be made of the amount of the obligation.

When the effect of discounting is material, the amount recognised for a provision is the present value at the balance sheet date of the future expenditures expected to be required to settle the obligation. The increase in the discounted present value amount arising from the passage of time is included in finance costs in the income statement.

Provisions for dismantlement are made based on the present value of the future costs expected to be incurred, on a site by site basis, in respect of the Group's expected dismantlement costs at the end of the related oil exploration and recovery activities.

(All amounts expressed in Renminbi unless otherwise stated)

4. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONT'D)

Deferred tax

Deferred tax is provided, using the liability method, on all significant timing differences to the extent it is probable that the liability will crystallise in the foreseeable future. A deferred tax asset is not recognised until its realisation is assured beyond reasonable doubt.

Revenue recognition

Revenue is recognised when it is probable that the economic benefits will flow to the Group and when the revenue can be measured reliably, on the following bases:

(i) Oil and gas sales

Revenues represent the invoiced value of sales of oil and gas attributable to the interests of the Group, net of royalties and government share of allocable share oil that are lifted and sold on behalf of the PRC government. Sales are recognised when the significant risks and rewards of ownership of oil and gas have been transferred to customers.

Oil and gas lifted and sold by the Group above or below the Group's participating interests in the production sharing contracts result in overlifts and underlifts. The Group records these transactions in accordance with the entitlement method under which overlifts are recorded as liabilities and underlifts are recorded as assets at year end oil prices. Settlement will be in kind when the liftings are equalised or in cash when production ceases.

The Group entered into a gas sales contract with a customer which contains take-or-pay clauses. The clauses require the customer to take a specified minimum volume of gas each year. If the minimum volume of gas is not taken, the customer must pay for the deficiency gas, even though the gas is not taken. The customer can offset the deficiency payment against any future purchases in excess of the specified volume. The Group records any deficiency payments as deferred revenue which is included in other payables until any make-up gas is taken by the customer or the expiry of the contract.

(ii) Marketing revenues

Marketing revenues represent sales of oil purchased from the foreign partners under the production sharing contracts and revenues from the trading of oil through the Company's subsidiary in Singapore. The title, together with the risks and rewards of the ownership of such oil purchased from the foreign partners, are transferred to the Group from the foreign partners and other unrelated oil and gas companies before the Group sells such oil to its customers. The cost of the oil sold is included in crude oil and product purchases.

(iii) Other income

Other income mainly represents project management fees charged to the foreign partners and handling fees charged to customers and is recognised when the services are rendered.

(iv) Interest income

Interest income from deposits placed with banks and other financial institutions is recognised on a time proportion basis taking into account the effective yield on the assets.

(All amounts expressed in Renminbi unless otherwise stated)

4. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONT'D)

Revenue recognition (cont'd)

(v) Dividend income

Dividend income is recognised when the right to receive payment has been established.

Borrowing costs

Borrowing costs directly attributable to the acquisition, construction or production of qualifying assets, i.e. assets that necessarily take a substantial period of time to get ready for their intended use or sale, are capitalised as part of the cost of those assets. The capitalisation of such borrowing costs ceases when the assets are substantially ready for their intended use or sale.

To the extent that funds are borrowed specifically for the purpose of obtaining a qualifying asset, the amount of borrowing costs eligible for capitalisation on that asset is determined as the actual borrowing costs incurred on that borrowing during the period less any investment income on the temporary investment of those borrowings.

To the extent that funds are borrowed generally and used for the purpose of obtaining a qualifying asset, the amount of borrowing costs eligible for capitalisation is determined by applying a capitalisation rate to the expenditures on that asset. The capitalisation rate is the weighted average of the borrowing costs applicable to the borrowings of the enterprise that are outstanding during the period, other than borrowings made specifically for the purpose of obtaining a qualifying asset. The amount of borrowing costs capitalised incurred during a period should not exceed the amount of borrowing cost incurred during that period.

Borrowing costs include interest charges and other costs incurred in connection with the borrowing of funds, including amortisation of discounts or premiums relating to borrowings, and amortisation of ancillary costs incurred in connection with arranging borrowings.

Research and development costs

Research costs are charged to the income statement as incurred.

Development expenditure (other than relating to oil and gas properties discussed above) incurred on projects is capitalised and deferred only when the projects are clearly defined; the expenditure is separately identifiable and can be measured reliably, and there is reasonable certainty that the projects are technically feasible and have commercial value. Development expenditure which does not meet these criteria is expensed when incurred. No development costs were capitalised during the year.

Foreign currencies

The books and records of the Company and its subsidiary in China are maintained in Renminbi ("RMB"). Foreign currency transactions are recorded at the applicable rates of exchange ruling at the transaction dates. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are translated at the applicable rates of exchange ruling at that date. Exchange differences are dealt with in the income statement.

(All amounts expressed in Renminbi unless otherwise stated)

4. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONT'D)

Foreign currencies (cont'd)

On consolidation, the financial statements of overseas subsidiaries and an associate are translated into RMB using the net investment method, whereby assets and liabilities are translated at the rates of exchange prevailing at the balance sheet date and income and expenses are translated at the weighted average rates of exchange during the year. Share capital, share premium account and retained earnings are translated at historical rates. The resulting translation differences are included in the cumulative translation reserve.

For the convenience of the readers, translation of amounts from RMB into United States dollars ("US$") has been made at the rate of US$1.00=RMB 8.28 on December 31, 2002. No representation is made that RMB amounts could have been, or could be, converted into US$ at the rate on December 31, 2002, or at any other rate.

Retirement and termination benefits

The Group provides defined contribution plans based on local laws and regulations for full-time employees in the PRC and other countries in which it operates. The plans provide for contributions ranging from 5% to 22.5% of employees' basic salaries. The Group's contributions to defined contribution plans are charged to expense in the year to which they relate.

Share options scheme

The Company operates share option schemes for the purpose of providing incentives and rewards to eligible participants who contribute to the success of the Group's operations. The financial impact of share options granted under the share option schemes is not recorded in the Company's or the Group's balance sheet until such time as the options are exercised, and no charge is recorded in the income statement or balance sheet for their cost. Upon the exercise of share options, the resulting shares issued are recorded by the Company as additional share capital at the nominal value of the shares, and the excess of the exercise price per share over the nominal value of the shares is recorded by the Company in the share premium account. Options which are cancelled prior to their exercise date, or which lapse, are deleted from the register of outstanding options.

Repairs, maintenance and overhaul costs

Repairs, maintenance and overhaul costs are normally charged to the income statement as operating expenses in the period in which they are incurred.

Financial instruments

The Group has currency swap contracts with financial institutions which are not designated as hedging instruments and are carried at fair value, with any changes in fair value thereof included in the income statement.

(All amounts expressed in Renminbi unless otherwise stated)

4. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONT'D)

Dividends

Final dividends proposed by the directors are classified as a separate allocation of retained earnings within capital and reserves in the balance sheet, until they have been approved by the shareholders in a general meeting. When these dividends have been approved by the shareholders and declared, they are recognised as a liability.

Interim dividends are simultaneously proposed and declared, because the Company's memorandum and articles of association grant the directors the authority to declare interim dividends. Consequently, interim dividends are recognised immediately as a liability when they are proposed and declared.

Operating leases

Leases of assets under which substantially all the risks and rewards of ownership are retained by the lessor are classified as operating leases. Lease payments under an operating lease are recognised as an expense on a straight-line basis over the lease terms.

Contingencies

Contingent liabilities are not recognised in the financial statements. They are disclosed unless the possibility of an outflow of resources embodying economic benefits is remote.

A contingent asset is not recognised in the financial statements, but are disclosed when an inflow of economic benefits is probable.

Subsequent events

Post-year-end events that provide additional information about the Company's position at the balance sheet date or those that indicate the going concern assumption is not appropriate (adjusting events) are reflected in the financial statements. Post-year-end events that are not adjusting events are disclosed in the notes when material.

Use of estimates

The preparation of financial statements in conformity with Hong Kong GAAP requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

(All amounts expressed in Renminbi unless otherwise stated)

5. ACQUISITION

During the year, the Company acquired nine subsidiaries of Repsol-YPF, S.A. which holds a portfolio of operated and non-operated interests in oil and gas production sharing and technical assistance contracts in contract areas located offshore and onshore of Indonesia. The assets acquired included a 65.3% interest in the Offshore Southeast Sumatra Contract Area production sharing contract, a 36.7% interest in the Offshore Northwest Java Contract Area production sharing contract, a 25.0% interest in the West Madura Offshore Block production sharing contract, a 50.0% interest in the Poleng Field technical assistance contract and a 16.7% interest in the Blora Block production sharing contract. The aggregate cash consideration for the acquisition was a total cash consideration of US$585 million which was adjusted for a working capital adjustment. The effective date of the purchase agreement was January 1, 2002 and the profit of the acquired companies would accrue to the Group from that date. The acquisition was completed on April 19, 2002. For practical reasons, the operations of the acquired companies are included in the Company's consolidated financial statements from April 1, 2002. The profit that had accrued to the Group prior to April 1, 2002 has been treated as a purchase price reduction.

Subsequent to the acquisition, the Company established five companies in Labuan, Malaysia and transferred the assets and liabilities of these nine subsidiaries of Repsol-YPF, S.A. to the five companies established in Labuan.

The transfer of the assets and liabilities were completed by December 30, 2002. The Company was in the process of winding up the acquired companies as of December 31, 2002.

The following unaudited pro forma consolidated financial information reflects the results of the operation of the Company for the years ended December 31, 2002 and 2001, as if the acquisition described above had completed on January 1, 2001.

	Pro forma financial results	
	2001	**2002**
Total revenue	24,953,612	27,306,093
Income before tax	12,171,582	13,092,812
Profit after tax	8,563,807	9,397,483
Earnings per share — Basic	RMB1.04	RMB1.14
— Diluted	RMB1.04	RMB1.14

6. PRODUCTION SHARING CONTRACTS

PRC

For production sharing contracts in the PRC, the foreign party to the contracts ("foreign partners") are normally required to bear all exploration costs during the exploration period and such exploration costs can be recovered according to the production sharing formula after commercial discoveries are made and production begins.

After the initial exploration stage, the development and operating costs are funded by the Group and the foreign partners according to their respective participating interest.

The Group has the option to take a participating interest as mutually agreed by both participants in a production sharing contract and may exercise such option after the foreign partners have independently undertaken all the exploration risks and costs and made viable commercial discoveries.

After the Group exercises its option to take a participating interest in a production sharing contract, the Group accounts for the oil and gas properties using the "proportional method" under which the Group recognises its share of development costs, revenues and expenses from such operations based on its participating interest in the production sharing contract. The Group does not account for either the exploration costs incurred by its foreign partners or the foreign partners share of development costs and revenues and expenses from such operations.

Part of the annual gross production of oil and gas in the PRC is distributed to the PRC government as settlement of royalties which are payable pursuant to a sliding scale. The Group and the foreign partners also pay a production tax to the tax bureau at a pre-determined rate. In addition, there is a pre-agreed portion of oil and gas designated to recover all exploration costs, development costs, operating costs incurred and related interests according to the participating interests between the Group and the foreign partners. Any remaining oil after the foregoing priority allocations is first distributed to the PRC government as share oil on a pre-determined ratio pursuant to a sliding scale, and then distributed to the Group and the foreign partners based on their respective participating interests. As the government share is not included in the Group's interest in the annual production, the net sales of the Group do not include the sales revenue of the government share oil.

The foreign partners have the right either to take possession of their allocable remainder oil for sale in the international market, or to negotiate with the Group to sell their allocable remainder oil to the Group for resale in the PRC market.

(All amounts expressed in Renminbi unless otherwise stated)

6. PRODUCTION SHARING CONTRACTS (CONT'D)

Overseas

The Group and the other partners to the production sharing contracts in Indonesia are required to bear all exploration, development and operating costs according to their respective participating interests. Exploration, development and operating costs which qualify for recovery can be recovered according to the production sharing formula after commercial discoveries are made and production begins.

The Group's net interest in the production sharing contracts in Indonesia consists of its participating interest in the properties covered under the relevant production sharing contracts, less oil and gas distributed to the Indonesian government and the domestic market obligation.

7. SEGMENT INFORMATION

The Group is organised on a worldwide basis into three major operating segments. Segment information is presented by way of two segment formats: (i) on a primary reporting basis, by business segment; and (ii) on a secondary segment reporting basis, by geographical segment.

Intersegment transactions: segment revenue, segment expenses and segment performance include transfers between business segments and between geographical segments. Such transfers are accounted for at cost. Those transfers are eliminated on consolidation.

(a) Business segments

The Group is involved in the upstream operating activities of the petroleum industry that comprise production sharing contracts with foreign partners, independent operations and trading business. These segments are determined primarily because the senior management makes key operating decisions and assesses performance of the segments separately. The Group evaluates performance based on profit or loss from operations before income taxes.

(All amounts expressed in Renminbi unless otherwise stated)

7. SEGMENT INFORMATION (CONT'D)

(a) Business segments (cont'd)

The following tables present revenue, profit and certain asset, liability and expenditure information for the Group's business segments.

	Independent operations			Production sharing contracts			Trading business			Unallocated			Eliminations			Consolidated		
	2000	2001	2002	2000	2001	2002	2000	2001	2002	2000	2001	2002	2000	2001	2002	2000	2001	2002
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
Segment revenue																		
Sales to external customers:																		
Oil and gas sales	9,283,228	9,845,019	10,318,549	8,859,606	7,023,926	13,460,745	—	—	—	—	—	—	—	—	—	18,142,834	16,868,945	23,779,294
Marketing revenues	—	—	—	—	—	—	5,802,504	3,228,875	2,377,469	—	—	—	—	—	—	5,802,504	3,228,875	2,377,469
Intersegment revenues	—	—	—	676,489	691,843	1,023,547	—	—	—	—	—	—	(676,489)	(691,843)	(1,023,547)	—	—	—
Other income	161,790	558,368	43,513	107,390	123,312	133,108	—	—	—	9,400	40,057	40,431	—	—	—	278,580	721,737	217,052
Total	9,445,018	10,403,387	10,362,062	9,643,485	7,839,081	14,617,400	5,802,504	3,228,875	2,377,469	9,400	40,057	40,431				24,223,918	20,819,557	26,373,815
Segment results																		
Operating expenses	(894,813)	(1,183,252)	(1,268,360)	(1,229,265)	(1,145,878)	(2,506,974)	—	—	—	—	—	—	—	—	—	(2,124,078)	(2,329,130)	(3,775,334)
Production taxes	(526,491)	(525,454)	(556,583)	(510,238)	(355,544)	(466,466)	—	—	—	—	(2,770)	—	—	—	—	(1,036,729)	(883,768)	(1,023,049)
Exploration costs	(523,633)	(955,475)	(1,241,759)	(29,236)	(83,822)	(76,564)	—	—	—	—	—	—	—	—	—	(552,869)	(1,039,297)	(1,318,323)
Depreciation, depletion and amortisation	(1,443,045)	(1,531,184)	(1,635,131)	(1,130,820)	(1,035,736)	(2,384,401)	—	—	—	(4,017)	—	—	—	—	—	(2,577,882)	(2,566,920)	(4,019,532)
Dismantlement	(49,145)	(41,530)	(72,751)	(54,424)	(48,837)	(53,388)	—	—	—	—	—	—	—	—	—	(103,569)	(90,367)	(126,139)
Impairment losses related to property, plant and equipment	—	(60,907)	—	—	(38,768)	—	—	—	—	—	—	—	—	—	—	—	(99,675)	—
Crude oil and product purchases	—	—	—	—	—	(1,023,547)	(5,774,254)	(3,145,155)	(2,326,338)	—	—	—	676,489	691,843	1,023,547	(5,097,765)	(2,453,312)	(2,326,338)
Selling and administrative expenses	(33,146)	(35,686)	(38,548)	(99)	(100)	(553,537)	—	—	—	(422,757)	(579,603)	(414,455)	—	—	—	(456,002)	(615,389)	(1,006,540)
Other	(133,976)	(514,655)	—	—	—	(30,866)	—	—	—	(83,623)	(3,221)	—	—	—	—	(217,599)	(517,876)	(30,866)
Interest income	—	—	—	—	—	3,831	—	—	—	236,624	317,706	144,039	—	—	—	236,624	317,706	147,870
Interest expense	(262,274)	(69,437)	(62,081)	(171,230)	(13,871)	(17,100)	—	—	—	(41,500)	(33,326)	(215,611)	—	—	—	(475,004)	(116,634)	(294,792)
Exchange (loss)/gain, net	—	—	—	—	—	794	—	—	—	381,336	235,409	(114,608)	—	—	—	381,336	235,409	(113,814)
Investment income	—	—	—	—	—	—	—	—	—	—	220,650	193,277	—	—	—	—	220,650	193,277
Share of profit of an associate	—	—	—	—	—	—	—	—	—	218,326	89,963	165,387	—	—	—	218,326	89,963	165,387
Non-operating (loss)/gain, net	(221,442)	18,267	(85,414)	—	—	(220)	—	—	—	25,411	16,674	14,255	—	—	—	(196,031)	34,941	(71,379)
Tax	—	—	—	—	—	—	—	—	—	(1,926,076)	(3,048,227)	(3,541,416)	—	—	—	(1,926,076)	(3,048,227)	(3,541,416)
Net profit	5,357,053	5,504,074	5,401,435	6,518,173	5,116,525	7,508,962	28,250	83,720	51,131	(1,606,876)	(2,746,688)	(3,728,701)				10,296,600	7,957,631	9,232,827
Other information																		
Segment assets	15,592,100	15,422,016	16,899,455	9,829,861	10,295,857	22,446,447	—	368,670	630,704	6,704,417	17,771,115	20,581,722	—	—	—	32,126,378	43,857,658	60,558,328
Investment in an associate	—	—	—	—	—	—	—	—	—	471,027	461,990	537,377	—	—	—	471,027	461,990	537,377
Total assets	15,592,100	15,422,016	16,899,455	9,829,861	10,295,857	22,446,447	—	368,670	630,704	7,175,444	18,233,105	21,119,099	—	—	—	32,597,405	44,319,648	61,095,705
Segment liabilities	(4,795,521)	(4,254,418)	(3,033,327)	(3,878,273)	(3,372,175)	(10,200,032)	—	(106,862)	(21,665)	(7,801,808)	(3,275,687)	(7,272,193)	—	—	—	(16,475,602)	(11,009,142)	(20,527,217)
Capital expenditures	3,326,893	1,922,074	2,770,640	1,244,159	2,398,601	4,396,933	—	—	—	13,291	18,063	37,652	—	—	—	4,584,343	4,338,738	7,205,225

(All amounts expressed in Renminbi unless otherwise stated)

7. SEGMENT INFORMATION (CONT'D)

(b) Geographical segments

In determining the Group's geographical segments, revenues and results are attributed to the segments based on the location of the Group's customers, and assets are attributed to the segments based on the location of the Group's assets.

The Group is an oil and gas entity mainly engaged in the exploration, development and production of crude oil and natural gas offshore China. Approximately 86% of the total revenue of the Group is contributed by PRC customers, therefore, the Group's activities are conducted predominantly in the PRC. An analysis by geographical segment is as follows:

	PRC			Outside PRC			Total		
	2000	2001	2002	2000	2001	2002	2000	2001	2002
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
External sales	17,559,042	18,104,658	22,781,301	6,664,876	2,714,899	3,592,514	24,223,918	20,819,557	26,373,815
Segment assets	32,432,338	43,783,409	50,647,452	165,067	536,239	10,448,253	32,597,405	44,319,648	61,095,705
Capital expenditures	4,566,554	4,311,241	6,453,798	17,789	27,497	751,427	4,584,343	4,338,738	7,205,225

(c) An analysis of sales to the major customers by business segment is as follows:

	2000	2001	2002
	RMB'000	RMB'000	RMB'000
Production sharing contracts			
China Petroleum & Chemical Corporation	1,850,239	2,861,847	3,707,536
PetroChina Company Limited	690,853	1,126,127	1,187,571
Castle Peak Power Company Limited	1,199,090	1,205,649	1,247,639
	3,740,182	5,193,623	6,142,746
Independent operations			
China Petroleum & Chemical Corporation	4,474,822	3,420,685	3,183,341
PetroChina Company Limited	767,576	194,460	—
	5,242,398	3,615,145	3,183,341
	8,982,580	8,808,768	9,326,087

(All amounts expressed in Renminbi unless otherwise stated)

8. OIL AND GAS SALES

	2000	2001	2002
	RMB'000	RMB'000	RMB'000
Gross sales	21,747,888	19,663,251	26,086,646
Royalties	(208,885)	(283,014)	(464,113)
PRC government share oil	(2,719,680)	(1,819,449)	(1,843,239)
	18,819,323	17,560,788	23,779,294

9. MARKETING PROFIT

	2000	2001	2002
	RMB'000	RMB'000	RMB'000
Marketing revenues	5,126,015	2,537,032	2,377,469
Crude oil and product purchases	(5,097,765)	(2,453,312)	(2,326,338)
	28,250	83,720	51,131

10. SELLING AND ADMINISTRATIVE EXPENSES

	2000	2001	2002
	RMB'000	RMB'000	RMB'000
Salary and staff benefits	172,593	228,782	390,376
Utility and office expenses	70,069	89,462	100,502
Recovery of doubtful accounts	(57,658)	(4,966)	—
Transportation and entertainment	60,682	64,923	64,319
Rentals and maintenance	89,184	121,483	75,738
Selling expenses	36,481	38,069	38,548
Other	84,651	77,636	337,057
	456,002	615,389	1,006,540

(All amounts expressed in Renminbi unless otherwise stated)

11. INTEREST EXPENSES

	2000	2001	2002
	RMB'000	**RMB'000**	**RMB'000**
Interest on bank loans which are:			
- wholly repayable within five years	241,749	219,045	177,156
- not wholly repayable within five years	191,755	81,634	—
Interest expense to the parent company	41,500	8,415	—
Interest on long-term guaranteed notes	—	—	215,028
Other borrowing costs	—	6,510	12,426
Total interest	475,004	315,604	404,610
Less: Amount capitalised in property, plant and equipment	—	(198,970)	(187,714)
	475,004	116,634	216,896
Other finance costs:			
Increase in discounted amount of provisions arising from the passage of time (note 28)	—	—	77,896
	475,004	116,634	294,792

The interest rates used for interest capitalisation represented the cost of capital from raising the related borrowings and varied from 2.35% to 9.15% per annum for the year ended December 31, 2002 (2001: 2.35% to 9.15%, 2000: Nil).

12. DIRECTORS' REMUNERATION

Directors' remuneration disclosed pursuant to the Listing Rules and Section 161 of the Companies Ordinance is as follows:

	2000	2001	2002
	RMB'000	**RMB'000**	**RMB'000**
Fees for executive directors	—	—	—
Fees for non-executive directors	—	890	890
Other emoluments for executive directors			
- Basic salaries and allowances	400	6,106	6,654
- Bonus	440	560	1,109
- Pension scheme contribution	160	207	214
- Other	1,500	1,500	1,500

12. DIRECTORS' REMUNERATION (CONT'D)

The number of directors whose remuneration fell within the following bands is as follows:

	Number of Directors		
	2000	**2001**	**2002**
Nil to HK$1,000,000	7	6	8
HK$1,000,001 - HK$1,500,000	—	—	—
HK$1,500,001 - HK$2,000,000	—	2	2
HK$2,000,001 - HK$2,500,000	—	—	1
HK$2,500,001 - HK$3,000,000	—	1	—
	7	9	11

There was no arrangement under which a director waived or agreed to waive any remuneration during the years ended December 31, 2002, 2001 and 2000.

13. FIVE HIGHEST PAID INDIVIDUALS

The five highest paid individuals during the year are as follows:

	2000	**2001**	**2002**
	RMB'000	**RMB'000**	**RMB'000**
Basic salaries and allowances	400	7,280	8,227
Bonus	440	1,280	2,518
Pension scheme contributions	160	416	505
Other	1,500	1,500	2,732
Number of directors	5	4	4
Number of employees	—	1	1

(All amounts expressed in Renminbi unless otherwise stated)

13. FIVE HIGHEST PAID INDIVIDUALS (CONT'D)

The number of highest paid individuals whose remuneration fell within the following bands is as follows:

	Number of Senior Executives		
	2000	**2001**	**2002**
Up to HK$1,000,000	5	1	1
HK$1,500,001 - HK$2,000,000	—	2	2
HK$2,500,001 - HK$3,000,000	—	2	1
HK$4,500,001 - HK$5,000,000	—	—	1
	5	5	5

14. TAX

(i) Income tax

The Company and its subsidiaries are subject to income taxes on an entity basis on profit arising in or derived from the tax jurisdictions in which they are domiciled and operate. The Company is not liable for profits tax in Hong Kong as it does not have any assessable income currently sourced from Hong Kong.

The Company's subsidiary, CNOOC China Limited, is a wholly foreign-owned enterprise established in the PRC. It is exempt from the 3% local surcharge and is subject to an enterprise income tax of 30% under the prevailing tax rules and regulations. Moreover, CNOOC China Limited was entitled to a 50% reduction of enterprise income tax for three years until end of year 2000. Starting from January 1, 2001, CNOOC China Limited is subject to enterprise income tax at the normal rate of 30%.

The Company's subsidiary in Singapore, China Offshore Oil (Singapore) International Pte. Ltd., is subject to income tax at the rate of 10% and 26%, for its oil trading activities and other income generating activities respectively. The Company's subsidiaries owning interests in oil properties in Indonesia along the Malacca Strait are subject to corporate and dividend tax of 44%. The nine subsidiaries of Repsol-YPF, S.A. in Indonesia acquired by the Company during the year are all subject to corporate and branch profit tax at a rate of 48%. All of the Company's other subsidiaries are not subject to any income taxes in their respective jurisdictions for the year presented.

(All amounts expressed in Renminbi unless otherwise stated)

14. TAX (CONT'D)

(i) Income tax (cont'd)

An analysis of the provision for tax in the consolidated income statement was as follows:

	2000	2001	2002
	RMB'000	RMB'000	RMB'000
Overseas income taxes			
- Current	43,873	20,401	406,493
- Deferred	—	—	26,094
PRC enterprise income tax			
- Current	1,600,608	2,715,409	2,786,938
- Deferred	281,595	312,417	321,891
Tax charge for the year	1,926,076	3,048,227	3,541,416

With the tax holiday exemption, current income tax liabilities of our subsidiary in the PRC were reduced by approximately RMB 1,920,730,000 for the year ended December 31, 2000. The tax holiday exemption also increased the net income per share by RMB 0.30 for the year ended December 31, 2000.

The reconciliation of the statutory PRC enterprise income tax rate to the effective income tax rate of the Group was as follows:

	2000	2001	2002
	%	%	%
Statutory PRC enterprise income tax rate	33.0	33.0	33.0
Effect of tax holiday	(15.0)	—	—
Effect of tax exemption granted	(3.0)	(3.0)	(3.0)
Effect of future tax rate changes on originating timing differences	1.2	—	—
Effect of different tax rates for overseas subsidiaries	0.3	(1.2)	0.2
Tax effect of additional depreciation on revaluation and other permanent differences	(0.7)	(1.1)	(0.4)
Tax credit from government	—	—	(2.1)
Effective income tax rate	15.8	27.7	27.7

(All amounts expressed in Renminbi unless otherwise stated)

14. TAX (CONT'D)

(i) Income tax (cont'd)

The tax effect of significant timing differences of the Group was as follows:

	2001	2002
	RMB'000	RMB'000
Deferred tax assets		
- Provision for retirement and termination benefits	—	86,602
- Provision for dismantlement	479,439	671,796
- Provision for impairment of property, plant and equipment and write-off of unsuccessful exploratory drillings	1,880,791	933,636
	2,360,230	1,692,034
Deferred tax liabilities		
- Accelerated amortisation allowance for oil and gas properties	(4,123,867)	(7,833,190)
Net deferred tax liabilities	(1,763,637)	(6,141,156)

There were no significant unprovided deferred taxes in respect of the year (2001: Nil).

(ii) Other taxes

The Company's PRC subsidiary pays the following taxes:

— production taxes equal to 5% of independent production and production under production sharing contracts; and

— business tax of 3% to 5% on other income.

(All amounts expressed in Renminbi unless otherwise stated)

15. DIVIDENDS

	2000	2001	2002
	RMB'000	RMB'000	RMB'000
Final — HK$0.15 (2001: Nil; 2000: RMB0.98) per ordinary share	6,426,424	—	1,306,740
Interim — HK$0.11 (2001: HK$0.10; 2000: Nil) per ordinary share	—	871,194	958,314
	6,426,424	871,194	2,265,054

The payment of future dividends will be determined by the Company's board of directors. The payment of dividends will depend upon, among other things, future earnings, capital requirements and financial condition and general business conditions of the Company. The Company's ability to pay dividends will also depend on the cash flows determined by the dividends, if any, received by the Company from its subsidiaries and associated company. As the controlling shareholder, CNOOC will be able to influence the Company's dividend policy.

Cash dividends to the shareholders in Hong Kong will be paid in Hong Kong dollars and dividends to the ADS holders will be paid to the depositary in Hong Kong dollars and will be converted by the depositary into United States dollars and paid to the holders of ADSs.

On December 20, 2000, our board of directors proposed a dividend of RMB 0.98 per share, totaling approximately RMB 6,426,424,000, to our shareholders for the year ended December 31, 2000. The dividend distribution was approved by the shareholders in their annual general meeting held on February 4, 2001.

On August 27, 2001, the board of directors declared a 2001 interim dividend of HK$0.10 per share, totaling approximately RMB 871,194,000 to its shareholders, which was paid in October 2001.

On March 27, 2002, the board of directors proposed a final dividend of HK$0.15 per share, totaling approximately RMB 1,306,740,000 to its shareholders for the year ended December 31, 2001. The dividend distribution was approved by the shareholders in an annual meeting held on June 6, 2002 and the dividend was paid in June 2002. On August 23, 2002, the board of directors declared an interim dividend of HK$0.11 per share, totaling approximately RMB 958,314,000 to its shareholders.

(All amounts expressed in Renminbi unless otherwise stated)

16. EARNINGS PER SHARE AND PER ADS

The calculations of basic and diluted earnings per share are based on:

	2000	2001	2002
Earnings			
Net profit attributable to shareholders, used in the basic and diluted earnings per share calculations	RMB10,296,600,000	RMB7,957,631,000	RMB9,232,827,000
Shares			
Weighted average number of ordinary shares in issue during the year used in basic earnings per share calculation	6,331,114,421	7,941,383,305	8,214,165,655
Weighted average number of ordinary shares assumed issued at no consideration on deemed exercise of all share options outstanding during the year	—	905,498	5,119,729
Weighted average number of ordinary shares used in diluted earnings per share calculation	6,331,114,421	7,942,288,803	8,219,285,384

Net income per ADS for the three years ended December 31, 2002 has been computed by dividing net income by the number of ADS outstanding. Each ADS represented 20 shares.

(All amounts expressed in Renminbi unless otherwise stated)

17. PROPERTY, PLANT AND EQUIPMENT, NET

Movements in property, plant and equipment were:

	2002			
	Oil and gas properties	**Land and buildings**	**Vehicles and office equipment**	**Total**
	RMB'000	**RMB'000**	**RMB'000**	**RMB'000**
Cost or valuation:				
At beginning of the year				
As previously reported	41,177,459	824,781	57,900	42,060,140
Cumulative effect of change in accounting policy (Note 3)	1,515,088	—	—	1,515,088
At beginning of year as restated	42,692,547	824,781	57,900	43,575,228
Additions	7,419,956	—	37,653	7,457,609
Acquisition of subsidiaries	8,646,487	—	—	8,646,487
Disposals and write-offs	(438,011)	—	(2,011)	(440,022)
Exchange realignment	801	—	178	979
End of year	58,321,780	824,781	93,720	59,240,281
Analysis of cost or valuation				
At cost	58,321,780	—	93,720	58,415,500
At revaluation	—	824,781	—	824,781
	58,321,780	824,781	93,720	59,240,281
Accumulated depreciation, depletion and amortisation:				
At beginning of the year				
As previously reported	(18,154,653)	(55,653)	(22,335)	(18,232,641)
Cumulative effect of change in accounting policy (Note 3)	(778,240)	—	—	(778,240)
At beginning of year as restated	(18,932,893)	(55,653)	(22,335)	(19,010,881)
Depreciation provided during the year	(4,126,625)	(25,374)	(7,110)	(4,159,109)
Disposals	—	—	1,777	1,777
Exchange realignment	(82)	—	(166)	(248)
End of year	(23,059,600)	(81,027)	(27,834)	(23,168,461)
Net book value:				
Beginning of year as restated	23,759,654	769,128	35,565	24,564,347
End of year	35,262,180	743,754	65,886	36,071,820
Had the property, plant and equipment been carried at cost less accumulated depreciation, depletion and amortisation, the carrying amount of each class would have been:				
Cost	58,321,780	550,110	93,720	58,965,610
Accumulated depreciation, depletion and amortisation	(23,059,600)	(55,131)	(27,834)	(23,142,565)
	35,262,180	494,979	65,886	35,823,045

(All amounts expressed in Renminbi unless otherwise stated)

17. PROPERTY, PLANT AND EQUIPMENT, NET (CONT'D)

	2001			
	Oil and gas properties	**Land and buildings**	**Vehicles and office equipment**	**Total**
	RMB'000	**RMB'000**	**RMB'000**	**RMB'000**
Cost or valuation:				
At beginning of year	37,319,924	824,781	39,837	38,184,542
Additions	4,320,675	—	18,063	4,338,738
Disposals and write-offs	(463,140)	—	—	(463,140)
End of year	41,177,459	824,781	57,900	42,060,140
Analysis of cost or valuation				
At cost	41,177,459	—	57,900	41,235,359
At revaluation	—	824,781	—	824,781
	41,177,459	824,781	57,900	42,060,140
Accumulated depreciation, depletion and amortisation:				
At beginning of year	(15,482,082)	(30,280)	(17,805)	(15,530,167)
Depreciation provided during the year	(2,572,896)	(25,373)	(4,530)	(2,602,799)
Impairment during the year recognised in income statement	(99,675)	—	—	(99,675)
End of year	(18,154,653)	(55,653)	(22,335)	(18,232,641)
Net book value:				
Beginning of year	21,837,842	794,501	22,032	22,654,375
End of year	23,022,806	769,128	35,565	23,827,499
Had the property, plant and equipment been carried at cost less accumulated depreciation, depletion and amortisation, the carrying amount of each class would have been:				
Cost	41,177,459	550,110	57,900	41,785,469
Accumulated depreciation, depletion and amortisation	(18,154,653)	(38,914)	(22,335)	(18,215,902)
	23,022,806	511,196	35,565	23,569,567

Impairment loss for the year ended December 31, 2001, represented the estimated impairment resulting from downward revision of the reserves of certain oil fields.

Land and buildings are held outside Hong Kong with lease terms of 50 years.

17. PROPERTY, PLANT AND EQUIPMENT, NET (CONT'D)

The land and buildings were revalued by an independent valuer, Sallmanns (Far East) Limited, Chartered Surveyors (the "Valuer") as of December 31, 2000 using a depreciated replacement cost approach. The depreciated replacement cost approach considers the cost to reproduce or replace in new condition the property being appraised in accordance with current construction costs for similar property in the locality with allowance for accrued depreciation as evidenced by observed condition or obsolescence present, whether arising from physical, functional or economic causes. The Valuer assumed that the assets would be used for the purposes for which they are presently used and did not consider alternative uses. Certain land use rights were previously granted by the PRC government at no cost.

The revaluation surplus of approximately RMB104,073,000 arising from the revaluation of the land and buildings as at December 31, 2000 has been recorded by us.

18. INVESTMENT IN AN ASSOCIATE

Investment in an associate represents a 30% equity interest of CNOOC China Limited in Shanghai Petroleum and Natural Gas Company Limited ("SPC"). SPC was incorporated on September 7, 1992 in the PRC with limited liability and is principally engaged in offshore petroleum exploration, development, production and sales in the South Yellow Sea and East China Sea areas. The issued and paid-up capital of SPC is RMB 900,000,000.

	2001	**2002**
	RMB'000	**RMB'000**
Unlisted shares, at cost	270,000	270,000
Accumulated share of profit	290,990	357,377
Dividends received	(99,000)	(90,000)
	461,990	537,377

The directors are of the opinion that the underlying value of the investment in an associate is not less than the carrying amount of the associate as of December 31, 2002 and 2001.

(All amounts expressed in Renminbi unless otherwise stated)

19. ACCOUNTS RECEIVABLE, NET

	2001	2002
	RMB'000	RMB'000
Trade receivables	1,204,907	3,063,266
Less: Provision for doubtful accounts	(10,727)	—
	1,194,180	3,063,266

The Group's trading terms with its customers are mainly on credit, except for new customers, where payment in advance is normally required. The customers are required to make payment within 30 days after the delivery of oil and gas. As of December 31, 2002 and 2001, substantially all the accounts receivable were aged within six months.

20. INVENTORIES AND SUPPLIES

	2001	2002
	RMB'000	RMB'000
Materials and supplies	428,991	585,431
Oil in tanks	198,346	263,174
	627,337	848,605

21. SHORT-TERM INVESTMENTS

As of December 31, 2002 and 2001, short-term investments mainly represented investments in liquidity funds and were stated at fair value at the balance sheet date.

Details were as follows:

	2001	2002
	RMB'000	RMB'000
Liquidity funds	7,675,622	5,537,191
Corporate bonds	1,177,991	951,876
Common stock	42,191	42,211
	8,895,804	6,531,278

22. ACCOUNTS PAYABLE

As of December 31, 2002 and 2001, substantially all the accounts payable were aged within six months.

(All amounts expressed in Renminbi unless otherwise stated)

23. OTHER PAYABLES AND ACCRUED LIABILITIES

	2001	2002
	RMB'000	RMB'000
Accrued payroll and welfare payable	132,773	149,501
Provision for retirement and termination benefit	—	211,321
Accrued expenses	434,766	793,823
Advances from customers	86,301	60,101
Royalties payable	—	208,214
Other payables	159,306	289,448
	813,146	1,712,408

As of December 31, 2002, deferred revenue from gas sales contract amounted to approximately RMB 5,582,000 (2001: RMB 5,581,000) and was included in other payables.

24. LONG-TERM BANK LOANS

As of December 31, 2002 and 2001, long-term bank loans of the Group were used primarily to finance the development of oil and gas properties and to meet working capital requirements.

	Interest rate and final maturity	2001	2002
		RMB'000	RMB'000
RMB denominated bank loans	Floating prevailing market rate adjusted annually with maturities through 2006	670,000	—
	Fixed interest rate at 5.94% per annum through 2005	66,270	57,270
US$ denominated bank loans	Floating LIBOR rate with maturities through 2003	1,177,761	259,907
	Fixed interest rate of 9.15% per annum with maturities through 2006	827,660	827,730
Japanese Yen denominated bank loans	Fixed interest rate ranging from 2.35% to 5.15% per annum, with maturities through 2007	1,745,848	93,704
		4,487,539	1,238,611
Less: current portion of long-term bank loans		(1,231,840)	(297,518)
		3,255,699	941,093

(All amounts expressed in Renminbi unless otherwise stated)

24. LONG-TERM BANK LOANS (CONT'D)

As of December 31, 2002, LIBOR was approximately 1.4% per annum (2001: 2.0% per annum).

As of December 31, 2002, all the bank loans of the Group were unsecured and approximately RMB 259,907,000 (2001: RMB 991,537,000) of the outstanding borrowings were guaranteed by CNOOC.

The maturities of long-term bank loans are as follows:

	2001	2002
	RMB'000	RMB'000
Balances due:		
- Within one year	1,231,840	297,518
- After one year but within two years	794,593	27,541
- After two years but within three years	462,564	48,341
- After three years but within four years	483,364	846,471
- After four years but within five years	1,231,423	18,740
	4,203,784	1,238,611
- More than five years	283,755	—
	4,487,539	1,238,611
Amount due within one year shown under current liabilities	(1,231,840)	(297,518)
	3,255,699	941,093

Supplemental information with respect to long-term bank loans:

For the year ended December 31,	Balance at year end	Weighted average interest rate at year end	Maximum amount outstanding during the year	Average amount outstanding during the year*	Weighted average interest rate during the year**
	RMB'000		RMB'000	RMB'000	
2000	5,746,377	6.28%	8,908,583	7,017,601	6.18%
2001	4,487,539	5.03%	5,746,377	5,116,958	5.66%
2002	1,238,611	7.19%	4,487,539	2,863,075	6.11%

* The average amount outstanding is computed by dividing the total of outstanding principal balances as of January 1 and December 31 by two.

** The weighted average interest rate is computed by dividing the total of weighted average interest rates as of January 1 and December 31 by two.

(All amounts expressed in Renminbi unless otherwise stated)

25. 6.375% LONG-TERM GUARANTEED NOTES

On March 1, 2002, CNOOC Finance (2002) Limited, a company incorporated in the British Virgin Islands on January 24, 2002 and a wholly-owned subsidiary of the Company, issued US$500,000,000 principal amount of 6.375% guaranteed notes due in 2012. The obligations of CNOOC Finance (2002) Limited in respect of the notes are unconditionally and irrevocably guaranteed by the Company.

26. BALANCES WITH THE PARENT COMPANY

As of December 31, 2002 and 2001, the balances with CNOOC were unsecured, interest-free and repayable on demand.

27. RELATED PARTY TRANSACTIONS

The Group has entered into several agreements with CNOOC and its affiliates, which govern the provision of materials, utilities and ancillary services, the provision of technical services, the provision of research and development services, the provision of bank guarantees and various other commercial arrangements.

(All amounts expressed in Renminbi unless otherwise stated)

27. RELATED PARTY TRANSACTIONS (CONT'D)

In addition to the transactions and balances detailed elsewhere in these financial statements, the Group had the following material transactions with related parties during the year:

	Notes	2000	2001	2002
		RMB'000	RMB'000	RMB'000
Included in exploration costs:				
Provision of geological and geophysical services	(ii)	55,295	139,659	100,738
Provision of research and development services	(iii)	109,880	89,999	95,507
Provision of drilling services	(ii)	106,150	389,847	396,814
Included in operating expenses:				
Provision of technical services	(ii)	254,276	44,044	68,130
Provision of research and development services	(iii)	51,853	29,587	46,226
Provision of oil transportation services	(i)	171,490	68,399	200,709
Provision of production related services	(i)	597,579	579,207	208,730
Provision of materials, utilities and ancillary services	(i)	163,828	148,149	470,030
Included in selling and administrative expenses:				
Rental of office lease	(iv)	49,089	45,524	54,421
Provision of research and development services	(iii)	—	40,763	25,621
Provision of other ancillary services		31,748	87,557	110,407
Included in interest expense:				
Interest income from a related company		25	—	—
Interest expense to CNOOC		41,500	8,415	—
Capitalised under property, plant and equipment:				
Provision of oil and gas property construction services	(ii)	865,549	1,341,545	1,837,573
Provision of drilling services	(ii)	445,414	285,834	591,749
Provision of well measurement services	(ii)	140,065	97,633	83,883

(i) Provision of materials, utilities and ancillary services

CNOOC China Limited has entered into materials, utilities and ancillary services supply agreements with the affiliates of CNOOC. Under these agreements, the affiliates of CNOOC provide to CNOOC China Limited various materials, utilities and ancillary services for a term of three years from September 9, 1999.

(All amounts expressed in Renminbi unless otherwise stated)

27. RELATED PARTY TRANSACTIONS (CONT'D)

(i) Provision of materials, utilities and ancillary services (cont'd)

The materials, utilities and ancillary services are provided at:

— state-prescribed prices; or

— where there is no state-prescribed price, market prices, including the local or national market prices or the prices at which CNOOC's affiliates previously provided the relevant materials, utilities and ancillary services to independent third parties, or

— where neither of the prices mentioned above is applicable, the cost to CNOOC's affiliates of providing the relevant materials, utilities and services, including the cost of sourcing or purchasing from third parties, plus a margin of not more than 5% before any applicable taxes.

On December 5, 2002, the Group has renewed the agreement for the term of three years from December 31, 2002.

(ii) Technical services

CNOOC China Limited has entered into technical service agreements with specialised companies formed by CNOOC.

According to the agreements, the Group uses the technical services provided by these specialised companies, including:

— offshore drilling;

— ship tugging, oil tanker transportation and security services;

— well survey, well logging, well cementation and other related technical services;

— collection of geophysical data, ocean geological prospecting, and data processing;

— platform fabrication service and maintenance; and

— design, construction, installation and test of offshore and onshore production facilities.

The technical services are provided by the related companies at prices on an arms-length negotiation on normal commercial terms or on terms no less favourable than those available to independent third parties, under prevailing market conditions.

(All amounts expressed in Renminbi unless otherwise stated)

27. RELATED PARTY TRANSACTIONS (CONT'D)

(iii) Research and development services

Under the terms of a general research and development services agreement with CNOOC's subsidiary, China Offshore Oil Research Centre (the "Centre"), the Group pays the Centre for a term of three years from September 9, 1999, with an annual amount of RMB 110,000,000, for the provision of such services, including:

— geophysical exploration services;

— seismic data processing;

— comprehensive exploration research services; and

— information technology services.

On December 5, 2002, the Company renewed the agreement for a term of three years from December 31, 2002. Under the agreement, the Group will pay the Centre RMB 140,000,000, RMB 150,000,000 and RMB 160,000,000 respectively.

(iv) Lease agreements

The Group has entered into lease agreements with affiliates of CNOOC for the leasing of various office, warehouse and residential premises for a three-year term commencing September 9, 1999. The lease charges were based on the prevailing market rates at the inception of the leases.

On December 5, 2002, the Group has renewed the lease agreements for the terms of three years from December 31, 2002.

(v) Sales of crude oil, condensate oil and liquefied petroleum gas

The Group sells crude oil, condensate oil and liquefied petroleum gas to CNOOC's affiliates which engage in the downstream petroleum business at the international market price. For the year ended December 31, 2002, the total sales amounted to approximately RMB 4,361,852,000 (2001: RMB 1,814,197,000, 2000: RMB 507,677,000).

As of December 31, 2002, the Group had cash and cash equivalents and time deposits aggregating RMB 2,740 million (2001: Nil) placed with CNOOC Finance Corporation Limited ("CNOOC Finance"), a wholly-owned subsidiary of CNOOC. CNOOC Finance is a non-bank finance company supervised by the People's Bank of China ("PBOC") and the Company is one of its customers. The interest rates offered by CNOOC Finance were same as the rates promulgated by the PBOC which were applicable to accounts deposits with PRC banks or finance companies. The interest income received for the year ended 31 December 2002 was approximately RMB 3,516,000 (2001: Nil, 2000: Nil).

(All amounts expressed in Renminbi unless otherwise stated)

27. RELATED PARTY TRANSACTIONS (CONT'D)

In addition to the recurring transactions described above, pursuant to a conditional agreement dated August 27, 2001, the Group will acquire interests in certain oil and natural gas fields in the Xihu Trough in the East China Sea of the PRC from CNOOC for a total consideration of US$45,000,000. As of December 31, 2002, the transaction had not been completed and the legal title of the reserves had not been passed to the Group. The amount paid for the interests is included in the property, plant and equipment in the balance sheet as of December 31, 2002.

28. PROVISION FOR DISMANTLEMENT

Provision for dismantlement represents the estimated costs of dismantling offshore oil platforms and abandoning oil and gas properties. Provision for dismantlement has been classified under long-term liabilities. As detailed in Note 3 above, the Group changed its method of accounting for the provision for dismantlement during the year. As such, the associated cost is capitalised and the liability is discounted and an accretion expense is recognised during the credit-adjusted risk-free interest rate in effect when the liability is initially recognised. The current year income statement charge represents the amortisation charge on the dismantlement liabilities capitalised in accordance with SSAP 28 and is included in the accumulated depreciation, depletion and amortisation in Note 17. The prior year income statement charges were calculated using the unit-of-production method on the estimated total undiscounted dismantlement costs.

The details of the provision for dismantlement were as follows:

	2001	2002
	RMB'000	**RMB'000**
At beginning of year:		
As previously reported	1,507,763	1,598,130
Cumulative effect of change in accounting policy (Note 3)	—	310,911
As restated	1,507,763	1,909,041
Additional provision based on unit-of-production method	90,367	—
Additions during the year and capitalised in oil and gas properties	—	252,383
Increase in discounted amount of provisions arising from the passage of time	—	77,896
End of year	1,598,130	2,239,320

(All amounts expressed in Renminbi unless otherwise stated)

29. SHARE CAPITAL

Shares

	Number of Shares	Share capital
		HK$'000
Authorised:		
Ordinary shares of HK$0.10 each at December 31, 2002 and 2001	15,000,000,000	1,500,000

	Number of Shares	Share capital	Share capital equivalent of
		HK$'000	**RMB'000**
Issued and fully paid:			
Ordinary shares of HK$0.10 each at January 1, 2001	6,557,575,755	655,758	701,181
Issue of shares during the initial public offering (i)	1,656,589,900	165,659	175,797
At December 31, 2001	8,214,165,655	821,417	876,978
Ordinary shares of HK$0.10 each at January 1 and December 31, 2002	8,214,165,655	821,417	876,978

(i) The Company completed its initial public offering in 2001 and the details were as follow:

— issued 1,442,426,000 shares of HK$0.10 each at HK$6.01 per share and in the form of ADSs were listed on the Stock Exchange of Hong Kong Limited ("HKSE") and the New York Stock Exchange on February 28, 2001 and February 27, 2001, respectively; and

— issued 214,163,900 shares of HK$0.10 each at HK$6.01 per share on March 23, 2001 upon the exercise of an over-allotment option by the underwriters of the global offering.

The net proceeds from the initial public offering (including the exercise of the over-allotment option) amounted to approximately RMB 10,101,564,000, after deducting expenses of approximately RMB 288,058,000.

Share options

The Company has share option schemes which provide for the grant of options to the Company's senior management. Under these share option schemes in accordance with SSAP 34, the remuneration committee of the Company's board of directors will from time to time propose for the board's approval the recipient of and number of shares underlying each option. These scheme provide for issuance of options exercisable for shares granted under these schemes as described below not exceeding 10% of the total number of the Company's outstanding shares, excluding shares issued upon exercise of options granted under the scheme from time to time.

29. SHARE CAPITAL (CONT'D)

Share options (cont'd)

On February 4, 2001, the Company adopted a pre-global offering share option scheme (the "Pre-Global Offering Share Option Scheme"). Pursuant to the Pre-Global Offering Share Option Scheme:

1. options for an aggregate of 4,620,000 shares have been granted;
2. the subscription price per share is HK$5.95; and
3. the period during which an option may be exercised is as follows:
   (a) 50% of the shares underlying the option shall vest 18 months after the date of the grant; and
   (b) 50% of the shares underlying the option shall vest 30 months after the date of the grant.

The exercise period for options granted under the Pre-Global Offering Share Option Scheme shall end not later than 10 years from March 12, 2001.

On February 4, 2001, the Company adopted a share option scheme (the "2001 Share Option Scheme") for the purposes of recognising the contribution that certain individuals had made to the Company and attracting and retaining the best available personnel to the Company. Pursuant to the 2001 Share Option Scheme:

1. options for an aggregate of 8,820,000 shares have been granted;
2. the subscription price per share is HK$6.16; and
3. the period during which an option may be exercised is as follows:
   (a) one-third of the shares underlying the option shall vest on the first anniversary of the date of the grant;
   (b) one-third of the shares underlying the option shall vest on the second anniversary of the date of the grant; and
   (c) one-third of the shares underlying the option shall vest on the third anniversary of the date of the grant.

The exercise period for options granted under the 2001 Share Option Scheme shall end not later than 10 years from August 27, 2001.

In view of the amendments to the relevant provisions of the Listing Rules regarding the requirements of share option schemes of a Hong Kong listed company effective on September 1, 2001, no further options will be granted under the 2001 Share Option Scheme.

In June 2002, the Company adopted a new share option scheme (the "2002 Share Option Scheme").

(All amounts expressed in Renminbi unless otherwise stated)

29. SHARE CAPITAL (CONT'D)

Share options (cont'd)

Under the 2002 Share Option Scheme, the Directors of the Company may, at their discretion, invite employees, including executive directors, of the Company or any of its subsidiaries, to take up options to subscribe for shares. The maximum aggregate number of shares (including those that could be subscribed for under the Pre-Global Offering Share Option Scheme and the 2001 Share Option Scheme) which may be granted shall not exceed 10% of the total issued share capital of the Company. The maximum number of shares which may be granted under the 2002 Share Option Scheme to any individual in any 12 months period up to the next grant shall not exceed 1% of the total issued share capital of the Company from time to time.

According to the 2002 Share Option Scheme, the consideration payable by a participant for the grant of an option will be HK$1.00. The subscription price of a share payable by a participant upon the exercise of an option will be determined by the Directors at their discretion at the date of grant, except that such price may not be set below a minimum price which is the highest of:

1. the nominal value of a share;

2. the average closing price of the shares on the HKSE as stated in the HKSE's quotation sheets for the five trading days immediately preceding the date of grant of the option; and

3. the closing price of the shares on the HKSE as stated in the HKSE's quotation sheets on the date of grant of the option.

The period under which an option may be exercised is as follows:

1. one-third of the shares underlying the option shall vest on the first anniversary of the date of the grant;

2. one-third of the shares underlying the option shall vest on the second anniversary of the date of the grant; and

3. one-third of the shares underlying the option shall vest on the third anniversary of the date of the grant.

The exercise period for options granted under the 2002 Share Option Scheme shall end not later than 10 years from the date on which the option is granted.

No options granted under the share option scheme and the pre-global offering share option scheme have been exercised since the date of grant and up to the date when the board of directors approved the financial statements. The total number of options exercisable as of December 31, 2002 was 9,864,167.

(All amounts expressed in Renminbi unless otherwise stated)

30. RESERVES

According to the laws and regulations of the PRC and articles of association of CNOOC China Limited, CNOOC China Limited is required to provide for certain statutory funds, namely, general reserve fund and staff and workers' bonus and welfare funds, which are appropriated from net profit and after making good losses from previous years, but before dividend distribution. CNOOC China Limited is required to allocate at least 10% of its net profit as reported in accordance with the generally accepted accounting principles in the PRC ("PRC GAAP") to the general reserve fund until the balance of such fund has reached 50% of its registered capital. Appropriation to staff and workers' bonus and welfare funds, which is determined at the discretion of CNOOC China Limited's directors, is charged to expense as incurred under Hong Kong GAAP. The general reserve fund can only be used, upon approval by the relevant authority, to offset against accumulated losses or increase capital. Staff and workers' bonus and welfare fund can only be used for special bonuses or collective welfare of employees, and assets acquired through this fund shall not be taken as assets of CNOOC China Limited.

As of December 31, 2002, the general reserve fund appropriated amounted to RMB 2,232,410,000 (2001: RMB 1,535,360,000), representing approximately 22.3% (2001: 15.4%) of the total registered capital of CNOOC China Limited.

As of December 31, 2002 and 2001, the distributable profits of the Company amounted to approximately RMB 2,939,757,000 and RMB 220,127,000 respectively.

Included in retained earnings is an amount of RMB 456,377,000 (2001: RMB 311,990,000), being the retained earnings attributable to an associate.

The cumulative translation reserves and revaluation reserves have been established and will be dealt with in accordance with the accounting policies adopted for foreign currency translation and the revaluation of land and buildings.

31. RETIREMENT AND TERMINATION BENEFITS

All the Group's full-time employees in the PRC are covered by a government regulated pension, and are entitled to an annual pension equal to their basic salaries at their retirement dates. The PRC government is responsible for the pension liabilities to these retired employees. The Group is required to make annual contributions to the government-regulated pension at rates ranging from 12% to 22.5% of the employees' basic salaries.

The contribution made by the Group to the PRC government pension plan for the year ended December 31, 2002 amounted to approximately RMB 7,042,000 (2001: RMB 6,392,000, 2000: RMB 12,842,000).

The Company is required to make contributions to a defined contribution of a mandatory provident fund at a rate of 5% of the basic salaries for all full time employees in Hong Kong. The related pension costs are treated expenses as incurred.

(All amounts expressed in Renminbi unless otherwise stated)

31. RETIREMENT AND TERMINATION BENEFITS (CONT'D)

The Group provides retirement and termination benefits for all local employees in Indonesia in accordance with Indonesia labour law, while the employee benefits provides to expatriate staff in accordance with the relevant employment contracts. The Company has adopted an accounting policy to record liabilities for the retirement and termination benefits. The provisions for retirement and termination benefits in Indonesia for the year ended December 31, 2002 amounted to approximately RMB 46,350,000 (2001: Nil, 2000: Nil).

32. NOTES TO THE CASH FLOW STATEMENT

(a) Reconciliation of profit before tax to cash generated from operations

	2000	2001	2002
	RMB'000	RMB'000	RMB'000
Profit before tax	12,222,676	11,005,858	12,774,243
Adjustments for:			
Interest income	(236,624)	(317,706)	(147,870)
Interest expense	475,004	116,634	294,792
Exchange losses/(gains), net	(324,178)	(261,305)	113,814
Share of profit of an associate	(218,326)	(89,963)	(165,387)
Short-term investment income	—	(220,650)	(193,277)
Depreciation, depletion and amortisation	2,577,882	2,566,920	4,019,532
Provision for impairment of property, plant and equipment	—	99,675	—
Recovery of doubtful accounts	(57,658)	(4,966)	—
Loss on disposals and write-off of property, plant and equipment	220,146	456,827	437,799
Dismantlement	103,569	90,367	126,139
Amortisation of discount of long-term guaranteed notes	—	—	6,100
Operating cash flows before movements in working capital	14,762,491	13,441,691	17,265,885
Decrease in accounts receivables	1,146,613	726,976	497,959
(Increase)/decrease in inventories and supplies	(2,438)	35,422	(20,211)
Increase in other current assets	(39,386)	(447,473)	(705,664)
Increase in amounts due from related companies	—	—	(276,771)
Increase/(decrease) in accounts payable, other payables and accrued liabilities	(1,440,278)	379,233	353,452
Increase/(decrease) in other taxes payable	2,701	(110,867)	73,551
Increase in amounts due to related companies	—	—	73,769
Cash generated from operations	14,429,703	14,024,982	17,261,970

32. NOTES TO THE CASH FLOW STATEMENT (CONT'D)

(b) Acquisition of subsidiaries

	2000	2001	2002
	RMB'000	RMB'000	RMB'000
Net assets acquired:			
Property, plant and equipment, net	—	—	8,646,487
Other current assets	—	—	35,175
Inventories and supplies	—	—	187,619
Accounts receivable	—	—	2,367,045
Cash and bank balances	—	—	1,652
Accounts payable	—	—	(1,577,214)
Other payables and accrued liabilities	—	—	(952,911)
Tax payable	—	—	(70,247)
Deferred tax	—	—	(3,901,780)
	—	—	4,735,826
Satisfied by:			
Cash	—	—	4,735,826

An analysis of the net outflow of cash and cash equivalents in respect of the acquisition of subsidiaries is as follows:

	2000	2001	2002
	RMB'000	RMB'000	RMB'000
Cash consideration	—	—	4,735,826
Cash and bank balances acquired	—	—	(1,652)
Net outflow of cash and cash equivalents in respect of the acquisition of subsidiaries	—	—	4,734,174

On April 19, 2002, the Group acquired nine subsidiaries of Repsol-YPF, S.A. which held a portfolio of operated and non-operated interests in oil and gas production sharing and technical assistance contracts in contract areas located offshore and onshore Indonesia. Further details of the transaction are included in note 5 to the financial statements.

The subsidiaries acquired during the year contributed RMB 3,317 million to turnover and RMB 464 million to the consolidated profit after tax for the year ended December 31, 2002.

(All amounts expressed in Renminbi unless otherwise stated)

32. NOTES TO THE CASH FLOW STATEMENT (CONT'D)

(c) Major non-cash transaction

The cash generated from operations of RMB 17,634,448,000 did not take into account of a transfer of prepayment of RMB 372,479,000 recorded in 2001 to property, plant and equipment relating to acquisition of interests in certain oil and natural gas fields in the Xihu Trough in the East China Sea of the PRC from CNOOC for a total consideration of US$45,000,000.

33. CONTINGENT LIABILITIES

As of December 31, 2002 and 2001, there were no material contingent liabilities not provided for in the financial statements.

34. COMMITMENTS

(i) Capital commitments

As of 31 December 2002 and 2001, the Group had the following capital commitments, principally for the construction and purchase of property, plant and equipment:

	2001	2002
	RMB'000	RMB'000
Contracted for	1,606,700	1,715,173
Authorised, but not contracted for	5,183,690	9,060,722

As of December 31, 2002, the Group had unutilised banking facilities amounted to approximately RMB 31,646,389,000 (2001: RMB 7,599,371,000).

(ii) General research and development commitments

According to the general research and development services agreement with the Centre renewed on December 5, 2002, the Group agreed to pay the Centre for a term of three years from December 31, 2002, an annual amount of RMB 140,000,000, RMB 150,000,000 and RMB 160,000,000 respectively for provision of general geophysical exploration services, comprehensive exploration research services, information technology services and seismic data processing. As of December 31, 2002, commitments for research and development services to be provided by the Centre amounted to approximately RMB 450,000,000 (2001: RMB 83,382,500).

(All amounts expressed in Renminbi unless otherwise stated)

34. COMMITMENTS (CONT'D)

(iii) Operating lease commitments

Operating lease commitments as of December 31, 2002 amounted to approximately RMB 50,645,000 (2001: RMB 94,079,000) and were as follows:

	2001	2002
	RMB'000	RMB'000
Commitment due:		
- Within one year	48,789	47,017
- After one year but within two years	45,290	2,131
- After two years but within three years	—	1,497
	94,079	50,645

(iv) Commitment to invest in an Australian gas project

In August 2001, the Company signed a Memorandum of Understanding to explore the feasibility of acquiring an equity interest in certain oil and gas assets in a large natural gas field in Australia, and to develop the natural gas market in coastal China. In November 2001, the Company entered into a Heads of Agreement to establish a joint venture to develop Northwest Shelf gas in Australia. The Company has agreed to co-invest in the development of Australia's Northwest Shelf gas project and to produce and process liquefied natural gas to sell to the China markets, subject to the joint venture successfully bidding for the contract to supply liquefied natural gas to an import facility in Guangdong Province, in which CNOOC, the parent company, has an equity interest.

On October 21, 2002, the Company entered into a definitive agreement with Northwest Shelf Venture partner to acquire an interest up to 5.56% in the North West Shelf Gas Project ("NWS Gas Project") titles and assume a 25% interest in the China LNG Joint Venture for a total consideration of US$366 million.

(v) Commitments to invest in an Indonesian gas project

In September 2002, the Company entered into a Heads of Agreement to acquire a participating interest in the reserves and upstream production of the proposed joint venture known as the Tangguh LNG Project of Indonesia ("Tangguh LNG Project"). The Heads of Agreement provides for the Company to acquire from BP an equivalent 12.5% stake in the Tangguh LNG Project for approximately US$275 million through the acquisition of certain interests in PSCs. The Tangguh LNG Project comprises three PSC areas: the Berau PSC, the Muturi PSC and the Wiriagar PSC. The Tangguh LNG Project partners have signed a conditional 25-year LNG Supply Contract to provide up to 2.6 million tonnes per annum of LNG to the Fujian LNG terminal project in China, beginning in 2007. Subsequent to December 31, 2002, the Company completed the acquisition (which was effective as of January 1, 2003) for a consideration of US$275 million.

(All amounts expressed in Renminbi unless otherwise stated)

34. COMMITMENTS (CONT'D)

(v) Commitments to invest in an Indonesian gas project (cont'd)

In addition, a repurchase agreement was entered into whereby put options and call options are granted to the Company and the sellers, respectively, to sell or to repurchase the interests in the abovementioned PSCs. The options are exercisable if

1) the LNG Supply Contract is terminated due to the non-satisfaction of the conditions precedent to the LNG Supply Contract; or

2) the LNG Supply Contract is otherwise legally ineffective

on or before December 31, 2004. The exercise prices of the options are determined based on the original consideration paid plus adjustments stipulated in the repurchase agreement.

(vi) Financial instruments

(a) Currency swap contracts

As of December 31, 2002 and 2001, the Group had currency swap contracts with a financial institution to sell United States dollars in exchange for Japanese Yen in order to hedge against future repayments of certain Japanese Yen denominated loans. The hedged Japanese Yen loans bore interest at fixed rate of 4.5% per annum. The interest stipulated in the swap contract for the United States dollars was floating LIBOR rate.

The details are as follows:

	2001		2002	
	Notional contract amount	Weighted average contractual exchange rate	Notional contract amount	Weighted average contractual exchange rate
	(JPY'000)	(JPY/US$)	(JPY'000)	(JPY/US$)
Year				
2002	271,470	95.00	—	—
2003	271,470	95.00	271,470	95.00
2004	271,470	95.00	271,470	95.00
2005	271,470	95.00	271,470	95.00
2006	271,470	95.00	271,470	95.00
2007	271,470	95.00	271,470	95.00

(All amounts expressed in Renminbi unless otherwise stated)

34. COMMITMENTS (CONT'D)

(vi) Financial instruments (cont'd)

(b) Fair value of financial instruments

The carrying amounts of cash and cash equivalents, time deposits and short-term investments approximated fair value due to the short maturity of these instruments.

The estimated fair value of long-term bank loans based on current market interest rates was approximately RMB 1,388,720,000 as of December 31, 2002 and comparably approximated their book value as of December 31, 2001.

The estimated fair value of 6.375% long-term guaranteed notes based on current market interest rates was approximately RMB 4,482,378,000 as of December 31, 2002.

35. CONCENTRATION OF RISKS

(a) Credit risk

The carrying amount of cash and cash equivalents, time deposits, liquidity funds and bond investments, accounts receivable and other receivables, and due from related parties and other current assets except for prepayments represents our maximum exposure to credit risk in relation to financial assets.

The majority of our accounts receivable is related to sales of oil and natural gas to third party customers. We perform ongoing credit evaluations of our customers' financial condition and generally do not require collateral on accounts receivable. We maintain a provision for doubtful accounts and actual losses have been within management's expectation.

No other financial assets carry a significant exposure to credit risk.

(b) Interest rate risk

The directors of the Company believe that the exposure to interest rate risk of financial assets and liabilities as of December 31, 2002 was not significant. The interest rates and terms of repayment of our long-term bank loans are disclosed in Note 24.

(c) Currency risk

Substantially all of the revenue-generating operations of the Group are transacted in US$ for overseas sales and RMB for domestic sales. On January 1, 1994, the PRC government abolished the dual rate system and introduced single rate of exchange as quoted by the People's Bank of China. However, the unification of the exchange rate does not imply free convertibility of RMB into foreign currencies. As foreign exchange transactions continue to take place either through the People's Bank of China or other banks authorised to buy and sell foreign currencies at the exchange rates quoted by the People's Bank of China, approval of foreign currency payment by the People's Bank of China or other institution requires submitting a payment application form together with suppliers' invoices, shipping documents and signed contracts.

(All amounts expressed in Renminbi unless otherwise stated)

35. CONCENTRATION OF RISKS (CONT'D)

(d) Business risk

The major operations are conducted in the PRC and Indonesia and accordingly are subject to special considerations and significant risks not typically associated with investments in equity securities of the United States of America and Western European companies. These include risks associated with, among others, the oil and gas industry, the political, economic and legal environments, influence of the national authorities over price setting and competition in the industry.

(e) Customer risk

A substantial portion of the oil and gas sales of the Group is made to a small number of customers on an open account basis.

	2000	**2001**	**2002**
	RMB'000	**RMB'000**	**RMB'000**
China Petroleum & Chemical Corporation	6,325,061	6,282,532	6,890,877
PetroChina Company Limited	1,458,429	1,320,587	1,187,571
Castle Peak Power Company Limited	1,199,090	1,205,649	1,247,639

36. ADDITIONAL FINANCIAL INFORMATION

As of December 31, 2002, net current assets and total assets less current liabilities of the Group amounted to approximately RMB 17,352,044,000 and RMB 53,961,241,000 (2001: RMB 15,638,483,000 and RMB 39,927,972,000), respectively.

37. SUBSEQUENT EVENTS

(i) Material acquisition

Subsequent to the year end, on March 7, 2003, the Company entered into an agreement with BG International Limited ("BG"), a wholly-owned subsidiary of BG Group, to acquire from BG a 1/12th (8.33%) interest in the North Caspian Sea Project (the "Project") in Kazakhstan for US$615 million (subject to certain adjustments). The partners of the Project include ENI-Agip (operator), BG Group, ConocoPhillips, ExxonMobil, INPEX, Shell and TotalFinaElf. Completion of the acquisition is subject to a number of conditions including the wavier of certain preemption rights and receipt of governmental approvals.

(All amounts expressed in Renminbi unless otherwise stated)

37. SUBSEQUENT EVENTS (CONT'D)

(ii) Share Options

On February 24, 2003, the board of directors approved to grant options in respect of 8,410,000 shares to the Company's senior management under the share option scheme approved in June 2002. The exercise price for the options is HK$10.54 per share. Options granted under this scheme may be exercised, in whole or in part, in accordance with the following vesting schedule:

— one-third of the shares underlying the options shall vest on the first anniversary of the date of the grant;

— one-third of the shares underlying to the options shall vest on the second anniversary of the date of the grant; and

— one-third of the shares underlying the options shall vest on the third anniversary of the date of the grant.

(iii) Dividends

On March 27, 2003, the board of directors proposed a final dividend of HK$0.15 per share, totaling HK$1,232,124,848 (equivalent of RMB 1,307,407,676) and a special dividend of HK$0.15 per share, totaling HK$1,232,124,848 (equivalent to RMB 1,307,407,676) to its shareholders for the year ended December 31, 2002. The proposed dividend distribution is subject to shareholders approval in their forth coming annual general meeting.

38. SIGNIFICANT DIFFERENCES BETWEEN HONG KONG GAAP AND US GAAP

The accounting policies adopted by the Group conform to Hong Kong GAAP, which differ in certain respects from generally accepted accounting principles in the United States of America ("US GAAP").

(a) Net profit and net equity

(i) Revaluation of land and buildings

The Group revalued certain land and buildings on August 31, 1999 and December 31, 2000 and the related revaluation surplus was recorded on the respective dates. Under Hong Kong GAAP, revaluation of property, plant and equipment is permitted and depreciation, depletion and amortisation is based on the revalued amount. Additional depreciation arising from the revaluation for the year ended December 31, 2002 was approximately RMB 9,156,000 (2001: RMB 9,156,000). Under US GAAP, property, plant and equipment is required to be stated at cost. Accordingly, no additional depreciation, depletion and amortisation from the revaluation is recognised under US GAAP.

(All amounts expressed in Renminbi unless otherwise stated)

38. SIGNIFICANT DIFFERENCES BETWEEN HONG KONG GAAP AND US GAAP (CONT'D)

(a) Net profit and net equity (cont'd)

(ii) Short-term investments

According to Hong Kong GAAP, available-for-sale investments in marketable securities are measured at fair value and related unrealised holding gains and losses are included in current period earnings. According to US GAAP, such investments are also measured at fair value and classified in accordance with Statement of Financial Accounting Standards ("SFAS") No.115. Under US GAAP, related unrealised gains and losses on available-for-sale securities are excluded from current period earnings and included in other comprehensive income.

(iii) Impairment of long-lived assets

Under Hong Kong GAAP, impairment charges are recognised when a long-lived asset's carrying amount exceeds the higher of an asset's net selling price and value in use, which incorporates discounting the asset's estimated future cash flows.

Under US GAAP, long-lived assets are assessed for possible impairment in accordance with SFAS No.144, "Accounting for the impairment or disposal of long-lived assets." SFAS No. 144 was issued in August 2001 and is effective for fiscal years beginning after December 15, 2001. SFAS No. 144 retains the requirements of SFAS No. 121 to (a) recognise an impairment loss only if the carrying amount of a long-lived asset is not recoverable from its undiscounted cash flows and (b) measure an impairment loss as the difference between the carrying amount and fair value of the asset. SFAS No. 144 requires that a long-lived asset to be abandoned, exchanged for a similar productive asset, or distributed to owners in a spin-off be considered held and used until it is disposed of.

SFAS 144 requires the Group to assess the need for an impairment of capitalised costs of proved oil and gas properties and the costs of wells and related equipment and facilities on a property-by-property basis. If an impairment is indicated based on undiscounted expected future cash flows, then an impairment is recognised to the extent that net capitalised costs exceed the estimated fair value of the property. Fair value of the property is estimated by the Group using the present value of future cash flows. The impairment was determined based on the difference between the carrying value of the assets and the present value of future cash flows. It is reasonably possible that a change in reserve or price estimates could occur in the near term and adversely impact management's estimate of future cash flows and consequently the carrying value of properties.

For the year ended December 31, 2002, there were no impairment losses recognised under Hong Kong GAAP and US GAAP.

(All amounts expressed in Renminbi unless otherwise stated)

38. SIGNIFICANT DIFFERENCES BETWEEN HONG KONG GAAP AND US GAAP (CONT'D)

(a) Net profit and net equity (cont'd)

(iv) Stock compensation plans

As described in Note 29 to the financial statements, as of December 31, 2002, the Group had two stock option plans. The Group applies Accounting Principles Board Opinion 25 and related Interpretations in accounting for these stock option plans. Accordingly, compensation costs that have been recognised for the stock option plans were RMB 5,631,500 for the year ended December 31, 2002 (2001: RMB 2,755,000). Had compensation costs for the Group's stock option plans been determined based on the fair value at the grant dates for awards under the plans consistent with the method of SFAS No. 123, the Group's net income and earnings per share for the year ended December 31, 2002 would have been reduced to the pro forma amounts indicated below:

	Pro forma		**As reported**
	2001	**2002**	**2002**
	RMB'000	**RMB'000**	**RMB'000**
Net income	7,912,150	9,085,917	9,088,371
Earnings per share			
- Basic	RMB1.00	RMB1.11	RMB1.11
- diluted	RMB1.00	RMB1.11	RMB1.11

Weighted average fair value of the options at the grant dates for awards under the plans was RMB 3.10 per share which was estimated using the Black-Scholes model with the following assumptions: dividend yield of 2.0%, an expected life of five years; expected volatility of 44%; and risk-free interest rates of 5.25%. Weighted average exercise price of the stock options was HK$6.09 per share.

(v) Provision for dismantlement

HK GAAP require the provision of dismantlement to be recorded for a present obligation whether that obligation is legal or constructive. The associated cost is capitalised and the liability is discounted and accretion expense is recognised using the credit-adjusted risk-free interest rate in effect when the liability is initially recognised. However, under US GAAP, the provisions for dismantlement are provided on a unit-of-production basis over field lives, there is no corresponding tangible fixed asset.

(All amounts expressed in Renminbi unless otherwise stated)

38. SIGNIFICANT DIFFERENCES BETWEEN HONG KONG GAAP AND US GAAP (CONT'D)

(a) Net profit and net equity (cont'd)

(v) Provision for dismantlement (cont'd)

The impact on the consolidated balance sheet as of December 31, 2002 is summarised below:

Increase (Decrease) in caption heading	**December 31, 2002**
	RMB'000
Property, plant and equipment, net	(863,093)
Provision for dismantlement	(240,077)
Deferred tax liabilities	(186,904)
Reserves	(436,112)

Effects on net profit and net equity of differences between Hong Kong GAAP and US GAAP are summarised below:

	Net profit		
	2000	**2001**	**2002**
	RMB'000	**RMB'000**	**RMB'000**
As reported under Hong Kong GAAP	10,296,600	7,957,631	9,232,827
Impact of US GAAP adjustments:			
- Reversal of additional depreciation, depletion and amortisation arising from the revaluation surplus on land and buildings	5,687	9,156	9,156
- Unrealised holding gains from available-for-sale marketable securities	—	(43,796)	(36,965)
- Realised holding gains from available-for-sale marketable securities	—	—	26,940
- Additional dismantlement based on unit-of-production method	—	—	(197,079)
- Impact of income tax	—	—	59,124
- Recognition of stock compensation cost	—	(2,755)	(5,632)
As restated under US GAAP	10,302,287	7,920,236	9,088,371
Net income per share under US GAAP			
- Basic	RMB1.63	RMB1.00	RMB1.11
- Diluted	RMB1.63	RMB1.00	RMB1.11

(All amounts expressed in Renminbi unless otherwise stated)

38. SIGNIFICANT DIFFERENCES BETWEEN HONG KONG GAAP AND US GAAP (CONT'D)

(a) Net profit and net equity (cont'd)

	Net equity	
	2001	**2002**
	RMB'000	**RMB'000**
As reported under Hong Kong GAAP	33,310,506	40,568,488
Impact of US GAAP adjustments:		
- Reversal of revaluation surplus on land and buildings	(274,671)	(274,671)
- Reversal of additional accumulated depreciation, depletion and amortisation charges arising from the revaluation surplus on land and buildings	16,739	25,895
- Cumulative adjustment for provision for dismantlement	—	(436,112)
As restated under US GAAP	33,052,574	39,883,600

There are no significant GAAP differences that affect classifications within the balance sheet or income statement but do not affect net income or shareholders' equity.

(b) Comprehensive income

According to SFAS No. 130, it is required to include a statement of other comprehensive income for revenues and expenses, gains and losses that under US GAAP are included in comprehensive income and excluded from net income.

	2000	**2001**	**2002**
	RMB'000	**RMB'000**	**RMB'000**
Net income under US GAAP	10,302,287	7,920,236	9,088,371
Other comprehensive income:			
Foreign currency translation adjustments	(6,350)	702	(7,948)
Unrealised gains on short-term investments	—	43,796	36,965
Less: reclassification adjustment for realised gains included in net income	—	—	(26,940)
Comprehensive income under US GAAP	10,295,937	7,964,734	9,090,448

(All amounts expressed in Renminbi unless otherwise stated)

38. SIGNIFICANT DIFFERENCES BETWEEN HONG KONG GAAP AND US GAAP (CONT'D)

(b) Comprehensive income (cont'd)

Roll forward of accumulated other comprehensive income components are as follows:

	Foreign currency translation adjustments	Unrealised gains on short-term investments	Accumulated other comprehensive income
	RMB'000	RMB'000	RMB'000
Balance at January 1, 2001	(6,350)	—	(6,350)
Current year change	702	43,796	44,498
Balance at January 1, 2002	(5,648)	43,796	38,148
Reversal of current year realised gains	—	(26,940)	(26,940)
Current year change	(7,948)	36,965	29,017
Balance at December 31, 2002	(13,596)	53,821	40,225

(c) Derivative instruments

The Group had a currency swap contract with a financial institution to sell United States dollars in exchange for Japanese Yen in order to hedge certain Japanese Yen denominated loan repayments in the future. In accordance with SFAS No. 133, the derivative contract was recorded as "other current liabilities" in the consolidated balance sheet at fair value. For the year ended December 31, 2002, the Group recognised related changes in fair value, a gain of RMB 14,485,000 (2001: RMB 29,134,000), and included the amount in "exchange (loss)/gain, net" in the consolidated income statement.

(d) Accounting for asset retirement obligations

On August 15, 2001, SFAS No. 143 "Accounting for asset retirement obligation" ("SFAS No. 143") was released and will be effective for the fiscal years beginning after June 15, 2002. The Statement requires that the fair value of a liability for an asset retirement obligation be recognised in the period in which it is incurred if a reasonable estimate of fair value can be made. The associated asset retirement costs are capitalised as part of the carrying amount of the long-lived assets. Further, under the Statement, the liability is discounted and accretion expense is recognised using the credit-adjusted risk-free interest rate in effect when the liability was initially recognised.

Adoption of the statement will likely result in increase in both costs of assets and total liabilities. The Group is currently assessing these matters and has not yet determined whether or the extent to which they will affect the financial statements.

38. SIGNIFICANT DIFFERENCES BETWEEN HONG KONG GAAP AND US GAAP (CONT'D)

(e) Use of estimates in the preparation of financial statements

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. The most significant estimates pertain to proved oil and gas reserve volumes and the future development, provision for dismantlement as well as estimates relating to certain oil and gas revenues and expenses. Actual amounts could differ from those estimates and assumptions.

(f) Deferred income taxes

Under Hong Kong GAAP, the Group provides deferred taxes for timing differences only to the extent that it is probable a liability or asset will crystallise in the foreseeable future. US GAAP requires full provision for deferred taxes under the asset and liability method on all temporary differences. In August 2002, a revised accounting standard SSAP 12 "Income Taxes" was issued in Hong Kong. The revised standard is effective for accounting periods beginning on or after January 1, 2003 and requires full provision for deferred taxes similar to US GAAP.

For Hong Kong GAAP purposes, deferred taxes are provided using the liability method whereby it is calculated using tax rates estimated to be applicable when timing differences reverse.

For US GAAP purposes, deferred tax assets and liabilities are recognised for the expected future tax consequences of existing differences between financial reporting and tax reporting bases of assets and liabilities, and loss or tax credit carry forwards using enacted tax rates expected to be in effect when these differences are realised. Valuation allowances are recorded for deferred tax assets for which it is more likely than not that such assets will be realised.

For the year ended December 31, 2002, there was no difference on the amounts of deferred income taxes recognised under Hong Kong GAAP and US GAAP.

(g) Segment reporting

The Group's segment information is based on the segmental operating results regularly reviewed by the Group's chief operating decision maker. The accounting policies used are the same as those used in the preparation of the Group's consolidated Hong Kong GAAP financial statements.

(All amounts expressed in Renminbi unless otherwise stated)

The following disclosures are included in accordance with the United States Statements of Financial Accounting Standards No. 69, "Disclosures about Oil and Gas Producing Activities."

(a) Reserve quantity information

Crude oil and natural gas reserve estimates are determined through analysis of geological and engineering data which appear, with reasonable certainty, to be recoverable at commercial rates in the future from known oil and natural gas reservoirs under existing economic and operating conditions.

Estimates of crude oil and natural gas reserve have been made by independent engineers. The Group's net proved reserves consist of its percentage interest in reserves, comprised of a 100% interest in its independent oil and gas properties and its participating interest in the properties covered under the production sharing contracts in PRC, less (a) an adjustment for the Group's share of royalties payable by the Group to the PRC government and the Group's participating interest in share oil payable to the PRC government under the production sharing contracts, and less (b) an adjustment for production allocable to foreign partners under the PRC production sharing contracts as reimbursement for exploration expenses attributable to the Group's participating interest, plus its participating interest in the properties covered under the production sharing contracts in Indonesia less an adjustment of share oil attributable to Indonesian government and the domestic market obligation.

The proved developed and undeveloped reserves for Indonesia in 2000 and 2001 were less than 1% to the total and no separate disclosure was presented.

Proved developed and undeveloped reserves (net of royalties and government share oil):

	PRC		Indonesia		Total	
	Oil (Mmbbls)	Natural gas (Bcf)	Oil (Mmbbls)	Natural gas (Bcf)	Oil (Mmbbls)	Natural gas (Bcf)
December 31, 1999	1,242	3,332	—	—	1,242	3,332
Discoveries and extensions	76	5	—	—	76	5
Sales of reserves	(41)	—	—	—	(41)	—
Production	(75)	(72)	—	—	(75)	(72)
Revisions of prior estimates	14	(15)	—	—	14	(15)
December 31, 2000	1,216	3,250	—	—	1,216	3,250
Discoveries and extensions	199	166	—	—	199	166
Production	(84)	(71)	—	—	(84)	(71)
Revisions of prior estimates	(52)	(97)	—	—	(52)	(97)
December 31, 2001	1,279	3,248	—	—	1,279	3,248
Purchase of reserves	—	—	143	241	143	241
Discoveries and extensions	150	169	—	—	150	169
Production	(96)	(79)	(13)	(26)	(109)	(105)
Revisions of prior estimates	(46)	(5)	8	—	(38)	(5)
December 31, 2002	1,287	3,333	138	215	1,425	3,548

(All amounts expressed in Renminbi unless otherwise stated)

(a) Reserve quantity information (cont'd)

Proved developed reserves:

	PRC		Indonesia		Total	
	Oil (Mmbbls)	Natural gas (Bcf)	Oil (Mmbbls)	Natural gas (Bcf)	Oil (Mmbbls)	Natural gas (Bcf)
December 31, 2000	546	558	—	—	546	558
December 31, 2001	582	765	—	—	582	765
December 31, 2002	542	724	115	101	657	825

(b) Results of operations

	2000	2001	2002		
	PRC	PRC	PRC	Indonesia	Total
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
Net sales to customers	18,819,323	17,560,788	20,280,746	3,498,548	23,779,294
Operating expenses	(2,124,078)	(2,329,130)	(2,440,210)	(1,335,124)	(3,775,334)
Production taxes	(1,036,729)	(883,768)	(1,023,049)	—	(1,023,049)
Exploration	(552,869)	(1,039,297)	(1,286,670)	(31,653)	(1,318,323)
Depreciation, depletion and amortisation	(2,577,882)	(2,566,920)	(3,121,381)	(898,151)	(4,019,532)
	12,527,765	10,741,673	12,409,436	1,233,620	13,643,056
Income tax expenses	(2,265,847)	(3,992,578)	(3,816,008)	(592,138)	(4,408,146)
Result of operations	10,261,918	6,749,095	8,593,428	641,482	9,234,910

(c) Capitalised costs

	2000	2001	2002		
	PRC	PRC	PRC	Indonesia	Total
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
Proved oil and gas properties	36,323,472	40,748,848	46,426,684	9,605,744	56,032,428
Unproved oil and gas properties	996,452	428,611	521,880	—	521,880
Accumulated depreciation, depletion and amortisation	(15,482,082)	(18,154,653)	(21,161,905)	(993,316)	(22,155,221)
Net capitalised costs	21,837,842	23,022,806	25,786,659	8,612,428	34,399,087

(All amounts expressed in Renminbi unless otherwise stated)

(d) Costs incurred

	2000	2001	2002		
	PRC	PRC	PRC	Indonesia	Total
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
Acquisition costs	—	—	—	4,735,826	4,735,826
Exploration costs	610,159	996,121	1,519,683	32,405	1,552,088
Development cost	4,176,555	3,958,357	5,458,199	750,532	6,208,731
Total costs incurred	4,786,714	4,954,478	6,977,882	5,518,763	12,496,645

(e) Standardised measure of discounted future net cash flows and changes therein

In calculating the standardised measure of discounted future net cash flows, year-end constant price and cost assumptions were applied to the Group's estimated annual future production from proven reserves to determine future cash inflows. Year end average realised oil prices used in the estimation of proved reserves and calculation of the standardised measure were US$28 as of December 31, 2002 (2001: US$17; 2000: US$22). Future development costs are estimated based upon constant price assumptions and assume the continuation of existing economic, operating and regulatory conditions. Future income taxes are calculated by applying the year-end statutory rate to estimate future pre-tax cash flows after provision for the tax cost of the oil and natural gas properties based upon existing laws and regulations. The discount was computed by application of a 10% discount factor to the estimated future net cash flows.

(All amounts expressed in Renminbi unless otherwise stated)

(e) Standardised measure of discounted future net cash flows and changes therein (cont'd)

Management believes that this information does not represent the fair market value of the oil and natural gas reserves or the present value of estimated cash flows since no economic value is attributed to potential reserves, the use of a 10% discount rate is arbitrary, and prices change constantly from year-end levels.

Present value of estimated future net cash flows:

		2000	2001	2002		
	Notes	**PRC**	**PRC**	**PRC**	**Indonesia**	**Total**
		RMB'000	**RMB'000**	**RMB'000**	**RMB'000**	**RMB'000**
Future cash inflows	(1)	326,513,363	261,339,180	389,025,791	37,242,644	426,268,435
Future production costs		(73,402,341)	(74,404,378)	(89,657,677)	(22,386,603)	(112,044,280)
Future development costs	(2)	(31,279,348)	(38,640,756)	(44,699,729)	(5,381,081)	(50,080,810)
Future income taxes		(30,833,803)	(39,097,483)	(73,757,925)	(4,301,926)	(78,059,851)
Future net cash flows		190,997,871	109,196,563	180,910,460	5,173,034	186,083,494
10% discount factor	(3)	(97,607,274)	(58,114,105)	(84,478,856)	(1,463,589)	(85,942,445)
Standardised measure		93,390,597	51,082,458	96,431,604	3,709,445	100,141,049

(1) Future cash flows consist of the Group's 100% interest in the independent oil and gas properties and the Group's participating interest in the properties under production sharing contracts in PRC less (a) an adjustment for the royalties payable to the PRC government and share oil payable to the PRC under production sharing contracts and (b) an adjustment for production allocable to foreign partners under the PRC production sharing contracts for exploration costs attributable to the Group's participating interest, plus its participating interest in the properties covered under the production sharing contracts in Indonesia less an adjustment of share oil attributable to Indonesian government and the domestic market obligation.

(2) Future development costs include the estimated costs of drilling future development wells and building the production platforms.

(3) Future net cash flows have been prepared taking into consideration estimated future dismantlement costs of dismantling offshore oil platforms and gas properties.

(All amounts expressed in Renminbi unless otherwise stated)

(e) Standardised measure of discounted future net cash flows and changes therein (cont'd)

Changes in the standardised measure of discounted future net cash flows:

	2000	2001	2002
Standardised measure, beginning of year	87,722,457	93,390,597	51,082,458
Sales of production, net of royalties and production costs	(15,658,516)	(14,347,890)	(18,980,911)
Net change in prices, net of royalties and production costs	578,121	(32,289,445)	58,471,355
Extensions discoveries and improved recovery, net of related future costs	5,417,977	9,985,707	14,603,893
Change in estimated future development costs	3,433,517	(9,651,681)	(13,947,849)
Development costs incurred during the year	4,176,555	3,958,357	6,208,731
Revisions in quantity estimates	830,236	(3,272,326)	(3,301,510)
Accretion of discount	10,361,478	10,846,714	6,873,378
Net change in income taxes	815,779	(3,241,861)	(23,296,206)
Purchase of properties	—	—	15,899,375
Sales of property	(2,865,132)	—	—
Changes in timing and other	(1,421,875)	(4,295,714)	6,528,335
Standardised measure, end of year	93,390,597	51,082,458	100,141,049

SUMMARY REPORT OF RYDER SCOTT COMPANY, L.P.

RYDER SCOTT COMPANY
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April 8, 2003

CNOOC Limited
No. 6, Dongzhimenwai Xiaojie
Beijing, China 100027

Gentlemen:

At your request, we have prepared an estimate of the reserves, future production, and income attributable to certain interests of CNOOC Limited (CNOOC) as of December 31, 2002. The subject properties are located in China and Indonesia. The income data were estimated using the Securities and Exchange Commission (SEC) guidelines for future price and cost parameters.

The estimated reserves and future income amounts presented in this report are related to hydrocarbon prices. Hydrocarbon prices on December 31, 2002 were used in the preparation of this report as required by SEC guidelines; however, actual future prices may vary significantly from December 31, 2002 prices. Therefore, volumes of reserves actually recovered and amounts of income actually received may differ significantly from the estimated quantities presented in this report. The results of this study are summarized below.

SEC PARAMETERS
Estimated Net Reserves and Income
Attributable to Certain Interests of
CNOOC Limited
As of December 31, 2002

	Proved			
	Developed			Total
	Producing	Non-Producing	Undeveloped	Proved
Net Remaining Reserves				
Oil/Condensate – Barrels	621,204,098	33,484,525	764,612,781	1,419,301,404
Plant Products – Barrels	2,010,962	20,634	3,109,786	5,141,382
Gas – MMCF	778,355	46,834	2,722,692	3,547,881
Income Data – M$				
Future Gross Revenue	$19,462,417	$1,106,181	$28,587,655	$49,156,253
Deductions	6,530,649	343,028	10,370,800	17,244,477
Future Net Income (FNI)	$12,931,768	$ 763,153	$18,216,855	$31,911,776
Discounted FNI @ 10%	$ 8,893,631	$ 503,433	$ 7,613,030	$17,010,094

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Liquid hydrocarbons are expressed in standard 42 gallon barrels. All gas volumes are sales gas expressed in millions of cubic feet (MMCF) at the official temperature and pressure base of the area in which the gas reserves are located.

The future gross revenue is after royalty and government share of oil. The deductions are comprised of the normal direct costs of operating the wells, recompletion costs, development costs, and certain abandonment costs net of salvage. The future net income is before the deduction of government income taxes and general administrative overhead, and has not been adjusted for outstanding loans that may exist nor does it include any adjustment for cash on hand or undistributed income. Liquid hydrocarbon reserves account for approximately 79 percent and gas reserves account for the remaining 21 percent of total future gross revenue from proved reserves.

The discounted future net income shown above was calculated using a discount rate of 10 percent per annum compounded monthly. Future net income was discounted at four other discount rates which were also compounded monthly. These results are shown on each estimated projection of future production and income presented in a later section of this report and in summary form below.

	Discounted Future Net Income – M$ As of December 31, 2002
Discount Rate Percent	Total Proved
7	$20,147,415
8	$19,010,815
9	$17,968,300
11	$16,127,610

The results shown above are presented for your information and should not be construed as our estimate of fair market value.

CNOOC has interests in properties that are controlled by terms of Production Sharing Contracts (PSCs). A certain number of properties in domestic China and all of the properties in Indonesia are controlled by PSCs, and the net entitlement reserves in these properties were estimated using the economic interest based analysis. Ryder Scott has identified the PSC and non-PSC controlled properties and summarized the results in the following set of tables.

CNOOC Limited
Non-PSC Controlled Properties

	Proved			
	Developed			Total
	Producing	Non-Producing	Undeveloped	Proved
Net Remaining Reserves				
Oil/Condensate – Barrels	341,131,436	6,182,125	281,402,464	628,716,025
Plant Products – Barrels	0	0	0	0
Gas – MMCF	198,398	43,272	2,416,068	2,657,738
Income Data – M$				
Future Gross Revenue	$9,581,735	$278,410	$14,584,073	$24,444,218
Deductions	2,325,018	87,936	5,549,831	7,962,785
Future Net Income (FNI)	$7,256,717	$190,474	$ 9,034,242	$16,481,433
Discounted FNI @ 10%	$4,772,015	$ 91,334	$ 3,164,669	$ 8,028,018

CNOOC Limited
PSC Controlled Properties

	Proved			
	Developed			Total
	Producing	Non-Producing	Undeveloped	Proved
Net Remaining Reserves				
Oil/Condensate – Barrels	280,072,662	27,302,400	483,210,317	790,585,379
Plant Products – Barrels	2,010,962	20,634	3,109,786	5,141,382
Gas – MMCF	579,957	3,562	306,624	890,143
Income Data – M$				
Future Gross Revenue	$9,880,681	$827,771	$14,003,582	$24,712,034
Deductions	4,205,631	255,093	4,820,969	9,281,693
Future Net Income (FNI)	$5,675,050	$572,678	$ 9,182,613	$15,430,341
Discounted FNI @ 10%	$4,121,616	$412,099	$ 4,448,361	$ 8,982,076

Reserves Included in This Report

The proved reserves included herein conform to the definition as set forth in the Securities and Exchange Commission's Regulation S-X Part 210.4-10 (a) as clarified by subsequent Commission Staff Accounting Bulletins. The definitions of proved reserves are included in the attached "Petroleum Reserves Definitions" in this report.

Because of the direct relationship between volumes of proved undeveloped reserves and development plans, we include in the proved undeveloped category only reserves assigned to undeveloped locations that we have been assured will definitely be drilled, and reserves assigned to the undeveloped portions of secondary or tertiary projects which we have been assured will definitely be developed.

The proved developed non-producing reserves included herein are comprised of shut–in and behind pipe categories. The various reserve status categories are defined in the attached "Petroleum Reserves Definitions" in this report.

Estimates of Reserves

In general, the reserves included herein were estimated by performance methods or the volumetric method; however, other methods were used in certain cases where characteristics of the data indicated that such other methods were more appropriate in our opinion. The reserves estimated by the performance method utilized extrapolations of various historical data in those cases where such data were definitive in our opinion. Reserves were estimated by the volumetric method in those cases where there were inadequate historical performance data to establish a definitive trend or where the use of production performance data as a basis for the reserve estimates was considered to be inappropriate.

The reserves included in this report are estimates only and should not be construed as being exact quantities. They may or may not be actually recovered, and if recovered, the revenues therefrom and the actual costs related thereto could be more or less than the estimated amounts. Moreover, estimates of reserves may increase or decrease as a result of future operations.

Future Production Rates

Initial production rates are based on the current producing rates for those wells now on production. Test data and other related information were used to estimate the anticipated initial production rates for those wells or locations which are not currently producing. If no production decline trend has been established, future production rates were held constant, or adjusted for the effects of curtailment where appropriate, until a decline in ability to produce was anticipated. An estimated rate of decline was then applied to depletion of the reserves. If a decline trend has been established, this trend was used as the basis for estimating future production rates. For reserves not yet on production, sales were estimated to commence at an anticipated date furnished by CNOOC.

The future production rates from wells now on production may be more or less than estimated because of changes in market demand or allowables set by regulatory bodies. Wells or locations which are not currently producing may start producing earlier or later than anticipated in our estimates of their future production rates.

Hydrocarbon Prices

CNOOC furnished us with hydrocarbon prices in effect at December 31, 2002 and with its forecasts of future prices which take into account SEC and Financial Accounting Standards Board (FASB) rules, current market prices, contract prices, and fixed and determinable price escalations where applicable.

In accordance with FASB Statement No. 69, December 31, 2002 market prices were determined using the daily oil price or daily gas sales price ("spot price") adjusted for oilfield or gas gathering hub and wellhead price differences (e.g. grade, transportation, gravity, sulfur and BS&W) as appropriate. Also in accordance with SEC and FASB specifications, changes in market prices subsequent to December 31, 2002 were not considered in this report.

For hydrocarbon products sold under contract, the contract price including fixed and determinable escalations, exclusive of inflation adjustments, was used until expiration of the contract. Upon contract expiration, the price was adjusted to the current market price for the area and held at this adjusted price to depletion of the reserves.

The effects of derivative instruments designated as price hedges of oil and gas quantities are generally not reflected in our individual property evaluations.

Costs

Operating costs for the leases and wells in this report are based on the operating expense reports of CNOOC and include only those costs directly applicable to the contract areas or wells. When applicable, the operating costs include a portion of general and administrative costs allocated directly to the properties under terms of operating agreements. No deduction was made for indirect costs such as general administration and overhead expenses, loan repayments, interest expenses, and exploration and development prepayments that are not charged directly to the contract areas or wells.

Development costs were furnished to us by CNOOC and are based on authorizations for expenditure for the proposed work or actual costs for similar projects. The estimated net cost of abandonment after salvage was included for properties where abandonment costs net of salvage are significant. The estimates of the net abandonment costs furnished by CNOOC were accepted without independent verification.

Current costs were held constant throughout the life of the properties.

General

Table A presents a one line summary of proved reserve and income data for each of the subject properties which are ranked according to their future net income discounted at 10 percent per year. Table B presents a one line summary of gross and net reserves and income data for each of the subject properties. Table C presents a one line summary of initial basic data for each of the subject properties. Tables 1 through 1,800 present our estimated projection of production and income by years beginning January 1, 2003, by regional group, contract area, field, and well.

While it may reasonably be anticipated that the future prices received for the sale of production and the operating costs and other costs relating to such production may also increase or decrease from existing levels, such changes were, in accordance with rules adopted by the SEC, omitted from consideration in making this evaluation.

The estimates of reserves presented herein were based upon a detailed study of the properties in which CNOOC owns an interest; however, we have not made any field examination of the properties. No consideration was given in this report to potential environmental liabilities which may exist nor were any costs included for potential liability to restore and clean up damages, if any, caused by past operating practices. CNOOC has informed us that they have furnished us all of the accounts, records, geological and engineering data, and reports and other data required for this investigation. The ownership interests, prices, and other factual data furnished by CNOOC were accepted without independent verification. The estimates presented in this report are based on data available through December 31, 2002.

Neither we nor any of our employees have any interest in the subject properties, and neither the employment to make this study nor the compensation is contingent on our estimates of reserves and future income for the subject properties.

CNOOC has assured us of their intent and ability to proceed with the development activities included in this report, and that they are not aware of any legal, regulatory or political obstacles that would significantly alter their plans.

This report was prepared for the exclusive use and sole benefit of CNOOC Limited. The data, work papers, and maps used in this report are available for examination by authorized parties in our offices. Please contact us if we can be of further service.

Very truly yours,

RYDER SCOTT COMPANY, L.P.

Harris Ghozali
Petroleum Engineer–International

HG/sw

Reviewed by:

Guale Ramirez, P.E.
Managing Senior Vice President–International

PETROLEUM RESERVES DEFINITIONS

SECURITIES AND EXCHANGE COMMISSION

INTRODUCTION

Reserves are those quantities of petroleum which are anticipated to be commercially recovered from known accumulations from a given date forward. All reserve estimates involve some degree of uncertainty. The uncertainty depends chiefly on the amount of reliable geologic and engineering data available at the time of the estimate and the interpretation of these data. The relative degree of uncertainty may be conveyed by placing reserves into one of two principal classifications, either proved or unproved. Unproved reserves are less certain to be recovered than proved reserves and may be further sub-classified as probable and possible reserves to denote progressively increasing uncertainty in their recoverability. It should be noted that Securities and Exchange Commission Regulation S-K prohibits the disclosure of estimated quantities of probable or possible reserves of oil and gas and any estimated value thereof in any documents publicly filed with the Commission.

Reserves estimates will generally be revised as additional geologic or engineering data become available or as economic conditions change. Reserves do not include quantities of petroleum being held in inventory, and may be reduced for usage or processing losses if required for financial reporting.

Reserves may be attributed to either natural energy or improved recovery methods. Improved recovery methods include all methods for supplementing natural energy or altering natural forces in the reservoir to increase ultimate recovery. Examples of such methods are pressure maintenance, cycling, waterflooding, thermal methods, chemical flooding, and the use of miscible and immiscible displacement fluids. Other improved recovery methods may be developed in the future as petroleum technology continues to evolve.

PROVED RESERVES (SEC DEFINITIONS)

Securities and Exchange Commission Regulation S-X Rule 4-10 paragraph (a) defines proved reserves as follows:

Proved oil and gas reserves*. Proved oil and gas reserves are the estimated quantities of crude oil, natural gas, and natural gas liquids which geological and engineering data demonstrate with reasonable certainty to be recoverable in future years from known reservoirs under existing economic and operating conditions, i.e., prices and costs as of the date the estimate is made. Prices include consideration of changes in existing prices provided only by contractual arrangements, but not on escalations based upon future conditions.*

(i) Reservoirs are considered proved if economic producibility is supported by either actual production or conclusive formation test. The area of a reservoir considered proved includes:

(A) that portion delineated by drilling and defined by gas-oil and/or oil-water contacts, if any; and

(B) the immediately adjoining portions not yet drilled, but which can be reasonably judged as economically productive on the basis of available geological and engineering data. In the absence of information on fluid contacts, the lowest known structural occurrence of hydrocarbons controls the lower proved limit of the reservoir.

(ii) Reserves which can be produced economically through application of improved recovery techniques (such as fluid injection) are included in the "proved" classification when successful testing by a pilot project, or the operation of an installed program in the reservoir, provides support for the engineering analysis on which the project or program was based.

(iii) Estimates of proved reserves do not include the following:

(A) oil that may become available from known reservoirs but is classified separately as "indicated additional reserves";

(B) crude oil, natural gas, and natural gas liquids, the recovery of which is subject to reasonable doubt because of uncertainty as to geology, reservoir characteristics, or economic factors;

(C) crude oil, natural gas, and natural gas liquids, that may occur in undrilled prospects; and

(D) crude oil, natural gas, and natural gas liquids, that may be recovered from oil shales, coal, gilsonite and other such sources.

***Proved developed oil and gas reserves**. Proved developed oil and gas reserves are reserves that can be expected to be recovered through existing wells with existing equipment and operating methods. Additional oil and gas expected to be obtained through the application of fluid injection or other improved recovery techniques for supplementing the natural forces and mechanisms of primary recovery should be included as "proved developed reserves" only after testing by a pilot project or after the operation of an installed program has confirmed through production response that increased recovery will be achieved.*

***Proved undeveloped reserves**. Proved undeveloped oil and gas reserves are reserves that are expected to be recovered from new wells on undrilled acreage, or from existing wells where a relatively major expenditure is required for recompletion. Reserves on undrilled acreage shall be limited to those drilling units offsetting productive units that are reasonably certain of production when drilled. Proved reserves for other undrilled units can be claimed only where it can be demonstrated with certainty that there is continuity of production from the existing productive formation. Under no circumstances should estimates for proved undeveloped reserves be attributable to any acreage for which an application of fluid injection or other improved recovery technique is contemplated, unless such techniques have been proved effective by actual tests in the area and in the same reservoir.*

Certain Staff Accounting Bulletins published subsequent to the promulgation of Regulation S-X have dealt with matters relating to the application of financial accounting and disclosure rules for oil and gas producing activities. In particular, the following interpretations extracted from Staff Accounting Bulletins set forth the Commission staff's view on specific questions pertaining to proved oil and gas reserves.

Economic producibility of estimated proved reserves can be supported to the satisfaction of the Office of Engineering if geological and engineering data demonstrate with reasonable certainty that those reserves can be recovered in future years under existing economic and operating conditions. The relative importance of the many pieces of geological and engineering data which should be evaluated when classifying reserves cannot be identified in advance. In certain instances, proved reserves may be assigned to reservoirs on the basis of a combination of electrical and other type logs and core analyses which indicate the reservoirs are analogous to similar reservoirs in the same field which are producing or have demonstrated the ability to produce on a formation test. (extracted from SAB-35)

In determining whether "proved undeveloped reserves" encompass acreage on which fluid injection (or other improved recovery technique) is contemplated, is it appropriate to distinguish between (i) fluid injection used for pressure maintenance during the early life of a field and (ii) fluid injection used to effect secondary recovery when a field is in the late stages of depletion? ... The Office of Engineering believes that the distinction identified in the above question may be appropriate in a few limited circumstances, such as in the case of certain fields in the North Sea. The staff will review estimates of proved reserves attributable to fluid injection in the light of the strength of the evidence presented by the registrant in support of a contention that enhanced recovery will be achieved. (extracted from SAB-35)

Companies should report reserves of natural gas liquids which are net to their leasehold interest, i.e., that portion recovered in a processing plant and allocated to the leasehold interest. It may be appropriate in the case of natural gas liquids not clearly attributable to leasehold interests ownership to follow instruction (b) of Item 2(b)(3) of Regulation S-K and report such reserves separately and describe the nature of the ownership. (extracted from SAB-35)

The staff believes that since coalbed methane gas can be recovered from coal in its natural and original location, it should be included in proved reserves, provided that it complies in all other respects with the definition of proved oil and gas reserves as specified in Rule 4-10(a)(2) including the requirement that methane production be economical at current prices, costs, (net of the tax credit) and existing operating conditions. (extracted from SAB-85)

Statements in Staff Accounting Bulletins are not rules or interpretations of the Commission nor are they published as bearing the Commission's official approval; they represent interpretations and practices followed by the Division of Corporation Finance and the Office of the Chief Accountant in administering the disclosure requirements of the Federal securities laws.

SUB-CATEGORIZATION OF DEVELOPED RESERVES (SPE/WPC DEFINITIONS)

In accordance with guidelines adopted by the Society of Petroleum Engineers (SPE) and the World Petroleum Congress (WPC), developed reserves may be sub-categorized as producing or non-producing.

Producing. Reserves sub-categorized as producing are expected to be recovered from completion intervals which are open and producing at the time of the estimate. Improved recovery reserves are considered producing only after the improved recovery project is in operation.

Non-Producing. Reserves sub-categorized as non-producing include shut-in and behind pipe reserves. Shut-in reserves are expected to be recovered from (1) completion intervals which are open at the time of the estimate but which have not started producing, (2) wells which were shut-in awaiting pipeline connections or as a result of a market interruption, or (3) wells not capable of production for mechanical reasons. Behind pipe reserves are expected to be recovered from zones in existing wells, which will require additional completion work or future recompletion prior to the start of production.

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