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山東墨龍石油機械股份有限公司

Shandong Molong Petroleum Machinery Company Limited*

(A Sino-foreign joint stock limited company incorporated in the People's Republic of China with limited liability)

(Stock Code: 568)

INTERIM RESULTS ANNOUNCEMENT FOR THE SIX MONTHS ENDED 30 JUNE 2010

HIGHLIGHTS

- Achieved a revenue of approximately RMB1,318,845,000 for the six months ended 30 June 2010, which represents an increase of approximately 47.11% as compared to RMB896,527,000 in the same period last year.
- The net profit was approximately RMB120,900,000 with a decrease of approximately 13.70% as compared to RMB140,088,000 in the same period last year.
- Earnings per share of the Group were approximately RMB0.37 yuan for the six months ended 30 June 2010.
- The board of directors of the Company does not recommend the payment of an interim dividend for the six months ended 30 June 2010.

The board of directors of Shandong Molong Petroleum Machinery Company Limited (the “Company”) (the “Board”) is pleased to announce the unaudited results of the Company and its subsidiaries (collectively, the “Group”) for the six months ended 30 June 2010 (the “period under review”).

* For identification purpose only

UNAUDITED CONDENSED CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

For the six months ended 30 June 2010

The unaudited results of the Group for the six months ended 30 June 2010 together with the unaudited comparative figures for the corresponding period in 2009 are as follows:

		Six months ended 30 June	
		2010	2009
	Notes	RMB'000	RMB'000
Revenue	(2)	1,318,845	896,527
Cost of sales		<u>(1,120,341)</u>	<u>(695,917)</u>
Gross profit		198,504	200,610
Other income and gains	(3)	33,016	53,518
Distribution expenses		(23,103)	(42,466)
Administrative expenses		(32,382)	(30,417)
Gain on fair value change of foreign currency forward contracts		—	310
Other expenses		(9,862)	(3,137)
Finance costs		(19,551)	(12,637)
Share of results of associate		<u>—</u>	<u>(90)</u>
Profit before taxation	(4)	146,622	165,691
Taxation	(5)	<u>(24,672)</u>	<u>(24,401)</u>
Profit for the period		<u>121,950</u>	<u>141,290</u>
Other comprehensive income:			
Exchange differences arising on translation of foreign operations		<u>6</u>	<u>78</u>
Total comprehensive income for the period		<u>121,956</u>	<u>141,368</u>
Profit for the period attributable to:			
Owners of the Company		120,900	140,088
Non-controlling interests		<u>1,050</u>	<u>1,202</u>
		<u>121,950</u>	<u>141,290</u>
Total comprehensive income attributable to:			
Owners of the Company		120,905	140,101
Non-controlling interests		<u>1,051</u>	<u>1,267</u>
		<u>121,956</u>	<u>141,368</u>
Earnings per share — basic (RMB yuan)	(6)	<u>0.37</u>	<u>0.42</u>

UNAUDITED CONDENSED CONSOLIDATED STATEMENT OF FINANCIAL POSITION

As at 30 June 2010

		As at 30 June 2010 <i>RMB'000</i> (unaudited)	As at 31 December 2009 <i>RMB'000</i> (audited)
	<i>Notes</i>		
NON-CURRENT ASSETS			
Property, plant and equipment		1,505,455	1,307,306
Deposit paid for acquisition of property, plant and equipment		—	1,534
Prepaid lease payments		169,138	150,415
Intangible assets		40,574	35,535
Goodwill		142,973	142,973
Investment in an associate		2,436	2,436
Available-for-sale investment		10,000	10,000
Deferred tax assets		11,210	17,092
Other non-current assets		5,000	—
		<u>1,886,786</u>	<u>1,667,291</u>
CURRENT ASSETS			
Inventories	(7)	791,460	713,655
Trade and other receivables	(8)	853,380	528,195
Bills receivables	(8)	9,761	34,631
Prepaid lease payments		2,126	2,960
Amount due from an associate		—	4,364
Pledged bank deposits		216,013	183,918
Bank balances and cash		65,902	121,592
		<u>1,938,642</u>	<u>1,589,315</u>

		As at 30 June 2010 <i>RMB'000</i> (unaudited)	As at 31 December 2009 <i>RMB'000</i> (audited)
	<i>Notes</i>		
CURRENT LIABILITIES			
Trade and bills payables	(9)	810,946	718,799
Other payables and accrued charges		124,017	96,064
Dividend payable		23,789	39,592
Bank borrowings — due within one year		834,930	467,649
Tax payable		20,720	30,398
		<u>1,814,402</u>	<u>1,352,502</u>
Total current liabilities			
		<u>1,814,402</u>	<u>1,352,502</u>
NET CURRENT ASSETS			
		<u>124,240</u>	<u>236,813</u>
TOTAL ASSETS LESS CURRENT LIABILITIES			
		<u>2,011,026</u>	<u>1,904,104</u>
NON-CURRENT LIABILITIES			
Bank borrowings — due after one year		610,000	580,000
Deferred tax liabilities		9,856	10,470
		<u>619,856</u>	<u>590,470</u>
Total non-current liabilities			
		<u>619,856</u>	<u>590,470</u>
NET ASSETS			
		<u>1,391,170</u>	<u>1,313,634</u>
CAPITAL AND RESERVES			
Share capital		328,924	328,924
Reserves		1,004,830	923,395
Equity attributable to owners of the Company		1,333,754	1,252,319
Non-controlling interests		57,416	61,315
		<u>1,391,170</u>	<u>1,313,634</u>
TOTAL EQUITY			
		<u>1,391,170</u>	<u>1,313,634</u>

UNAUDITED CONDENSED CONSOLIDATED STATEMENT OF CASH FLOWS

For the six months ended 30 June 2010

	Six months ended 30 June	
	2010	2009
	<i>RMB'000</i>	<i>RMB'000</i>
Net cash inflow from operating activities	(68,761)	59,618
Net cash outflow from investing activities	(268,200)	(191,523)
Net cash inflow from financing activities	<u>281,271</u>	<u>195,259</u>
Net increase/(decrease) in cash and cash equivalents	(55,690)	63,354
Cash and cash equivalents at the beginning of the period	<u>121,592</u>	<u>195,133</u>
Cash and cash equivalents at the end of the period	<u><u>65,902</u></u>	<u><u>258,487</u></u>
Analysis of balances of cash and cash equivalents		
Cash and bank balances	65,902	80,346
Time deposits with original maturity of less than three months when acquired, pledged	<u>—</u>	<u>178,141</u>
	<u><u>65,902</u></u>	<u><u>258,487</u></u>

UNAUDITED CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

For the six months ended 30 June 2010

	Attributable to owners of the Company						Non-controlling interests	Total equity
	Share capital	Capital reserve	Statutory surplus reserve	Retained profits	Translation reserve	Dividend reserve	Total	
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
At 1 January 2009	328,924	121,668	80,087	454,063	(811)	65,785	1,049,716	60,307
Profit for the period	—	—	—	140,088	—	—	140,088	1,202
Exchange differences arising on translation of foreign operations	—	—	—	—	13	—	13	65
Dividend paid	—	—	—	—	—	(65,785)	(65,785)	(4,500)
At 30 June 2009	<u>328,924</u>	<u>121,668</u>	<u>80,087</u>	<u>594,151</u>	<u>(798)</u>	<u>—</u>	<u>1,124,032</u>	<u>57,074</u>
At 1 January 2010	328,924	121,668	108,376	654,618	(737)	39,471	1,252,320	61,315
Profit for the period	—	—	—	120,900	—	—	120,900	1,050
Exchange differences arising on translation of foreign operations	—	—	—	—	5	—	5	1
Dividend paid	—	—	—	—	—	(39,471)	(39,471)	(4,950)
At 30 June 2010	<u>328,924</u>	<u>121,668</u>	<u>108,376</u>	<u>775,518</u>	<u>(732)</u>	<u>—</u>	<u>1,333,754</u>	<u>57,416</u>

NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Amounts expressed in Renminbi unless otherwise stated)

1. General Information and Basis of Preparation

The condensed consolidated financial statements were unaudited. The condensed consolidated financial statements have been reviewed by the audit committee of the Company.

The Company was incorporated as a joint stock company with limited liability in the People's Republic of China (the "PRC") on 30 December 2001 and its H shares were listed on the Growth Enterprise Market of The Stock Exchange of Hong Kong Limited (the "Stock Exchange") (the "GEM") on 15 April 2004. On 5 July 2004, the Company has authorized to become a Sino-foreign joint stock limited company. The Company transferred from the GEM to the Main Board of the Stock Exchange on 7 February 2007.

The unaudited condensed consolidated financial statements have been prepared in accordance with Hong Kong Financial Reporting Standards ("HKFRSs") (which also include Hong Kong Accounting Standards ("HKASs") and Interpretations) issued by the Hong Kong Institute of Certified Public Accountants ("HKICPA"), accounting principles generally accepted in Hong Kong and the disclosure requirements of Appendix 16 to the Rules Governing the Listing of Securities on the Stock Exchange of Hong Kong Limited.

The principal accounting policies used in the preparation of the condensed consolidated financial statements are consistent with those used in the preparation of the Group's annual financial statements for the year ended 31 December 2009.

In current interim period, the Group has applied, for the first time, the following new or revised standards, amendments and interpretations ("new or revised HKFRSs") issued by the HKICPA.

HKFRSs (Amendments)	Amendment to HKFRS 5 as part of Improvements to HKFRSs 2008
HKFRSs (Amendments)	Improvements to HKFRSs 2009
HKAS 27 (Revised)	Consolidated and Separate Financial Statements
HKAS 39 (Amendment)	Eligible Hedged Items
HKFRS 1 (Amendment)	Additional Exemptions for First-time Adopters
HKFRS 2 (Amendment)	Group Cash-settled Share-based Payment Transactions
HKFRS 3 (Revised)	Business Combinations
HK(IFRIC)-Int 17	Distributions of Non-cash Assets to Owners

The Group applies HKFRS 3 (Revised) Business Combinations prospectively to business combinations for which the acquisition date is on or after 1 January 2010. The requirements in HKAS 27 (Revised) Consolidated and Separate Financial Statements in relation to accounting for changes in ownership interests in a subsidiary after control is obtained and for loss of control of a subsidiary are also applied prospectively by the Group on or after 1 January 2010.

As there was no transaction during the current interim period in which HKFRS 3 (Revised) and HKAS 27 (Revised) are applicable, the application of HKFRS 3 (Revised), HKAS 27 (Revised) and the consequential amendments to other HKFRSs had no effect on the condensed consolidated financial statements of the Group for the current or prior accounting periods.

Results of the Group in future periods may be affected by future transactions for which HKFRS 3 (Revised), HKAS 27 (Revised) and the consequential amendments to the other HKFRSs are applicable.

The application of the other new and revised HKFRSs had no effect on the condensed consolidated financial statements of the Group for the current or prior accounting periods.

The Group has not early applied the following new or revised standards, amendments or interpretations that have been issued but are not yet effective:

HKFRSs (Amendments)	Improvements to HKFRSs 2010 ¹
HKAS 24 (Revised)	Related Party Disclosures ⁴
HKAS 32 (Amendment)	Classification of Rights Issues ²
HKFRS 1 (Amendment)	Limited Exemption from Comparative HKFRS 7 Disclosures for First-time Adopters ³
HKFRS 9	Financial Instruments ⁵
HK(IFRIC)-Int 14 (Amendment)	Prepayments of a Minimum Funding Requirement ⁴
HK(IFRIC)-Int 19	Extinguishing Financial Liabilities with Equity Instruments ³

¹ Effective for annual periods beginning on or after 1 July 2010 and 1 January 2011, as appropriate

² Effective for annual periods beginning on or after 1 February 2010

³ Effective for annual periods beginning on or after 1 July 2010

⁴ Effective for annual periods beginning on or after 1 January 2011

⁵ Effective for annual periods beginning on or after 1 January 2013

HKFRS 9 Financial Instruments introduces new requirements for the classification and measurement of financial assets and will be effective from 1 January 2013, with earlier application permitted. The Standard requires all recognised financial assets that are within the scope of HKAS 39 Financial Instruments: Recognition and Measurement to be measured at either amortised cost or fair value. Specifically, debt investments that (i) are held within a business model whose objective is to collect the contractual cash flows and (ii) have contractual cash flows that are solely payments of principal and interest on the principal outstanding are generally measured at amortised cost. All other debt investments and equity investments are measured at fair value. The application of HKFRS 9 might not affect the classification and measurement of the Group's financial assets.

The directors of the Company anticipate that the application of other new and revised standards, amendments or interpretations will have no material impact on the results and the financial position of the Group.

2. Segment Information

The following is an analysis of the Group's revenue and results by operating segment for the period under review:

For the six months ended 30 June 2010						
	Tubings	Casings	Three kings of pumping units	Petroleum machinery	Others	Total
	<i>RMB'000</i>	<i>RMB'000</i>	<i>RMB'000</i>	<i>RMB'000</i>	<i>RMB'000</i>	<i>RMB'000</i>
Segment revenue	<u>287,363</u>	<u>708,964</u>	<u>46,663</u>	<u>57,322</u>	<u>218,533</u>	<u>1,318,845</u>
Segment result	<u>42,358</u>	<u>105,307</u>	<u>9,654</u>	<u>14,261</u>	<u>3,821</u>	<u>175,401</u>
Unallocated corporate income						33,016
Unallocated corporate expenses						(42,244)
Finance costs						<u>(19,551)</u>
Profit before taxation						<u>146,622</u>

For the six months ended 30 June 2009						
	Tubings	Casings	Three kings of pumping units	Petroleum machinery	Others	Total
	<i>RMB'000</i>	<i>RMB'000</i>	<i>RMB'000</i>	<i>RMB'000</i>	<i>RMB'000</i>	<i>RMB'000</i>
Segment revenue	<u>333,689</u>	<u>457,942</u>	<u>35,627</u>	<u>60,098</u>	<u>9,171</u>	<u>896,527</u>
Segment result	<u>50,918</u>	<u>82,004</u>	<u>7,003</u>	<u>5,567</u>	<u>194</u>	<u>145,686</u>
Unallocated corporate income						53,518
Gain on fair value of foreign currency forward contracts						310
Share of results of associate						(90)
Unallocated corporate expenses						(21,096)
Finance costs						<u>(12,637)</u>
Profit before taxation						<u>165,691</u>

3. Other income and Gains

	Six months ended 30 June	
	2010	2009
	RMB'000	RMB'000
	(Unaudited)	(Unaudited)
Sale of materials	1,028	286
Technology transfer fees	—	4,305
Bank interest income	2,071	9,845
Government subsidies	17,237	37,097
Valued-added tax (“VAT” refund) refund	11,997	1,576
Others	683	409
	<u>33,016</u>	<u>53,518</u>
Total	<u>33,016</u>	<u>53,518</u>

4. Profit Before Taxation

The Group's profit before taxation is arrived at after charging/(crediting):

	Six months ended 30 June	
	2010	2009
	RMB'000	RMB'000
	(Unaudited)	(Unaudited)
Cost of inventories sold	1,120,341	695,917
Depreciation of property, plant and equipment	47,251	43,227
(Write-back of provision)/provision against inventories	(1,741)	5,816
Reversed of allowance for trade receivables	(431)	(10,756)
Research and development costs	6,524	8,347
	<u>6,524</u>	<u>8,347</u>

5. Taxation

The Company was named as one of the Shandong Province New and High Technical Enterprise (山東省高新技術企業). According to the People's Republic of China (the “PRC”) Law on Enterprise Income Tax promulgated on 16 March 2007, the Company is entitled to a concessionary rate of income tax at 15% over 3 years, beginning on 1 January 2008.

For the subsidiaries located in Mainland China, they are subject to the PRC corporate income tax at a rate of 25% (2008:25%) on its assessable profits. The subsidiary in Hong Kong is subject to Hong Kong Profits Tax rate of 16.5% (2008:16.5%) on its assessable profits.

Weifang Molong Drilling Equipment Company Limited (“Molong Drilling Equipment”), according to the tax document Cai Shui Zi [2007] No. 92 (財稅字[2007]92號文), with effect from 1 July 2007, Molong Drilling Equipment was entitled to claim twice of salaries paid to its disabled employees when calculating the PRC corporate income tax.

	Six months ended 30 June	
	2010	2009
	RMB'000	RMB'000
	(Unaudited)	(Unaudited)
Current taxation	18,211	20,579
Deferred taxation	6,461	3,822
	<u>24,672</u>	<u>24,401</u>

6. Earnings Per Share

The calculation of the basic earnings per share is based on the profit attributable to owners of the Company of approximately RMB120,900,000 for the six months ended 30 June 2010 (2009: RMB140,088,000) and on the weighted average number of 328,924,200 (2009: 3,289,242,000) shares in issue during the period.

7. Inventories

	30 June	31 December
	2010	2009
	RMB'000	RMB'000
	(unaudited)	(audited)
Raw materials	242,890	202,850
Work in progress	278,882	283,133
Finished goods	269,688	227,672
Total	<u>791,460</u>	<u>713,655</u>

8. Trade and Other Receivables and Bills Receivables

	30 June	31 December
	2010	2009
	RMB'000	RMB'000
	(unaudited)	(audited)
Trade receivables	547,847	450,746
Deposits and other receivables	65,656	24,369
Prepaymants	239,877	53,080
	<u>853,380</u>	<u>528,195</u>
Bills receivables	9,761	34,631
	<u>863,141</u>	<u>562,826</u>

The Group's trading terms with its customers are mainly on credit, except for new customers, where payment in advance is normally required. The credit period is generally for a period of three months, extending up to six months for major customers. The following is an analysis of the trade receivables by age, presented based on invoice date.

	30 June 2010 RMB'000 (unaudited)	31 December 2009 RMB'000 (audited)
Trade receivables		
Within three months	437,684	373,572
Three to six months	53,223	17,920
Six months to one year	12,606	8,179
Over one year	44,334	51,075
Total	547,847	450,746

Bills receivables are all aged within six months.

9. Trade and Bills Payables

An aged analysis of trade and bills payables by age, presented based on invoice date, is as follows:

	30 June 2010 RMB'000 (unaudited)	31 December 2009 RMB'000 (audited)
Trade and bill payables		
Within three months	458,694	373,466
Three to six months	272,867	259,822
Six months to one year	37,073	42,232
More than one year	42,312	43,279
Total	810,946	718,799

As at 30 June 2010, the Group's bills payables of RMB372,122,000 (31 December 2009: RMB373,611,000) were secured by the pledge of certain time deposits amounting to RMB179,058,000 (31 December 2009: RMB183,918,000). The average credit period on purchase is six months.

10. Capital Commitments

	30 June 2010 RMB'000 (unaudited)	31 December 2009 RMB'000 (audited)
Capital expenditure in respect of the acquisition of property, plant and equipment contracted for but not provided in the consolidated financial statements	170,644	173,726

MANAGEMENT DISCUSSION AND ANALYSIS

Financial Review

For the six months ended 30 June 2010, the Group recorded an unaudited revenue of approximately RMB1,318,845,000 (2009: approximately RMB896,527,000), representing an increase of approximately RMB422,318,000 or an increase of 47.11% as compared to the corresponding period in the previous year, and net profit of approximately RMB120,900,000 (2009: approximately RMB140,088,000) with a decrease of 13.70% as compared to the corresponding period last year, in which net profit operation was approximately RMB107,623,000, representing an increase of 11.55% from RMB96,476,000 over the corresponding period last year.

During the period under review, the revenue derived from domestic sales was RMB919,415,000, an increase of 88.28% as compared to the corresponding period in the previous year, and accounted for 69.71% of the total revenue during the period under review. Meanwhile, the revenue derived from overseas markets was RMB399,470,000, a decrease of 2.15% as compared to the corresponding period in the previous year and accounted for 30.29% of the total revenue during the period under review.

Region	For the six months ended 30 June 2010		For the six months ended 30 June 2009	
	Revenue RMB'000	percentage (%)	Revenue RMB'000	percentage (%)
PRC	919,415	69.71	488,313	54.47
United States	229,580	17.41	230,031	25.66
Japan	13,476	1.02	58,479	6.52
Other countries	<u>156,374</u>	<u>11.86</u>	<u>119,704</u>	<u>13.35</u>
Total	<u><u>1,318,845</u></u>	<u><u>100.00</u></u>	<u><u>896,527</u></u>	<u><u>100.00</u></u>

During the period under review, the gross profit was RMB198,504,000, basically equal to RMB200,610,000 during the same period in 2009. Gross margin for the first six months of 2010 was 15.05%, compared to 22.38% in the same period in 2009. The decrease in gross margin was mainly due to the significant increase in the production volume of a subsidiary as compared to the corresponding period last year. This has not only secured the supply of raw materials for the Group's internal use, but also generated a revenue of RMB217,880,000 from the external sales of the excessive products. However, the Group's consolidated gross profit margin reduced and it was attributable to the lower gross profit margin of such products in which the gross profit margin of its key products of tubing and casings were 17.04% and 17.13% respectively, declining from 19.57% and 19.79% respectively as recorded in last year. This was mainly resulted from the time lag between the sales price adjustment and the time in which the raw materials fluctuated. After the price adjustment of the products in June, the gross profit margin of tubing and casing were 20.32% and 21.43% respectively, higher than the annual average last year.

During the period under review, the selling expenses was RMB23,103,000, an decrease of 45.60% as compared to RMB42,466,000 during the same period in 2009. The decrease in the selling expenses was due to the realization of the benefit of the market expansion measures we have taken amid the gradual recovery of the market.

During the period under review, the administrative expenses was RMB32,382,000, an increase of 6.46% as compared to RMB30,417,000 during the same period in 2009. The increase in administrative expenses was mainly due to the increase in the amortisation of intangible assets.

During the period under review, finance costs was RMB19,551,000, an increase of 54.71% from RMB12,637,000 during the same period in 2009. The increase was mainly due to the increase in bank loans resulting from expansion of the Group's production and sales capacity.

As at the end of the period under review, the cash and cash equivalent was RMB65,902,000, representing a decrease of RMB55,690,000 from RMB121,592,000 as at the end of 2009, in which net cash inflow from the operation activities was RMB-68,761,000 which was mainly attributable to the prepayment of RMB200,000,000 made to the raw materials suppliers for purchase of raw materials after the determination of the raw material prices during the period. Net cash outflow from the investment business was RMB268,200,000, and this was mainly attributable to the investment expenses for the construction of 180mm designated oil pipes re-construction project. Net cash inflow from the financing activities was RMB281,271,000. This was mainly attributable to increase in bank loans for the prepayment made to suppliers at the price fixed, and increase in working capital loan for the expansion of the production and sales capacity.

Business Review

Main Business

During the period under review, the Group was engaged in the business of design, manufacture and sale of petroleum drilling and extraction machinery and related accessories. Its major products can be divided into six categories, namely oil well pipes, casings, oil well sucker rods, oil well pumps, oil well pumping machines and other petroleum drilling and extraction machinery accessories. These products are primarily used in petroleum drilling and extraction and are necessary equipment of the industry.

Release of Production Capacity

During the period under review, the 250,000-tonne oil casing production line has reached its full designed production capacity, and the output of it reached 126,000 tonnes. The release of the full potential of the production capacity of such production line has allowed the substantial increase in the production of oil casing and the production capacity of high value-added value non-API casing of the Group, which are beneficial to the Group's profitability and market competitiveness.

Enhance Marketing Strategies and Expand Domestic and Overseas Markets

Domestic market development

The Group's current major customers are oil fields operated by the two oil groups in the domestic markets, namely PetroChina Company Limited and its subsidiaries (collectively "PetroChina Group"), which own oil fields including Xinjiang Oil Field (新疆油田), Daqing Oil Field (大慶油田), Changqing Oil Field (長慶油田), Liaohe Oil Field (遼河油田), Tarim Oilfield (塔里木油田), Qinghai Oil Field (青海油田), Huabei Oil Field (華北油田) and Jilin Oil Field (吉林油田), and China Petroleum & Chemical Corporation and its subsidiaries (collectively "Sinopec Group"), which own oil fields including Shengli Oil Field (勝利油田), Zhongyuan Oil Field (中原油田), Jiangsu Oil Field (江蘇油田), Jiangnan Oil Field (江漢油田) etc.. During the period under review, the Group had once again become one of the seven major providers of finished oil well pipers in oil business in China, which laid solid foundation to increase the shares of the Group's products in the domestic market. Meanwhile, the Group actively promoted the cooperation in the ocean oil well-pipes and petroleum machinery aspects with CNOOC Limited and its subsidiaries (collectively "CNOOC Group"), and Shanxi Yanchang Petroleum (Group) Co., Ltd. (i.e. Yanchang Petroleum, 延長石油), and further implemented stated strategies of overall cooperation with the four major domestic oil groups.

During the period under review, the Group introduced various products to the market. For example, 80S tubing was supplied to Chuanqing Drilling, 12Cr1MoVG high-pressure boiler tubing was supplied to Tianjin Zhicheng Xinda Company Limited (天津至誠信達有限公司) and Tianjin YaDiEr Iron & Steel Trading Co., Ltd. (天津雅迪爾鋼鐵貿易有限公司); and 20# steel high-pressure fertilizer tubing was supplied to Qinghai Oil Field. The developments of new products and customers laid good foundation to enhance the market competitiveness of the Company's products.

In the emerging coal and coalbed gas exploitation market, the Company's products such as oil casing pipes, oil well pumps, oil well pumping machines and hydraulic supporting tubes have been successfully supplied in mass quantity to new customers such as Tianjin Baoye Steel Tube Company Limited (天津寶冶鋼管有限公司), Hubei Shenhe Hydraulic Machinery Company Limited (湖北神河液壓機械有限公司), Tianjin Shuofeng Steel Tube Company Limited (天津碩豐鋼管有限公司), Tianjin Haoyuan Weiye Steel Tube Company Limited (天津浩源偉業鋼管有限公司), Linyi Zhongkuang Jinding Co., Ltd. (臨沂中礦金鼎有限公司), Shandong Tiansheng Mine Equipment Co., Ltd. (山東天晟煤礦裝備有限公司), Henan Middlings Pipe Industry Co., Ltd. (河南中煤管業有限公司) and Shan Dong Xin Mei Machinery Co., Ltd. (山東新煤機械有限公司). With the rapid scale development of the emerging field of coalbed gas extraction, the demand for the Company's products will continue to increase.

Overseas markets

During the period under review, overcoming effect of the financial crisis, the Group further strengthened markets including Southeast Asia, the Middle East, South America, while the Group continued to step up its efforts in developing its business to regions such as South America, North Africa, Central Africa and had achieved good performance. The nickel plating corrosion resistant oil well sucker rod was supplied to the Canadian market. The Group continued to establish and maintain good cooperative relationships with several international oil companies, which in turn boosted the sales of its products in the overseas markets.

Comprehensive Development of New Products

The Group is proactively engaged in the R&D of new products, and it has successfully increased the number of suitable R&D and quality control experts in the industry in order to keep abreast of the latest information and technology in the world for maintaining its leading position in the industry.

The Group has increased investment in technology which is mainly for accelerating the development of new products, standardizing the technology basic administration, enhancing the improvement of technology and optimizing the structure of existing products.

During the period under review, the Group continued to increase its efforts to develop high-end products and strengthened technological cooperation with research institutes such as Xi'an Jiaotong University, Xi'an Pipe Material Research Institute of PetroChina Group, Xi'an Maurer Petroleum Engineering Material Lab and China University of Petroleum (East China). The Group actively expanded the product structure, enriched product categories and gradually develop new products, such as L80-1Cr tubing, 80S tubing, nickel plating corrosion resistant oil well sucker rod, 12Cr1MoVG high pressure boiler pipes, 20# aluminium high pressure chemical fertilizer pipes, which have been produced under mass production; 73 special couplings oil pipes and BNS acid conduit pipes which have been examined and tested by the authorities on the mainland and are in the pipeline for mass production; as well as Q125-1 high end aluminium casings and ML125TT strong anti-pressure casings which are currently being examined and tested by the authorities on the mainland.

Proposed A Share Issue

The A share proposal and relevant authorizations had been approved at the annual general meeting and the class meetings held on 28 March 2010 by the Company. The Company is compiling the relevant materials and will choose a good opportunity to submit the application for A share issue to the China Securities Regulatory Commission.

Major Acquisitions/Disposals and Significant Investment

During the period under review, the Group had no major acquisition or disposal and significant investments.

Outlook

International Monetary Fund (IMF) updated the World Economic Outlook on 8 July, where it forecasted that an approximately 4.5% and 4.25% growth in the world economy this year and next year will be recorded, respectively. As compared with the forecast last quarter, IMF raised its forecast of this year by 0.5%, implying buoyant economic activities in the first half of the year. IMF also believed that the risk of global deflation was considerably low, and the oil price would probably reach US\$75.3 per barrel by the end of the year.

The 2010 Energy Blue Book which was newly published by Social Sciences Academic Press indicates that oil supply in China will grow steadily, and although the demand slowed down in the short term, it is expected to rise in the long term.

With the recovery of the economy, the global demand for petroleum will increase, which will stimulate oil fields exploitation to increase output, to increase the market demand for petroleum drilling and extraction machinery, and to bring better development for the petroleum machinery industry. Hence the Group will continue to capture opportunities and further enhance its competitive capability through various strategies, including introduction of new products and high value-added products, improvement of product quality, strengthening of its research and development capability, enhancement of market promotion and adoption of effective cost control. Meanwhile, the Group will continue to develop its domestic and overseas markets in order to increase its market share in the industry.

Looking forward, the Group will continue to focus on its business of petroleum drilling and extraction machinery, and continue to research in and develop new products which respond to customers' needs. It will suitably increase the scale of the production, and continue to develop the petroleum and natural gas and the coal mine methane drilling and extraction equipment industry.

Progress of High Grade Special Petroleum Pipes Technical Reconstruction Project

As at the date of this report, the “180mm special petroleum pipes technical reconstruction project” (the “180 Project”) has completed investment of RMB590,180,000. After the completion of the 180 project, the Group is expected to produce additional 300,000 tonnes high grade special petroleum pipes per year, which will reach in the next 3 years, and will change the status of the limited capacity of the Company.

Bank Facilities and Pledge of Assets

As at 30 June 2010, the Group had bank credit loans amounting to RMB1,057,000,000. In addition, ten banks, including the Agricultural Bank of China (Shandong Branch), have granted credit facilities totaling RMB1,763,000,000 to the Group. None of these credit facilities have been utilized.

Employees

For the period under review, the breakdown of the number of employees of the Group is set out below:

	As of 30 June	
	2010	2009
Research and development	70	66
Production	2,258	2,197
Quality control	144	183
Sales and marketing	63	68
Administration	178	188
Total	<u>2,713</u>	<u>2,702</u>

During the period under review, the decline of employees is caused by natural attrition. The impact was compensated by the detailed management measures such as optimum composition of the jobs and improving efficiency taken by the Company.

CORPORATE GOVERNANCE

The Company has complied throughout the period under review with the code provisions set out in the Code on Corporate Governance (the “Code”) contained in Appendix 14 of the Listing Rules without any deviation. None of the Directors is aware of any information that would reasonably suggest that the Company is not or was not in compliance with the Code at any time during the period under review.

Audit Committee

The Audit Committee is mainly responsible for monitoring the completeness of the Company’s financial statements, reviewing the Company’s internal control system and its execution, through review of work undertaken by the internal and external auditors, evaluating financial information and related disclosures.

The Audit Committee consists of three independent non-executive Directors, namely Mr. Chau Shing Yim David, Mr. John Paul Cameron and Ms. Wang Chun Hua. Mr. Chau Shing Yim David is the Chairman of the Audit Committee. The Audit Committee held one meeting during the period under review with an attendance rate of 100%.

The Audit Committee has reviewed the Group’s unaudited financial statements and monitored internal control system and its execution for the six months ended 30 June 2010.

Purchase, Sale or Redemption of Securities

Neither the Company nor its subsidiaries has purchased, sold or redeemed any listed securities of the Company during the six months ended 30 June 2010.

Directors

As at the date of this announcement, the executive Directors of the Company are Mr. Zhang En Rong, Mr. Zhang Yun San, Mr. Lin Fu Long and Mr. Xie Xin Cang; the non-executive Directors are Mr. Chen Jian Xiong and Mr. Wang Ping; and the independent non-executive Directors are Mr. Chau Shing Yim David, Mr. John Paul Cameron and Ms. Wang Chun Hua.

By order of the Board of Directors
Zhang En Rong
Chairman

Shandong, the PRC
23 July 2010