**Honghua Group Limited**
**宏 華 集 團 有 限 公 司**
*(a company incorporated in the Cayman Islands with limited liability)*
**(Stock code: 0196)**

# ANNUAL RESULTS ANNOUNCEMENT FOR YEAR ENDED 31 DECEMBER 2011

## FINANCIAL HIGHLIGHT

| | For the year ended 31 December | | |
|---|---|---|---|
| | **2011** | 2010 | **change** |
| Turnover (RMB'000) | **3,485,046** | 1,877,931 | 85.6% |
| Gross profit (RMB'000) | **970,104** | 380,478 | 155.0% |
| Gross profit margin (%) | **27.8%** | 20.3% | |
| Profit/(loss) from operations (RMB'000) | **243,856** | (119,803) | |
| Profit/(loss) attributable to equity shareholders of the Company (RMB'000) | **167,984** | (184,165) | |
| Earnings/(loss) per share — Basic and Diluted (RMB cents) | **5.21** | (5.71) | |

The Directors recommend the payment of a final dividend of HK$0.04 per Share for the year ended 31 December 2011.

## ANNUAL RESULTS

The Board is pleased to announce the consolidated results of the Group for the year ended 31 December 2011, together with the comparative figures for the year ended 31 December 2010 as follows:

# CONSOLIDATED INCOME STATEMENT

*for the year ended 31 December 2011*

(Expressed in Renminbi)

| | Note | **2011** *RMB'000* | 2010 *RMB'000* |
|---|---|---|---|
| **Turnover** | 5 | **3,485,046** | 1,877,931 |
| Cost of sales | | **(2,514,942)** | (1,497,453) |
| **Gross profit** | | **970,104** | 380,478 |
| Other revenue | 6 | **27,444** | 29,900 |
| Other net income/(loss) | 6 | **60,012** | (5,274) |
| Selling expenses | | **(385,532)** | (180,642) |
| General and administrative expenses | | **(408,877)** | (340,360) |
| Other operating expenses | | **(19,295)** | (3,905) |
| **Profit/(loss) from operations** | | **243,856** | (119,803) |
| Finance income | | **27,291** | 23,691 |
| Finance expenses | | **(77,626)** | (83,132) |
| **Net finance expenses** | 7(a) | **(50,335)** | (59,441) |
| Share of profit from jointly controlled entities | | **293** | 2,801 |
| Share of profit from an associate | | **5,398** | — |
| **Profit/(loss) before taxation** | | **199,212** | (176,443) |
| Income tax (expenses)/credit | 8 | **(27,769)** | 4,372 |
| **Profit/(loss) for the year** | | **171,443** | (172,071) |
| **Attributable to:** | | | |
| Equity shareholders of the Company | | **167,984** | (184,165) |
| Non-controlling interests | | **3,459** | 12,094 |
| **Profit/(loss) for the year** | | **171,443** | (172,071) |
| **Earnings/(loss) per share — Basic and Diluted (RMB cents)** | 10 | **5.21** | (5.71) |

# CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

*for the year ended 31 December 2011*
(Expressed in Renminbi)

| | **2011** | 2010 |
|---|---|---|
| | ***RMB'000*** | *RMB'000* |
| **Profit/(loss) for the year** | **171,443** | (172,071) |
| **Other comprehensive income for the year:** | | |
| Exchange differences on translation of financial statements of operations outside the PRC, net of tax | **(30,422)** | (34,862) |
| Less: Reclassification adjustment for translation reserves transferred to profit or loss upon liquidation of a subsidiary | **(50,430)** | — |
| | **(80,852)** | (34,862) |
| **Total comprehensive income for the year** | **90,591** | (206,933) |
| **Attributable to:** | | |
| Equity shareholders of the Company | **87,463** | (219,037) |
| Non-controlling interests | **3,128** | 12,104 |
| **Total comprehensive income for the year** | **90,591** | (206,933) |

# CONSOLIDATED BALANCE SHEET

*at 31 December 2011*

(Expressed in Renminbi)

| | Note | **31 December 2011** *RMB'000* | 31 December 2010 *RMB'000* |
|---|---|---|---|
| **Non-current assets** | | | |
| Fixed assets | | | |
| — Property, plant and equipment | | **678,597** | 529,574 |
| — Interests in leasehold land held for own use under operating leases | | **181,189** | 140,058 |
| — Freehold land | | **5,080** | 5,339 |
| | | **864,866** | 674,971 |
| Deposits paid for acquisition of leasehold land | | **192,830** | 218,984 |
| Construction in progress | | **402,065** | 77,144 |
| Intangible assets | | **235,994** | 272,585 |
| Interests in jointly controlled entities | | **38,919** | 41,868 |
| Interest in an associate | | **63,405** | — |
| Deferred tax assets | | **84,253** | 69,341 |
| **Total non-current assets** | | **1,882,332** | 1,354,893 |
| **Current assets** | | | |
| Inventories | 11 | **1,544,127** | 1,859,897 |
| Trade and other receivables | 12 | **1,562,410** | 1,217,108 |
| Amounts due from related companies | | **64,854** | 25,761 |
| Current tax recoverable | | **34,418** | 27,508 |
| Other financial assets | | **678,000** | 473,680 |
| Pledged bank deposits | | **65,612** | 29,072 |
| Bank deposits maturing over three months | | **9,100** | 4,000 |
| Cash and cash equivalents | | **851,847** | 1,002,727 |
| **Total current assets** | | **4,810,368** | 4,639,753 |

# CONSOLIDATED BALANCE SHEET

*at 31 December 2011*

(Expressed in Renminbi)

| | *Note* | **31 December 2011** ***RMB'000*** | 31 December 2010 *RMB'000* |
|---|---|---|---|
| **Current liabilities** | | | |
| Interest-bearing borrowings | | **499,738** | 444,000 |
| Amounts due to related companies | | **28,290** | 48,206 |
| Trade and other payables | 13 | **1,531,323** | 1,209,911 |
| Current tax payable | | **38,543** | 11,196 |
| Provision for product warranties | | **21,243** | 15,738 |
| **Total current liabilities** | | **2,119,137** | 1,729,051 |
| **Net current assets** | | **2,691,231** | 2,910,702 |
| **Total assets less current liabilities** | | **4,573,563** | 4,265,595 |
| **Non-current liabilities** | | | |
| Interest-bearing borrowings | | **380,000** | 182,318 |
| Deferred tax liabilities | | **18,705** | 12,486 |
| **Total non-current liabilities** | | **398,705** | 194,804 |
| **Net assets** | | **4,174,858** | 4,070,791 |
| **Equity** | | | |
| Share capital | | **299,593** | 299,593 |
| Reserves | | **3,758,990** | 3,663,937 |
| **Total equity attributable to equity shareholders of the Company** | | **4,058,583** | 3,963,530 |
| **Non-controlling interests** | | **116,275** | 107,261 |
| **Total equity** | | **4,174,858** | 4,070,791 |

## 1. REVIEW OF ANNUAL RESULTS

The annual results have been reviewed by the Audit Committee.

The figures in respect of the preliminary announcement of the Group's results for the year ended 31 December 2011 have been compared by the Company's auditors, KPMG, Certified Public Accountants, to the amounts set out in the Group's draft financial statements for the year and the amounts were found to be in agreement. The work performed by KPMG in this respect was limited and did not constitute an audit, review or other assurance engagement and consequently no assurance has been expressed by the auditors on this announcement.

## 2. STATEMENT OF COMPLIANCE

The financial statements have been prepared in accordance with all applicable International Financial Reporting Standards ("IFRSs"), which collective term includes all applicable individual International Financial Reporting Standards, International Accounting Standards ("IASs") and Interpretations issued by the International Accountancy Standards Board ("IASB") and the disclosure requirements of the Hong Kong Companies Ordinance. The financial statements also comply with the applicable disclosure provisions of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited.

The IASB has issued certain new and revised IFRSs that are first effective or available for early adoption for the current accounting period of the Group and the Company. Note 3 provides information on any changes in accounting policies resulting from initial application of these developments to the extent that they are relevant to the Group for the current and prior accounting periods reflected in the financial statements.

## 3. CHANGES IN ACCOUNTING POLICIES

The IASB has issued a number of amendments to IFRSs that are first effective for the current accounting period of the Group and the Company. Of these, the following developments are relevant to the Group's financial statements:

— IAS 24 (revised 2009), Related party disclosures
— Improvements to IFRSs (2010)

The Group has not applied any new standard or interpretation that is not yet effective for the current accounting period.

The impacts of other developments are discussed below:

— IAS 24 (revised 2009) revises the definition of a related party. IAS 24 (revised 2009) also introduces modified disclosure requirements for government-related entities. As a result, the Group has re-assessed the identification of related parties and concluded that the revised definition does not have any material impact on the Group's related party disclosures in the current and previous periods.

— Improvements to IFRSs (2010) omnibus standard introduces a number of amendments to the disclosure requirements in IFRS 7, Financial instruments: Disclosures. The disclosures about the Group's financial instruments have been conformed to the amended disclosure requirements. These amendments do not have any material impact on the classification, recognition and measurements of the amounts recognised in the financial statements in the current and previous periods.

## 4. SEGMENT REPORTING

The Group manages its business by divisions, which are organised by business lines (land drilling rigs, offshore drilling rigs and parts and components). In a manner consistent with the way in which information is reported internally to the Group's most senior executive management for the purposes of resource allocation and performance assessment, the Group has presented the following three reportable segments. No operating segments have been aggregated to form the following reportable segments.

Land drilling rigs — This segment manufactures and sells land drilling rigs.

Offshore drilling rigs — This segment manufactures and sells offshore drilling rigs and related parts and components.

Parts and components — This segment manufactures and sells parts and components of land drilling rigs.

**(a) Segment results, assets and liabilities**

For the purposes of assessing segment performance and allocating resources between segments, the Group's senior executive management monitors the results, assets and liabilities attributable to each reportable segment on the following bases:

Segment assets include all tangible, intangible assets and current assets with the exception of interests in associates and jointly controlled entities, deferred tax assets, current tax recoverable, other financial assets and other corporate assets. Segment liabilities include trade payable, accruals, provision for product warranties and bills payable attributable to the manufacturing and sales activities of the individual segments.

Revenue and expenses are allocated to the reportable segments with reference to sales generated by those segments and the expenses incurred by those segments or which otherwise arise from the depreciation or amortisation of assets attributable to those segments.

The measure used for reporting segment profit is "adjusted profit from operations". To arrive at adjusted profit from operations, the Group's profit from operations are further adjusted for items not specifically attributed to individual segments, such as directors' remuneration and other head office or corporate administration costs.

In addition to receiving segment information concerning adjusted profit from operations, management is provided with segment information concerning revenue (including inter-segment sales), write-down of inventories, depreciation, amortisation and impairment losses and additions to non-current segment assets used by the segments in their operations. Inter-segment sales are priced with reference to prices charged to external parties for similar orders.

Information regarding the Group's reportable segments as provided to the Group's most senior executive management for the purposes of resource allocation and assessment of segment performance for the years ended 31 December 2011 and 2010 is set out below.

| | **Land drilling rigs** | | **Offshore drilling rigs** | | **Parts, components and others** | | **Total** | |
|---|---|---|---|---|---|---|---|---|
| | **2011** | 2010 | **2011** | 2010 | **2011** | 2010 | **2011** | 2010 |
| | ***RMB'000*** | *RMB'000* | ***RMB'000*** | *RMB'000* | ***RMB'000*** | *RMB'000* | ***RMB'000*** | *RMB'000* |
| Revenue from external customers | **2,543,003** | 1,455,812 | **80,030** | — | **862,013** | 422,119 | **3,485,046** | 1,877,931 |
| Inter-segment revenue | **—** | — | **—** | — | **959,580** | 648,952 | **959,580** | 648,952 |
| Reportable segment revenue | **2,543,003** | 1,455,812 | **80,030** | — | **1,821,593** | 1,071,071 | **4,444,626** | 2,526,883 |
| Reportable segment profit/(loss) | **392,765** | (20,120) | **(79,633)** | — | **5,067** | 36,532 | **318,199** | 16,412 |
| Depreciation and amortisation for the year | **36,709** | 69,161 | **38,616** | — | **29,587** | 18,827 | **104,912** | 87,988 |
| Impairment of trade and bills receivable | **11,709** | — | **—** | — | **2,117** | 1,604 | **13,826** | 1,604 |
| Write-down of inventories | **10,991** | 19,411 | **—** | — | **8,503** | 1,365 | **19,494** | 20,776 |
| Reportable segment assets | **2,461,847** | 2,667,836 | **960,013** | — | **1,516,210** | 1,442,078 | **4,938,070** | 4,109,914 |
| Additions to non-current segment assets during the year | **21,577** | 42,813 | **68,726** | — | **157,478** | 71,857 | **247,781** | 114,670 |
| Reportable segment liabilities | **1,142,449** | 1,060,022 | **179,854** | — | **525,600** | 626,991 | **1,847,903** | 1,687,013 |

**(b) Reconciliation of reportable segment profit or loss, assets and liabilities**

| | 2011<br>*RMB'000* | 2010<br>*RMB'000* |
|---|---|---|
| **Profit/(Loss)** | | |
| Reportable segment profit | **318,199** | 16,412 |
| Elimination of inter-segment profits | **(104,634)** | (103,343) |
| Reportable segment profit/(loss) derived from group's external customers | **213,565** | (86,931) |
| Share of profit from an associate | **5,398** | — |
| Share of profit from jointly controlled entities | **293** | 2,801 |
| Other revenue, other net income/(loss) and other operating expenses | **68,161** | 20,721 |
| Net finance expenses | **(50,335)** | (59,441) |
| Unallocated head office and corporate expenses | **(37,870)** | (53,593) |
| Consolidated profit/(loss) before taxation | **199,212** | (176,443) |
| **Assets** | | |
| Reportable segment assets | **4,938,070** | 4,109,914 |
| Elimination of inter-segment receivables | **(574,949)** | (476,144) |
| | **4,363,121** | 3,633,770 |
| Interests in jointly controlled entities | **38,919** | 41,868 |
| Interests in an associate | **63,405** | — |
| Current tax recoverable | **34,418** | 27,508 |
| Deferred tax assets | **84,253** | 69,341 |
| Other financial assets | **678,000** | 473,680 |
| Unallocated head office and corporate assets | **1,430,584** | 1,748,479 |
| Consolidated total assets | **6,692,700** | 5,994,646 |
| **Liabilities** | | |
| Reportable segment liabilities | **1,847,903** | 1,687,013 |
| Elimination of inter-segment payables | **(574,949)** | (476,144) |
| | **1,272,954** | 1,210,869 |
| Current tax payable | **38,543** | 11,196 |
| Deferred tax liabilities | **18,705** | 12,486 |
| Unallocated head office and corporate liabilities | **1,187,640** | 689,304 |
| Consolidated total liabilities | **2,517,842** | 1,923,855 |

**(c) Geographic information**

The following table sets out information about the geographical location of (i) the Group's revenue from external customers and (ii) the Group's fixed assets, construction in progress and intangible assets ("specified non-current assets"). The geographical location of customers is based on the location at which the services were provided or the goods are delivered. The geographical location of the specified non-current assets is based on the physical location of the asset, in the case of property, plant and equipment, and the location of the operation to which they are allocated, in the case of intangible assets.

| | **Revenue from external customers** | | **Specified non-current assets** | |
|---|---|---|---|---|
| | **2011** | 2010 | **2011** | 2010 |
| | ***RMB'000*** | *RMB'000* | ***RMB'000*** | *RMB'000* |
| PRC (country of domicile) | **335,150** | 289,098 | **1,306,974** | 925,129 |
| Americas | **1,425,665** | 357,907 | **47,047** | 49,716 |
| Middle East | **232,066** | 330,925 | **18,997** | 6,518 |
| Europe and Central Asia | **1,160,933** | 550,283 | **90,859** | 1,422 |
| South Asia and South East Asia | **253,456** | 316,603 | **—** | — |
| Others | **77,776** | 33,115 | **39,048** | 41,915 |
| | **3,485,046** | 1,877,931 | **1,502,925** | 1,024,700 |

## 5. TURNOVER

The principal activities of the Group are manufacturing, sale and trading of land drilling rigs, offshore drilling rigs and related parts and components. Turnover represents revenue recognised for the sales value of goods supplied to customers net of value-added tax, returns and trade discounts.

Further details regarding the Group's principal activities are disclosed in note 4 to the financial statements.

## 6. OTHER REVENUE AND OTHER NET INCOME/(LOSS)

| | **2011** | 2010 |
|---|---|---|
| | ***RMB'000*** | *RMB'000* |
| **Other revenue** | | |
| Repair services income | **18,874** | 15,607 |
| Government grants | **7,054** | 8,276 |
| Sale of scrap materials | **—** | 5,288 |
| Others | **1,516** | 729 |
| | **27,444** | 29,900 |
| **Other net income/(loss)** | | |
| Loss on disposals of fixed assets | **(474)** | (181) |
| Gain on liquidation of a subsidiary | **50,430** | — |
| Net gain on forward foreign exchange contracts | **12,457** | — |
| Others | **(2,401)** | (5,093) |
| | **60,012** | (5,274) |

## 7. PROFIT/(LOSS) BEFORE TAXATION

Profit/(loss) before taxation is arrived at after charging/(crediting):

### (a) Net finance expenses

| | **2011** | 2010 |
|---|---|---|
| | ***RMB'000*** | *RMB'000* |
| Foreign exchange loss, net | **33,723** | 42,801 |
| Interest income on bank deposits | **(6,604)** | (17,208) |
| Gain on disposal of other financial assets | **(20,687)** | (6,483) |
| Interest on interest-bearing borrowings wholly repayable within five years | **54,751** | 47,750 |
| Bank charges | **7,503** | 3,585 |
| | **68,686** | 70,445 |
| Less: interest expense capitalised into assets under construction * | **(18,351)** | (11,004) |
| | **50,335** | 59,441 |

* The borrowing costs have been capitalised at a rate of per annum 2.35% to 7.70% (2010: 2.35% to 7.06%).

### (b) Staff costs

| | | |
|---|---|---|
| Contributions to defined contribution retirement schemes | **44,079** | 35,997 |
| Equity-settled share based payment expenses | **7,590** | 17,574 |
| Salaries, wages and other benefits | **339,091** | 271,125 |
| | **390,760** | 324,696 |

### (c) Other items

| | | |
|---|---|---|
| Amortisation and depreciation | | |
| — leasehold land held for use under operating leases | **2,018** | 1,771 |
| — other fixed assets | **69,305** | 51,498 |
| — intangible assets | **34,741** | 36,407 |
| Auditors' remuneration | **3,243** | 3,538 |
| Operating lease charges: properties | **5,674** | 9,293 |
| Research and development costs (other than amortisation costs) * | **45,494** | 46,363 |

* The amounts included staff costs of employees in the Research and Development Department of RMB29,421,000 (2010: RMB39,829,000), which are included in the total staff costs as disclosed in note 7(b).

## 8. INCOME TAX EXPENSES/(CREDIT)

### (a) Taxation in the consolidated income statement represents:

| | **2011** | 2010 |
|---|---|---|
| | ***RMB'000*** | *RMB'000* |
| **Current tax — outside Hong Kong** | | |
| Provision for the year | **42,630** | 12,801 |
| (Over)/under-provision in respect of prior years | **(6,358)** | 596 |
| Sub-total | **36,272** | 13,397 |
| **Deferred tax** | | |
| Origination and reversal of temporary differences | **(8,503)** | (11,972) |
| Under-provision of deferred tax assets in respect of prior years | **—** | (5,797) |
| Sub-total | **(8,503)** | (17,769) |
| Income tax expenses/(credit) | **27,769** | (4,372) |

*(i) Hong Kong*

No provision for Hong Kong Profits Tax has been made as the Group did not have assessable profits subject to Hong Kong Profits Tax for the year (2010: Nil).

*(ii) PRC*

Pursuant to the income tax rules and regulations of the PRC, the companies comprising the Group in the PRC are liable to PRC enterprise income tax at a rate of 25% during the year ended 31 December 2011 (2010: 25%), except for the following companies:

*(a) Sichuan Honghua Petroleum Equipment Co., Ltd. ("Honghua Company")*

Honghua Company is a wholly foreign-owned enterprise, and is entitled to a reduced tax rate of 12.5% during the year ended 31 December 2010. During the year ended 31 December 2011, income tax is accrued at a tax rate of 15% applicable for Hi-Tech Enterprises pursuant to the relevant PRC tax rules and regulations.

*(b) Chengdu Hongtian Electric Drive Engineering Co., Ltd. ("Hongtian Company") and Sichuan Honghua Youxin Petroleum Machinery Co., Ltd. ("Youxin Company")*

Hongtian Company and Youxin Company are recognised as entities established in the western regions of the PRC with over 70% of principal revenue generated from the encouraged business activities. These companies are entitled to a preferential income tax rate of 15% during the year ended 31 December 2010.

On 27 July 2011, the Ministry of Finance, the General Administration of Customs and the State Administration of Taxation jointly issued CaiShui [2011] No.58 which states that enterprises within encouraged industries and located in the Western Region are entitled to a preferential tax rate of 15% for the period from 1 January 2011 to 31 December 2020 ("Tax Concession"). Hongtian Company and Youxin Company are in the process of applying for the Tax Concession in order to continue to enjoy the 15% preferential income tax rate from 2011 to 2020.

*(iii) Russian Federation*

In accordance with the Russian tax legislation, Russia Honghua Co, Ltd ("Russia Honghua") is subject to corporate profits tax at a rate of 20%. No provision for Russian Profits Tax has been made as Russia Honghua did not earn any assessable profits during the year ended 31 December 2011.

*(iv) United States of America ("US")*

Honghua America LLC ("Honghua America") is treated as a partnership for US federal income tax purposes and therefore makes no provision for federal and state income taxes while the partners are responsible for the tax on their share of the taxable income or loss and any available tax credits on their income tax returns. However, Honghua America is required, among other things, to withhold US federal income tax on fixed or determinable annual or periodic US source income gains and profits allocable to its foreign partners as required under applicable US tax law. It is also required to pay withholding tax with respect to the effectively connected taxable income for a taxable year allocable to any of its foreign partners as required under applicable US tax law.

*(v) Others*

Taxation for other entities is charged at the appropriate current rates of taxation ruling in the relevant jurisdictions.

**(b) Withholding tax**

Under the PRC tax law and its Implementation Rules, dividends receivable by non-PRC resident enterprises from PRC enterprises on earnings earned since 1 January 2008 are subject to withholding tax at a rate of 10%. Deferred tax liabilities have been recongnised for undistributed retained profits of its subsidiaries established in the PRC earned since 1 January 2008 to the extent that profits are likely to be distributed in the foreseeable future.

## 9. DIVIDENDS

Dividends payable to equity shareholders of the Company attribute to the year:

| | **2011** | 2010 |
|---|---|---|
| | ***RMB'000*** | *RMB'000* |
| Final dividend proposed after the balance sheet date of HK$0.04 per share (2010: HK$Nil per share) | **104,700** | — |

The final dividend proposed after the balance sheet date has not been recognised as a liability at the balance sheet date.

## 10. EARNINGS/(LOSS) PER SHARE

**(a) Basic earnings/(loss) per share**

The calculation of basic earnings/(loss) per share is based on the profit attributable to ordinary equity shareholders of the Company of RMB167,984,000 (2010: loss of RMB184,165,000) and the weighted average number of 3,223,798,400 (2010: 3,223,790,744 shares) ordinary shares in issue during the year calculated as follows:

*Weighted average number of ordinary shares*

| | **2011** | 2010 |
|---|---|---|
| Issued ordinary shares at 1 January | **3,223,798,400** | 3,223,219,100 |
| Effect of share options exercised | **—** | 571,644 |
| Weighted average number of ordinary shares at 31 December | **3,223,798,400** | 3,223,790,744 |

**(b) Diluted earnings/(loss) per share**

The calculation of diluted earnings/(loss) per share is based on the profit attributable to ordinary equity shareholders of the Company of RMB167,984,000 (2010: loss of RMB184,165,000) and the weighted average number of ordinary shares of 3,223,908,400 shares (2010: 3,223,813,744 shares) calculated as follows:

*Weighted average number of ordinary shares (diluted)*

| | 2011 | 2010 |
|---|---|---|
| Weighted average number of ordinary shares at 31 December | **3,223,798,400** | 3,223,790,744 |
| Effect of deemed issue of shares under the Company's share option scheme for nil consideration | **110,000** | 23,000 |
| Weighted average number of ordinary shares (diluted) at 31 December | **3,223,908,400** | 3,223,813,744 |

Diluted loss per share equals to basic loss per share for the year ended 31 December 2010 because the exercise of share options would result in a decrease in the loss per share.

## 11. INVENTORIES

**(a) Inventories in the balance sheet comprise:**

| | The Group | |
|---|---|---|
| | **2011** | 2010 |
| | ***RMB'000*** | *RMB'000* |
| Raw materials | **520,732** | 826,226 |
| Work in progress | **586,965** | 606,555 |
| Finished goods | **425,912** | 422,624 |
| Goods in transit | **10,518** | 4,492 |
| | **1,544,127** | 1,859,897 |

**(b) An analysis of the amount of inventories recognised as an expense is as follows:**

| | The Group | |
|---|---|---|
| | **2011** | 2010 |
| | ***RMB'000*** | *RMB'000* |
| Carrying amount of inventories sold | **2,468,536** | 1,450,084 |
| Write-down of inventories | **19,494** | 20,776 |
| | **2,488,030** | 1,470,860 |

## 12. TRADE AND OTHER RECEIVABLES

| | The Group | |
|---|---|---|
| | **2011** | 2010 |
| | ***RMB'000*** | *RMB'000* |
| Trade receivables | **1,235,780** | 1,018,668 |
| Bills receivable | **1,700** | 4,000 |
| Less: Allowance for doubtful debts | **(140,099)** | (126,273) |
| Sub-total | **1,097,381** | 896,395 |
| Value-added tax recoverable | **223,019** | 102,348 |
| Prepayments | **120,734** | 125,406 |
| Other receivables | **121,276** | 92,959 |
| | **1,562,410** | 1,217,108 |

All of the trade and other receivables are expected to be recovered within one year.

**(a) Ageing analysis**

Included in trade and other receivables are trade receivables and bills receivable (net of allowance for doubtful debts) with the following ageing analysis as of the balance sheet date:

| | The Group | |
|---|---|---|
| | **2011** | 2010 |
| | ***RMB'000*** | *RMB'000* |
| Current | **770,419** | 704,274 |
| Less than 1 month past due | **12,017** | 7,407 |
| 1 to 3 months past due | **25,136** | 16,707 |
| More than 3 months but less than 12 months past due | **213,628** | 40,132 |
| More than 1 year past due | **76,181** | 127,875 |
| | **1,097,381** | 896,395 |

The Group maintains different billing policies for different customers based on the negotiated terms with each of the customers. The Group will bill different percentages of the contract price at different stages such as upon the signing of contracts and upon the delivery of products. The exact percentage of each part of payment varies from contract to contract. Trade receivables are due for payment upon the Group presenting the bills to the customers.

**(b) Impairment of trade receivables and bills receivable**

Impairment losses in respect of trade receivables and bills receivable are recorded using an allowance account unless the Group is satisfied that recovery of the amount is remote, in which case the impairment loss is written off against trade receivables and bills receivable directly.

The movement in the allowance for doubtful debts during the year, including both specific and collective loss components, is as follows:

| | The Group | |
|---|---|---|
| | **2011** | 2010 |
| | ***RMB'000*** | *RMB'000* |
| At 1 January | **126,273** | 124,669 |
| Provision for impairment losses | **13,826** | 1,604 |
| At 31 December | **140,099** | 126,273 |

At 31 December 2011, the Group's trade debtors and bills receivable of RMB126,273,000 (2010: RMB126,273,000) was individually determined to be impaired. The individually impaired receivables relate to customers that are in financial difficulties and management assesses the recoverability is doubtful but not remote. Consequently, specific allowances for doubtful debts of RMB126,273,000 (2010: RMB126,273,000) were recognised. The Group does not hold any collateral over these balances.

**(c) Trade receivables that are not impaired**

The ageing analysis of trade debtors and bills receivable that are neither individually nor collectively considered to be impaired are as follows:

| | The Group | |
|---|---|---|
| | **2011** | 2010 |
| Neither past due nor impaired | **770,419** | 704,274 |
| Less than 1 month past due | **12,017** | 7,407 |
| 1 to 3 months past due | **25,136** | 16,707 |
| More than 3 months but less than 12 months past due | **213,628** | 40,132 |
| More than 1 year past due | **—** | 127,875 |
| Past due but not impaired | **250,781** | 192,121 |

Receivables that were neither past due nor impaired (disclosed as current in the table given in note 12(a)) relate to a wide range of customers for whom there was no recent history of default.

Receivables that were past due but not impaired relate to a number of independent customers that have a good track record with the Group. Based on past experience, management believes that no impairment allowance is necessary in respect of these balances as there has been no history of default and the balances are still considered recoverable. The Group does not hold any collateral over these balances.

## 13. TRADE AND OTHER PAYABLES

| | The Group | |
|---|---|---|
| | **2011** | 2010 |
| | ***RMB'000*** | *RMB'000* |
| Trade payables | **596,907** | 492,616 |
| Bills payable | **289,439** | 181,425 |
| Receipts in advance | **256,804** | 399,612 |
| Other payables | **388,173** | 136,258 |
| | **1,531,323** | 1,209,911 |

Bills payable as at 31 December 2010 and 2011 were secured by certain pledged bank deposits. All of the trade and other payables are expected to be settled or recognised as income within one year or are repayable on demand.

An ageing analysis of the trade and bills payable based on the invoice date is as follows:

| | The Group | |
|---|---|---|
| | **2011** | 2010 |
| | ***RMB'000*** | *RMB'000* |
| Within 3 months | **527,180** | 373,363 |
| 3 months to 6 months | **172,924** | 138,841 |
| 6 months to 1 year | **63,170** | 39,751 |
| Over 1 year | **123,072** | 122,086 |
| | **886,346** | 674,041 |

# MANAGEMENT DISCUSSION AND ANALYSIS

During the Year, the Group's revenue amounted to approximately RMB3,485 million, representing a significant increase of 85.6% as compared to Last Year. During the Year, the Group's gross profit was approximately RMB970 million, representing an increase of 155.0% as compared to Last Year. Profit attributable to equity shareholders was approximately RMB168 million. The Board recommends a final dividend of HK$0.04 per Share.

## Market Review

As influenced by the unstable political status in the Middle East, the nuclear accident in Japan, the unsolved European debt crisis, as well as the slowdown in economic recovery of developed countries, the crude oil price continued to be volatile, resulting in wild fluctuations. However, the crude oil price has recovered from the effects of the financial crisis and has been maintaining a high level. The annual average price of crude oil futures on the New York Mercantile Exchange reached US$95.11/barrel, representing an increase of 19.5% as compared to 2010 and reached the second highest level just below the peak reached in 2008. The annual average Brent crude oil price was US$110.91/barrel, which was an historical record, representing an increase of 38.05% as compared to 2010. The surge of oil price stimulated growth in oil and gas exploration expenditures and created consistent demand growth in oil and gas drilling equipment. According to Baker Hughes, global drilling activities increased and oil and gas exploration activities fully recovered during the Year. In 2011, the average number of global active drilling rigs was 3,466 units, as compared to 3,088 units in 2008.

During the Year, the new wave of non-conventional oil and gas resources development including shale gas and coalbed methane extended from North America to other parts of the world. More and more countries and regions accelerated the progress in exploration of non-conventional oil and gas resources. In 2011, the PRC government constantly launched encouraging policies in non-conventional oil and gas resources development. Subsequent to the first tender for the exploitation right of shale gas fields launched by the Ministry of Land and Resources of the PRC in June 2011, shale gas was officially categorised as a type of newly found mineral and should be managed as an independent mineral. The exploration and development of non-conventional oil and gas resources brought enormous business opportunities to drilling equipment manufacturers.

According to statistics of RS-Plauto, the global utilisation rate of jack-up platforms gradually recovered and that of the deep-water platforms stayed at high level during the Year. The government authorities of the PRC also launched the Outline for the National Marine Science and Technology Development Planning for the 12th Five-Year Period and the Strategies for the Innovative Development of Marine Engineering Equipment Industry, creating favorable conditions for the development of the offshore engineering equipment industry.

**Business Review**

During the Year, the Group proactively developed new products, markets and businesses according to needs of clients and markets, and continued to stabilise and optimise its diversified network, product and services structures to enhance revenue growth and profitability. Meanwhile, the Group strengthened its internal corporate governance and introduced comprehensive budget control measures to strengthen cost management and corporate efficiency, so as to propel the Group's sustainable development and raise the competitiveness of its products and services.

*Sales and Marketing*

During the Year, the Group put more efforts into promotion and marketing to enhance product recognition and developed new markets and clients. Through provision of high quality products and multi-faceted value-added services, the Group continued to consolidate its client base in mature markets. During the Year, the Group facilitated and strengthened its marketing via participation in 12 large-scaled domestic and overseas exhibitions, the launch of 33 issues of print advertisements in major publications of the industry, as well as other methods.

During the Year, the Group's sales of both drilling rigs and parts and components recorded marked growth as compared to Last Year. Regarding sales of drilling rigs, the Group achieved a historical breakthrough in South America. It entered into a land drilling rig contract worth around US$240 million with PDVSA Servicios Petroleros, S.A.. The Group also obtained a contract worth approximately US$300 million from National Drilling Company in the Middle East. In the Asian market, the Group signed a drilling rig contract worth around US$100 million with SDP Services Limited. As regards to sales of parts and components, self-manufactured top drives realised both individual and supporting sales and mud pumps were sold to Western Europe.

Apart from the oil and gas engineering services project in Kazakhstan, the Group also developed its oil and gas engineering services in the PRC. The Group's two projects in Xinjiang province progressed smoothly. It utilised new products such as in-house manufactured direct top drives, direct drive mud pumps and other products in the oil and gas engineering services, which provided first-hand data for new product modification and successfully promoted its latest products.

During the Year, there was a relatively remarkable progress in the sales of offshore equipment products. The Group entered into an offshore equipment contract worth around US$9.7 million with Nautilus Minerals Niugini Limited, which allowed its offshore products to enter the global offshore equipment market.

The agreement signed between the Company's indirect wholly-owned subsidiary, Sichuan Honghua Petroleum Equipment Co., Ltd. and Shanghai Zhenhua Heavy Industry Co., Ltd. ("Zhenhua Heavy Industry") is on hold. Although the Group discussed and negotiated with Zhenhua Heavy Industry for many times, the agreement was still not able to restart during the Year. Subsequent to discussion, the management believed that the agreement is less likely to restart. Currently, the Group is conducting negotiation with Zhenhua Heavy Industry to settle the contract issues properly.

*Production, R&D and Services*

During the Year, the Group continued to implement its "localisation" strategy to further enhance its production capability. The new facilities of the Group's maintenance and services centre in Dubai commenced operation during the Year. It will become the maintenance services and sales centre of the Group in the Middle East for rig maintenance and renovation services, parts and components provision, equipment leasing and after-sales services.

During the Year, the Group obtained administration approval for its offshore equipment production base in Qidong, Jiangsu Province, the PRC. The construction, research and market development work were carried out methodically. Temporary office buildings and staff dormitories have been completed and the construction of assembly plants, coaling plants, auxiliary buildings, air compression stations and slides have commenced. Regarding R&D, the designs of the Group's jack-up platform jacking and fixation systems have obtained the approval of the American Bureau of Shipping (the "ABS"). Also, the Group established a joint venture with SBI Offshore Limited from Singapore for proactive offshore market development.

The Group always believes that innovation is the momentum for corporate development. The Group not only possesses a strong R&D expert team, but also cooperates with tertiary institutions in enhancing its R&D capability, and to maintain its leading position in the industry. During the Year, the Group successfully produced the first 10000-meter scientific land drilling rig in the PRC, which has passed the examination and final inspection by China's Administrative Office of Deep Exploitation Technology and Experimentation and Jilin University.

During the Year, the Group's 44 patent applications were approved and 1 of them was a new invention patent. As at 31 December 2011, the Group had filed 142 patent applications and 77 of them had been approved.

*Preparation for Non-conventional Gas Business Development*

To capture domestic and overseas business opportunities in large-scale non-conventional gas exploration, the Group designed new products specifically tailored to non-conventional gas exploration, including 6000HP fracturing pumps, flexible water tanks, super single pipe rigs and hybrid coiled tubing drilling rigs. Leveraging on these new products and tools, the Group introduced a high-efficiency and low-cost innovative exploration solution guided by "Exploiting gas by using gas; simultaneously producing gas and electricity; supported by distribution network; scale industrialised production; comprehensive utilisation".

The Group also proactively positioned itself for the enormous demand in fracturing in the field of shale gas development. During the Year, the Group's subsidiary set up a joint venture with Gansu Huateng Oil & Gas Equipment Manufacturing Co., Ltd. ("Gansu Huateng") and successfully extended its production chain to the fracturing equipment production industry. The joint venture will benefit from the advanced R&D capability and production technologies of the Group and Gansu Huateng in oil and gas drilling and fracturing equipment, as well as their extensive domestic and international market networks, which create strong competitiveness and synergic effects.

*Corporate Governance*

During the Year, the Group continued to implement comprehensive budget control measures and strengthened cost management. Meanwhile, it also stressed revenue and receivables management, and introduced a dynamic revenue management system which includes monthly alert and monitoring. The Group also imposed receivables control for assessment of receivables ratio so as to reduce the receivables turnover period. It also enhanced its operating procedures in warehouses and standardised inventory logistics management. The Group attained remarkable results in enhancement of production skills, procedures and material delivery, improving its cost control, product quality and production efficiency.

During the Year, the Group's profitability and operating efficiency had significant enhancement as compared to Last Year. The average inventory and average receivables turnover periods showed marked improvement. The average inventory turnover period reduced from 458 days Last Year to 247 days, while the average receivables turnover period reduced from 163 days Last Year to 104 days.

During the Year, the Group promoted environmental management of its production base, established and improved the environmental management and protection system, and added various environmental protection measures. The Group emphasised on production safety and proactively enhanced its standards. During the Year, it obtained the ISO4001/2004 Environmental Management Certification and the OHSAS18001:2007 Occupational Health and Safety Management Certificate.

*Human Resources Management*

The Group continued to launch a variety of incentive measures in internal operation and applied a performance-oriented and accountability mechanism to boost business results and operating efficiency. In order to enhance operating efficiency, the Group optimised and adjusted the organisation structure, conducted organisational consolidation through resources sharing and personnel structure streamlining. It also arranged specific activities encouraging collaboration of the management and employees in modifying the working environment.

During the Year, the Group was committed to the establishment of a training centre and system, and upgraded the vocational skills of its employees through trainings and skill contests. The Group conducted a total of 367 training courses, including middle management trainings, orientation trainings, as well as streamlined management and drilling project management trainings.

## Prospects

It is anticipated that the harsh macro-economic environment will continue in 2012. Major markets such as Central America and Europe will continue to be weak, while the growth rate of the PRC and other emerging markets will slow down. Nevertheless, the oil and gas drilling equipment industry will still offer numerous business opportunities. The nuclear accident in Japan has urged other nations in the world to reassess the use of nuclear energy and will stimulate more oil and gas demand from different nations and enterprises, which will lead to an increase in exploration and production expenditures. Barclay's Capital estimates that the global oil and gas exploration and production expenditure will hit a new high in 2012 and the total investment will reach US$598 billion, representing an increase of 10% as compared to 2011. The political status in North Africa and other regions is gradually becoming stable, encouraging the systematic recovery of oil drilling activities. High oil prices will also increase the economic value of oil and gas exploration and production, and bring more demand for oil drilling equipment.

Currently, conventional crude oil and natural gas resources from land are limited and the proportion of mature oil and gas fields is constantly increasing. It leads to increasing input of more countries and regions in exploration and mining of the immense non-conventional and offshore oil and gas deposits, and creates opportunities for the Group's business development in the offshore and shale gas equipment sectors. Leveraging on the Group's robust foundation established through years, its high quality products with wide market recognition and its strong R&D capability, the Group will endeavor to maintain stable growth of its core business and will be well-positioned in capturing business opportunities in the offshore engineering equipment and non-conventional oil and gas equipment industries.

In the R&D field, the Group will continue to conduct modification and innovation in its key technologies and core products, to bring new profit driver of the Group's future development. The Group will proactively implement a variety of cost control measures, so as to raise quality of its products and services and consolidate its supply chain. In view of personnel management, the Group will strive to enhance its management standard and provide sufficient training resources for its new generation of management, motivating both corporate and staff development.

In 2012, the Group will endeavor to push ahead with its core business sales, to develop the new offshore and oil and gas engineering services businesses, as well as to boost operating efficiency and increase income sources, so as to sharpen the competitive edges and maintain the sustainable development of the Group and create more returns for the shareholders of the Company.

## FINANCIAL REVIEW

During the Year, the Group's gross profit and profit attributable to shareholders amounted to approximately RMB970 million and approximately RMB168 million respectively, as compared to a gross profit and loss attributable to shareholders of approximately RMB380 million and RMB184 million respectively Last Year. Gross margin and net profit margin amounted to 27.8% and 4.8% respectively. During the Year, the increase in gross profit and increase in profit attributable to shareholders were mainly attributable to the gradual recovery of demands of the global drilling equipment, the Group's efforts in proactive market development and control of cost and expenses.

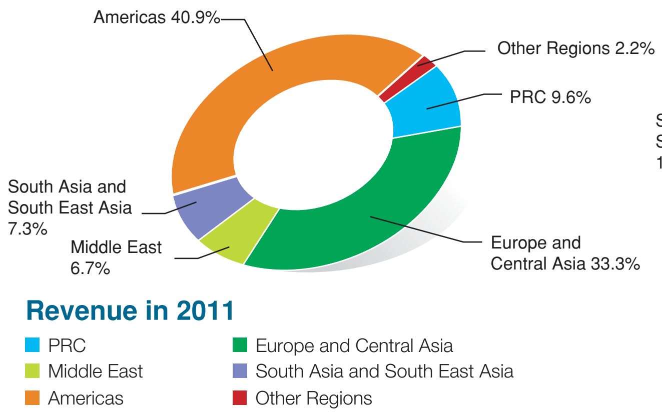
### Turnover

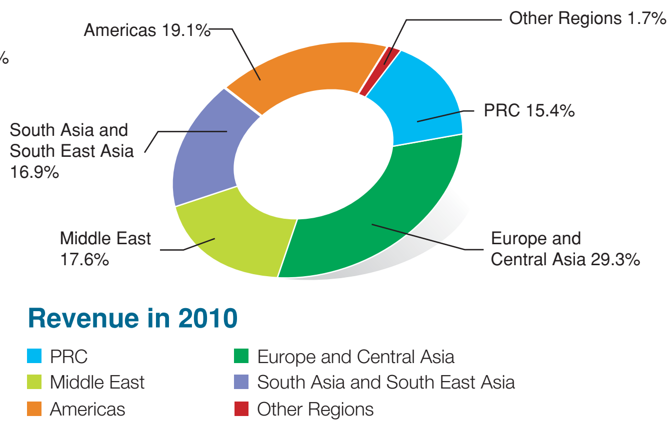
During the Year, the Group's turnover amounted to approximately RMB3,485 million, representing an increase of 85.6% as compared to approximately RMB1,878 million Last Year. The increase was mainly attributable to the gradual recovery of requirements of the global drilling equipment and the

Group's efforts in proactive market development. Among which, the number of drilling rigs sold increased from 23 units in 2010 to 48 units during the Year.

During the Year, revenue by geographical areas were as follows: revenue from exports amounted to approximately RMB3,150 million, accounting for approximately 90.4% of the Group's total revenue, representing an increase of approximately RMB1,561 million as compared to Last Year. Among which, sales from the Americas market and the European and Central Asian markets recorded a marked increase of approximately 298.3% and 111.0% respectively. Sales from the Middle Eastern market and the South Asian and South East Asian markets as well as other regions were similar to Last Year. Revenue from the PRC market also recorded a growth as compared to Last Year.

## Revenue by Geographical Areas




| | **For the year ended 31 December 2011** | | | For the year ended 31 December 2010 | | | **2011 VS 2010** | |
|---|---|---|---|---|---|---|---|---|
| **By Product Category** | **Revenue** ***RMB'000*** | **Proportion** ***(%)*** | **Quantity** ***(Unit)*** | Revenue *RMB'000* | Proportion *(%)* | Quantity *(Unit)* | **Change** ***RMB'000*** | **Change** ***(%)*** |
| Digitally-controlled Rigs | **2,415,466** | **69.3%** | **43** | 1,300,345 | 69.2% | 21 | 1,115,121 | 85.8% |
| Conventional Rigs | **127,537** | **3.7%** | **5** | 155,467 | 8.3% | 2 | (27,930) | (18.0%) |
| Subtotal | **2,543,003** | **73.0%** | **48** | 1,455,812 | 77.5% | 23 | 1,087,191 | 74.7% |
| Mud Pumps | **167,803** | **4.8%** | **168** | 110,841 | 5.9% | 100 | 56,962 | 51.4% |
| Other Parts and Components | **694,210** | **19.9%** | | 311,278 | 16.6% | | 382,932 | 123.0% |
| Subtotal | **862,013** | **24.7%** | **168** | 422,119 | 22.5% | 100 | 439,894 | 104.2% |
| Offshore Rigs and Parts and Components | **80,030** | **2.3%** | | — | — | | 80,030 | N/A |
| Total | **3,485,046** | **100.0%** | | 1,877,931 | 100.0% | | 1,607,115 | 85.6% |

Products of the Group comprise of land drilling rigs and parts and components as well as offshore rigs and parts and components.

During the Year, revenue from land drilling rigs and parts and components were approximately RMB2,543 million and RMB862 million respectively, representing an increase of 74.7% and 104.2% respectively as compared to RMB1,456 million and RMB422 million Last Year. Revenue from offshore rigs and parts and components were approximately RMB80 million, mainly due to the Group's sale of one offshore drilling module (2010: Nil).

Land drilling rigs comprise digitally-controlled land rigs and conventional land rigs, sales of which amounted to approximately RMB2,415 million and RMB128 million respectively. The increase in revenue from and drilling rigs was mainly due to the increase in sales volume of drilling rigs from 23 units Last Year to 48 units during the Year.

The increase in revenue from parts and components was mainly due to the Group's breakthrough in sales of new products and proactive market development. Among which, 4 units of self-manufactured direct top drives were sold and contributed to revenue of approximately RMB37 million. Rig modification and processing services contributed to revenue of approximately RMB118 million. The sales volume of mud pumps increased from 100 units Last Year to 168 units during the Year.

**Cost of Sales**

During the Year, the Group's cost of sales was approximately RMB2,515 million, as compared to RMB1,497 million Last Year.

**Gross Profit and Gross Margin**

During the Year, the Group recorded a gross profit of approximately RMB970 million, representing an increase of 155.0% or RMB590 million as compared to Last Year. Gross profit from drilling rigs amounted to RMB835 million, representing an increase of 197.5% as compared to last year. Gross profit from digitally-controlled rigs and conventional rigs were RMB817 million and RMB18 million respectively, representing an increase of 231.5% and decrease of 46.7% as compared to Last Year. Gross profit from parts and components amounted to approximately RMB112 million, representing an increase of 12.2% as compared to Last Year. Gross profit from offshore rigs and parts and components were RMB23 million (2010: Nil).

During the Year, the Group's overall gross margin was 27.8%, representing an increase of 7.5 percentage points as compared to that of Last Year. The increase was mainly due to the Group's breakthrough in sales of new products, the strengthening of cost control and proactive market development.

**Other Net Income/Loss**

During the Year, the Group's other net income amounted to approximately RMB60.01 million, as compared to that of other net loss of RMB5.27 million Last Year. The significant increase was mainly attributable to the gains on liquidation of a subsidiary and the gains from using forward foreign exchange contracts.

## Expenses in the Year

During the Year, the Group's selling expenses and general and administrative expenses amounted to approximately RMB794 million, representing an increase of RMB273 million or 52.4% as compared to approximately RMB521 million Last Year. The increase was mainly due to an increase in transportation costs and other related expenses caused by sales increase. The expenses ratio was 22.8%, representing a decrease of 4.9 percentage points as compared to 27.7% Last Year.

During the Year, the Group's net finance expenses amounted to approximately RMB50 million, as compared to that of RMB59 million Last Year. The decrease was mainly attributable to the Group recorded a net exchange loss from approximately RMB34 million as compared to that of RMB43 million Last Year.

## Share of Profit from Jointly Controlled Entities

During the Year, the Group's share of profit from jointly controlled entities amounted to approximately RMB0.29 million, representing a decrease in share of profit of RMB2.51 million as compared to Last Year, which was mainly due to the increase in depreciation cost of plants of Egyptian Petroleum HH Rigs Manufacturing Co. S.A.E., which were transformed into fixed assets during the Year.

## Share of Profit from an Associate

During the Year, the Group's share of profit from an associate amounted to approximately RMB5.4 million, while no such investment Last Year.

## Profit/Loss before Taxation

During the Year, the profit before taxation of the Group amounted to approximately RMB199 million, as compared to loss before taxation of approximately RMB176 million Last Year. The profit was mainly due to the significant increase in sales and gross profit.

## Income Tax Expenses/Credit

During the Year, the Group's income tax expenses amounted to approximately RMB27.77 million, as compared to income tax credit of approximately RMB4.37 million Last Year. This was mainly due to the Group's profit before taxation during the Year while a loss before taxation Last Year.

## Profit/Loss for the Year

During the Year, the Group's profit amounted to approximately RMB171 million, as compared to loss of approximately RMB172 million Last Year. Among which, profit attributable to equity shareholders of the Company was approximately RMB168 million, while profit attributable to non-controlling interests was approximately RMB3 million. Net profit margin during the Year amounted to approximately 4.8%, as compared to net loss margin of 9.8% Last Year. This was mainly attributable to the significant increase of gross margin and a decrease of expenses ratio.

## Earnings before Interest, Taxes, Depreciation and Amortisation ("EBITDA") and EBITDA Margin

During the Year, EBITDA amounted to approximately RMB356 million, as compared to loss of RMB27 million Last Year. It was mainly due to the Group's business turnaround during the Year. EBITDA margin was 10.2%, as compared to EBITDA loss margin of 1.5% Last Year.

## Dividend

For the Year ended 31 December 2011, the Directors recommend a final dividend of HK$0.04 per Share. Subject to the approval at the forthcoming Annual General Meeting of the Company, the final dividend will be payable on or around 18 June 2012 to the shareholders of the Company whose names appear on the register of members of the Company as on 1 June 2012.

## Source of Capital and Borrowings

The Group's principal sources of capital include listing proceeds, cash from operations and bank borrowings.

At 31 December 2011, the Group's bank borrowings amounted to approximately RMB880 million, representing an increase of RMB253 million as compared to that at 31 December 2010. Among which, borrowings repayable within one year amounted to approximately RMB500 million, representing an increase of RMB56 million as compared to that at 31 December 2010.

## Deposit and Cash Flow

At 31 December 2011, the Group's cash and cash equivalents amounted to approximately RMB852 million, representing a decrease of approximately RMB151 million as compared to that at 31 December 2010. During the Year, the Group's operating cash inflow amounted to approximately RMB214 million, which was mainly due to improvement in receivables and use of inventory; cash outflow from investing activities amounted to approximately RMB594 million, which was mainly due to increase in fixed assets, construction in progress and investment in financial products; and cash inflow from financing activities amounted to approximately RMB244 million, which was mainly due to increase in long-term loans.

## Assets Structure and Changes Thereof

At 31 December 2011, the Group's total assets amounted to approximately RMB6,693 million, representing an increase of RMB698 million as compared to that at 31 December 2010. The increase was mainly due to the increase in profit and investments during the Year. Among which, current assets amounted to approximately RMB4,810 million, which were mainly cash and cash equivalents, trade receivables and inventories, accounting for 71.9% of total assets; non-current assets amounted to approximately RMB1,882 million, accounting for approximately 28.1% of total assets.

### Liabilities

At 31 December 2011, the Group's total liabilities amounted to approximately RMB2,518 million, representing an increase of approximately RMB594 million as compared to that at 31 December 2010. Among which, current liabilities amounted to approximately RMB2,119 million, accounting for approximately 84.2% of total liabilities; non-current liabilities amounted to approximately RMB399 million, accounting for approximately 15.8% of total liabilities. At 31 December 2011, the Group's gearing ratio was approximately 37.6%.

### Total Equity

At 31 December 2011, total equity amounted to RMB4,175 million, representing an increase of RMB104 million as compared to that at 31 December 2010. Total equity attributable to equity shareholders of the Company amounted to approximately RMB4,059 million, representing an increase of RMB95 million as compared to that at 31 December 2010. Non-controlling interests amounted approximately to RMB116 million, representing an increase of RMB9 million as compared to that at 31 December 2010. Net asset value reached approximately RMB1.26 per Share. During the Year, the Group's earnings per Share was approximately RMB5.21 cents.

### Contingent Liabilities and Pledge

The Group's contingent liabilities were caused by legal claims generated from ordinary course of business. At 31 December 2011, the major litigations of the Group and its subsidiaries were mainly caused by disputes with natural persons, regional former sales agents and former employees. As at 31 December 2011, pursuant to the legal advices of the Group's external consultants, the management considered that these claims are not likely to cause damage to the Group's economic interests. Therefore, no compensation provision is made for these claims and sufficient provision in legal costs in respect to these claims has been made.

As at 31 December 2011, Honghua Holdings Limited ("Honghua Holdings") has issued a financial guarantee to Chengdu Investment Holding Group, which is a shareholder of Chengdu Jinkong Financial Leasing Co., Ltd. The maximum liability of Honghua Holdings as at 31 December 2011 under the single guarantee issued is the outstanding amount of the facility drawn down by the associate of RMB25,710,000 (2010: Nil).

At 31 December 2011, the Group has pledged bank deposits of approximately RMB66 million, representing an increase of approximately RMB37 million as compared to that at 31 December 2010.

### Capital Expenditure, Major Investment and Capital Commitments

During the Year, capital expenditure of the Group on infrastructure and technical improvements amounted to approximately RMB605 million, representing an increase of approximately RMB419 million as compared to Last Year. This was mainly attributable to the input in the infrastructure construction for the offshore project and 2 rigs for the oil and gas engineering services.

At 31 December 2011, the Group had capital commitments of approximately RMB1,600 million, which will be used for the construction of Jiangsu Qidong offshore manufacturing base.

**Foreign Currency Risk**

The Group owns certain foreign currency deposits. At 31 December 2011, the Group's foreign currency deposits were equivalent to approximately RMB147 million, trade and other receivables in foreign currency were equivalent to approximately RMB816 million. Exports and foreign currencies settled business exposed the Group to exchange risk.

**Use of Proceeds from the Initial Public Offerings**

After the reduction of the related expenses, total capital raised from the initial public offerings was approximately HK$2,958 million. In order to strengthen the Group's operation, the Group adjusted the use of parts of the proceeds. As at 31 December 2011, the adjusted use of proceeds are as follows: proceeds of HK$975 million to be used for offshore project, of which HK$714 million has been incurred; proceeds of HK$592 million to be used for the enlargement of oil and gas explorations, provision of products and services, oil and gas engineering services and oil and gas resources exploration, as well as other business which can create profitability for the Group, of which HK$104 million has been incurred; proceeds of HK$354 million to be used for production capacity expansion and R&D expenses, of which HK$354 million has been incurred; proceeds of HK$1,037 million to be used as working capital and day to day expenses, of which HK$1,037 million has been incurred.

**Employee Remuneration and Benefits**

During the Year, the average number of the Group's employees was 3,907. The total remuneration and benefits amounted to approximately RMB391 million. The Group continued to optimise its employment structure and implemented a variety of incentive measures. The Group also strictly implemented its internal assessment and performance management schemes, so as to strengthen its organisational efficiency and executive management. The Group adjusted the remuneration of certain key employees based on the performances of its subsidiaries, individual work performance, external human resources market conditions and the economic environment. The Group also provided sufficient welfare and benefits to its employees, including professional training schemes to enhance their vocational skills, knowledge and sense of belonging. The Group also established share option scheme and restricted share award scheme as a long-term incentive program for its core and high caliber staff, so as to propel the long-term collaborative development of the Group and its employees. The Group strives to enhance the working incentives and working ability of its employees and raise staff morale, in order to improve the overall competitiveness of the Group.

## PURCHASE, SALE OR REDEMPTION OF COMPANY'S LISTED SECURITIES

During the Year, neither the Company nor any of its subsidiaries has purchased, sold or redeemed any of the Company's Shares.

## CLOSURE OF REGISTER OF MEMBERS

The register of members of the Company will be closed during the following periods:

(i) from Wednesday, 16 May 2012 to Tuesday, 22 May 2012, both days inclusive, for the purpose of ascertaining shareholders' entitlement to attend and vote at the Annual General Meeting. In order to be eligible to attend and vote at the Annual General Meeting, all transfer documents accompanied by the relevant share certificates mush be lodged for registration with the Hong Kong branch share registrar and transfer office of the Company, Computershare Hong Kong Investor Services Limited, at Shops 1712–1716, 17th floor, Hopewell Centre, 183 Queen's Road East, Wanchai, Hong Kong for registration not later than 4:30 p.m. on Tuesday, 15 May 2012; and

(ii) from Monday, 28 May 2012 to Friday, 1 June 2012, both days inclusive, for the purpose of ascertaining shareholder's entitlement to the proposed final dividend. In order to establish entitlements to the proposed final dividend, all transfer documents accompanied by the relevant share certificates mush be lodged for registration with the Hong Kong branch share registrar and transfer office of the Company, Computershare Hong Kong Investor Services Limited at the address as set out in sub-paragraph (i) above not later than 4:30 p.m. on Friday, 25 May 2012.

During the periods mentioned in sub-paragraphs (i) and (ii) above, no transfers of shares will be registered.

## AUDIT COMMITTEE

The Audit Committee comprises all the Independent Non-executive Directors with written terms of reference in compliance with the Listing Rules. The Audit Committee is responsible for reviewing and supervising financial reporting process and internal control systems and providing advices and recommendations to the Board. The Audit Committee shall hold at least two meetings a year and review opinions of internal auditors, matters in respects of internal control, risk management and financial reporting. The Audit Committee has reviewed financial results of the Group for the year ended 31 December 2011 and the accounting principles and practices adopted by the Group during the Year.

## COMPLIANCE WITH THE CODE ON CORPORATE GOVERNANCE PRACTICES

The Company has complied with the principles as set out in the CG Code since listing on 7 March 2008 (the "Listing Date"), except the following deviations:

Based on the Rule A.2.1 of CG Code, the positions of Chairman and President (Chief Executive Officer) should be separated and should not be performed by the same individual. Mr. Zhang Mi is the Chairman of the Board and President (Chief Executive Officer) of the Company. Mr. Zhang Mi is the main founder of the Group and has extensive experiences in the industry and related industries. In the opinion of the Board, the vesting of duties of Chairman of the Board and President (Chief Executive Officer) of the Company to Mr. Zhang Mi would provide a strong and consistent leadership and allow effective planning and execution of business decisions and strategies, as well as ensure the interests of the shareholders of the Company as a whole. On the other hand, the balance between powers and duties could be ensured through the operation of the Board and the committees under it.

The Company will continue to review the effectiveness of the Group's corporate governance structure and consider whether it needs to make any changes, including the separation of duties of Chairman of the Board and President (Chief Executive Officer) of the Company.

## MODEL CODE FOR SECURITIES TRANSACTIONS BY DIRECTORS

The Company has adopted a set of Code for Securities Trading on 21 January 2008, the strict level of which is no less than that of the Model Code. After the specific enquiry by the Company, all the Directors have confirmed that they have complied with the standards specified in both of the Code for Securities Trading and the Model Code from the Listing Date to 31 December 2011.

## PUBLICATION OF ANNUAL RESULTS ANNOUNCEMENT AND ANNUAL REPORT FOR 2011

This announcement is published on both the websites of the Company (www.hh-gltd.com) and of the Stock Exchange (www.hkexnews.hk). The annual report of the Company for the year ended 31 December 2011 will be dispatched to shareholders of the Company and published on the aforesaid websites in due course.

## DEFINITION

| | | |
|---|---|---|
| "Annual General Meeting" | : | the annual general meeting of the Company which will be held on Tuesday, 22 May 2012 |
| "Audit Committee" | : | the audit committee of the Company |
| "Board" | : | the Board of Directors of the Company |
| "Code for Securities Trading" | : | code for securities trading adopted by the Company |
| "Company" or "Honghua Group" | : | Honghua Group Limited |
| "CG Code" | : | Code on Corporate Governance Practices set out in Appendix 14 to the Listing Rules |

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| "Directors" | : | directors of the Company |
| "During the Year" | : | For the year ended 31 December 2011 |
| "Group" | : | the Company and its subsidiaries, its associate and its jointly controlled entities |
| "HK$" or "HK dollars" | : | Hong Kong dollars, the lawful currency of Hong Kong |
| "Hong Kong" | : | the Hong Kong Special Administrative Region of the PRC |
| "Last Year" | : | For the year ended 31 December 2010 |
| "Listing Rules" | : | the rules governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (as amended from time to time) |
| "Model Code" | : | Model Code for Securities Transactions by Directors of Listed Issuers set out in Appendix 10 to the Listing Rules |
| "PRC" or "China" | : | the People's Republic of China, unless the context requires otherwise, reference in this announcement of the PRC or China excludes Hong Kong, the Macau Special Administrative Region of the PRC and Taiwan, China |
| "RMB" | : | Renminbi, the lawful currency of the PRC |
| "Share(s)" | : | ordinary shares issued by the Company, with a nominal value of HK$0.10 each |
| "Stock Exchange" | : | The Stock Exchange of Hong Kong Limited |
| "US$" | : | United States dollars, the lawful currency of the United States of America |

On behalf of the Board of
**Honghua Group Limited**
*Chairman*
**Zhang Mi**

Hong Kong, 20 March 2012

*As at the date of this announcement, the Executive Directors of the Company are Mr. Zhang Mi (Chairman), Mr. Ren Jie and Mr. Liu Zhi; the Non-executive Directors of the Company are Mr. Siegfried Meissner and Mr. Huang Dongyang; and the Independent Non-executive Directors of the Company are Mr. Liu Xiaofeng, Mr. Qi Daqing, Mr. Tai Kwok Leung Alexander, Mr. Chen Guoming, Mr. Shi Xingquan and Mr. Guo Yanjun.*