宏华集团有限公司
HONGHUA GROUP LIMITED

(incorporated in the Cayman Islands with limited liability)

Stock Code: 196

New equipment specialized in shale gas by
the innovative idea of “exploiting gas by using gas,
simultaneously producing gas and electricity”

2011 ANNUAL REPORT

CONTENTS

FINANCIAL HIGHLIGHTS

	2011 RMB'000	2010 RMB'000	Changes
Operating results			
Turnover	**3,485,046**	1,877,931	85.6%
Profit/(loss) from operations	**243,856**	(119,803)	
Profit/(loss) before taxation	**199,212**	(176,443)	
Profit/(loss) attributable to equity shareholders of the Company	**167,984**	(184,165)	
Figures per share			
Earnings/(loss) per share-Basic and Diluted (RMB cents)	**5.21**	(5.71)	
Financial position			
Total non-current assets	**1,882,332**	1,354,893	38.9%
Total current assets	**4,810,368**	4,639,753	3.7%
Total assets	**6,692,700**	5,994,646	11.6%
Total current liabilities	**2,119,137**	1,729,051	22.6%
Total non-current liabilities	**398,705**	194,804	104.7%
Total liabilities	**2,517,842**	1,923,855	30.9%
Total equity	**4,174,858**	4,070,791	2.6%
Key financial ratios*			
Gross Margin	**27.8%**	20.3%	7.5%
Net Margin	**4.8%**	(9.8%)	
Return on average assets	**2.6%**	(2.9%)	
Return on average equity	**4.2%**	(4.5%)	
Current Ratio	**2.27**	2.68	(0.41)
Quick ratio	**1.54**	1.61	(0.07)
Total debt/Total assets	**13.1%**	10.4%	2.7%
Total liabilities/Total assets	**37.6%**	32.1%	5.5%

* *Earnings exclude non-controlling interests*
Equity excludes non-controlling interests

CORPORATE INFORMATION

BOARD OF DIRECTORS

EXECUTIVE DIRECTORS

Zhang Mi *(Chairman)*
Ren Jie
Liu Zhi

NON-EXECUTIVE DIRECTORS

Siegfried Meissner
Huang Dongyang

INDEPENDENT NON-EXECUTIVE DIRECTORS

Liu Xiaofeng
Qi Daqing
Tai Kwok Leung, Alexander
Chen Guoming
Shi Xingquan
Guo Yanjun (appointed with effect from 20 June 2011)
Wang Li (resigned with effect from 20 June 2011)

SECRETARY OF BOARD OF DIRECTORS

Liu Gangqiang

BOARD COMMITTEE

AUDIT COMMITTEE

Qi Daqing *(Committee Chairman)*
Liu Xiaofeng
Tai Kwok Leung, Alexander
Chen Guoming
Shi Xingquan
Guo Yanjun (appointed with effect from 20 June 2011)
Wang Li (resigned with effect from 20 June 2011)

CORPORATE GOVERNANCE COMMITTEE

Liu Xiaofeng *(Committee Chairman)*
Qi Daqing
Tai Kwok Leung, Alexander
Chen Guoming
Shi Xingquan
Guo Yanjun (appointed with effect from 20 June 2011)
Wang Li (resigned with effect from 20 June 2011)

REMUNERATION COMMITTEE

Liu Xiaofeng *(Committee Chairman)*
Zhang Mi
Qi Daqing

STRATEGIC INVESTMENT AND RISK CONTROL COMMITTEE

Zhang Mi *(Committee Chairman)*
Ren Jie
Liu Zhi
Huang Dongyang
Shi Xingquan
Wang Li (resigned with effect from 20 June 2011)

NOMINATION COMMITTEE (formed on 17 January 2012)

Zhang Mi *(Committee Chairman)*
Liu Xiaofeng
Qi Daqing

JOINT COMPANY SECRETARIES

Liu Gangqiang
Corinna Leung

LEGAL ADVISORS

AS TO HONG KONG LAW

King & Wood Mallesons

AS TO PRC LAW

King & Wood Mallesons

AS TO CAYMAN ISLANDS LAW

Appleby

PRINCIPAL BANKERS

Bank of China Limited
China Construction Bank Corporation
China Merchants Bank Co., Ltd.
Industrial and Commercial Bank of China Limited
The Export-Import Bank of China
Bank of Communications Co., Ltd.
Industrial and Commercial Bank of China (Asia) Limited
The Hongkong and Shanghai Banking Corporation Limited
Industrial Bank Co., Ltd.

CORPORATE INFORMATION

AUDITOR

KPMG
Certified Public Accountants

REGISTERED OFFICE

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PO Box 1350
Grand Cayman, KY1-1108
Cayman Islands

HEAD OFFICE

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Jinniu District
Chengdu, Sichuan 610036
PRC

PLACE OF BUSINESS IN HONG KONG

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39 Gloucester Road
Wan Chai
Hong Kong

PRINCIPAL SHARE REGISTRAR AND TRANSFER OFFICE

Appleby Trust (Cayman) Ltd.
Clifton House,75 Fort Street
PO Box 1350
Grand Cayman, KY1-1108
Cayman Islands

HONG KONG BRANCH SHARE REGISTRAR AND TRANSFER OFFICE

Computershare Hong Kong
Investor Services Limited
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17th Floor Hopewell Centre
183 Queen's Road East
Wan Chai
Hong Kong

STOCK CODE

The Stock Exchange of Hong Kong Limited: 0196

WEBSITE

http://www.hh-gltd.com

CHAIRMAN'S STATEMENT

To achieve sustainable growth,
To realize win-win situation,
To overcome all challenges,
To propel the new development
in the second decade!

Zhang Mi
CHAIRMAN

DEAR SHAREHOLDERS AND INVESTORS,

On behalf of the Board of the Group, I am pleased to announce the annual results for the year ended 31 December 2011.

FINANCIAL HIGHLIGHTS

During the Year, the Group recorded a revenue of approximately RMB3,485 million, representing a significant increase of 85.6% as compared to approximately RMB1,878 million 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 shareholders amounted to RMB168 million, as compared to a loss of approximately RMB184 million last year.

DIVIDEND

The Board proposed to pay a final dividend of HK$0.04 per Share, subject to approval at the forthcoming annual general meeting of the Company. The final dividend is payable on or around 18 June 2012 to the Shareholders whose names appear on the register of members of the Company as on 1 June 2012.

BUSINESS REVIEW

During the Year, although the slowdown in economic growth of developed countries cast a shadow over oil and gas demand, the stable economic growth of emerging economic bodies and geopolitical risks served as a momentum for surge in oil prices, leading to a volatile and high global oil price. Meanwhile, many countries and regions begin to stress on and accelerate exploration and exploitation of non-conventional energy resources such as shale gas and coalbed methane, which in turn increases the demand for drilling equipment and provides enormous opportunities for the Group's development.

During the Year, the Group continued to execute its forward sales and global deployment strategy. It strived to maintain close communications and cooperation with customers so as to understand their needs. The Group's brand recognition was enhanced while its revenue recorded remarkable growth. Leveraging on its subsidiaries in North America and the Middle East, the Group proactively developed the domestic markets and has begun to obtain encouraging results. During the Year, the Group entered into a land drilling rig contract worth around US$240 million with PDVSA Servicios Petroleros, S.A., a subsidiary of Petróleros de Venezuela, S.A. It also obtained a cluster land drilling rig contract of approximately US$300 million from the UAE-based National Drilling Company.

Confronted with increasing costs and appreciation of the Renminbi, the Group tightened inventory control and adopted a variety of cost control measures to streamline its operations and optimize its efficiency, so as to effectively use and add value to its assets. Meanwhile, the Group insisted on innovation of product R&D and introduced safe and energy-saving products, maintaining the Group's core competitiveness in the market with increasingly intensified homogeneous competition. During the Year, the Group's gross margin surged and its financial performance recorded a significant improvement as compared to 2010.

During the Year, the Group took a step forward to stabilize and optimize its product and services structure, and proactively propelled the synergistic development of its equipment production, resource exploration and engineering services businesses. During the Year, the offshore production base in Qidong, Jiangsu, the PRC obtained administration approval. The construction and research works were carried out smoothly. The oil and gas engineering services projects in Kazakhstan and Xinjiang fully commenced. The Group also proactively positioned itself for development in shale gas exploration in terms of equipment, technologies and solutions.

Moreover, the Group invested in the Chengdu Jinkong Financial Leasing Co. Ltd. and established subsidiaries with SBI Offshore Limited and Gansu Huateng Petroleum Equipment Co., Ltd. ("Gansu Huateng"). These subsidiaries will contribute to the Group's design and production of new products, service chain extension and development of new businesses, bringing more income sources to the Group.

PROSPECT

Looking forward, in 2012, following the recovery of oil exploration activities and the increasingly intensified homogeneous competition, the Group will face more opportunities and challenges. In the future, the Group will streamline its operating procedures, enrich its product mix and services, and enhance the organizational structure and human resources system, so as to lay a solid development foundation and fully motivate the long-term development of the Group's multi-faceted business related to oil and gas drilling equipment.

Regarding internal management, the Group will fully implement lean production mechanism and process management. Moreover, the Group will constantly conduct in-depth and micro-modification in management of human resources, system and procedures, marketing and sales, budget control, cost control, quality control, operating efficiency, R&D, as well as establishment of corporate culture. The Group will fully utilize resources to upgrade operating efficiency and cut costs.

The Group will continue to strengthen production and operating management and proactively search for quality business resources to develop and strengthen the existing business. The Group will also strive to enhance its overall profitability and realize its long-term sustainable development strategy, so as to create more returns for Shareholders and to propel its development in the second decade.

ACKNOWLEDGEMENT

On behalf of the Board, I would also like to take this opportunity to sincerely thank the management team and employees for their strenuous contribution to the Group throughout the year. Furthermore, I would like to express my gratitude to all customers, vendors, partners and Shareholders for their trust and support. In the coming year, we will continue the close cooperation and create better results for the Group, so as to bring maximized returns to the Shareholders.

Chairman
Zhang Mi
Hong Kong, 20 March 2012

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, HongHua Company 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 jacking and fixation systems of the Group's jack-up 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 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 remarkable 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 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

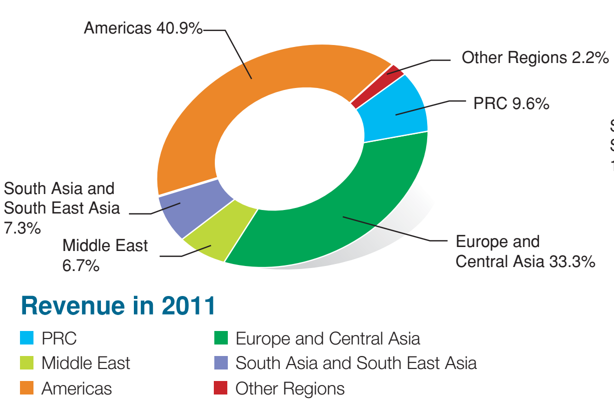
During the Year, the Group's gross profit and profit attributable to shareholders amounted to approximately RMB970 million and approximately RMB168 million respectively, as compared to a gross profit and loss attributable to shareholders of approximately RMB380 million and RMB184 million respectively 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.

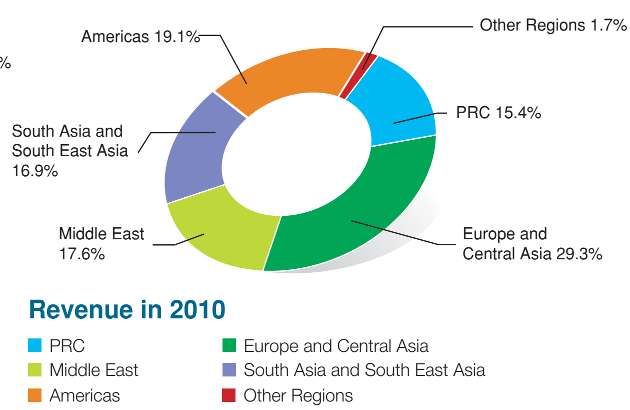
TURNOVER

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.

BY GEOGRAPHICAL AREAS





By Product Category	For the year ended 31 December 2011			For the year ended 31 December 2010			2011 VS 2010	
	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 (2010: Nil).

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 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

Details of contingent liabilities are set out in Note 36 to the financial statements of 2011 annual report.

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.

BIOGRAPHICAL DETAILS OF DIRECTORS AND SENIOR MANAGEMENT

EXECUTIVE DIRECTORS

Mr. Zhang Mi (張弭先生), aged 55, has been Chairman of the Company and an Executive Director since June 2007. He is also President of the Company.

Positions held by Mr. Zhang in the Company's subsidiaries are set forth in the table below.

Subsidiary	**Position**	**Term of Office**
Honghua Holdings Limited	director	Since 18 August 2006
	chairman, and chief executive officer	Since 8 September 2009
Sichuan Honghua Petroleum Equipment Co.,Ltd.	chairman	Since 31 December 1997 until 31 December 2011
	director	Since 31 December 1997
	general manager	Since 31 December 1997 until 18 January 2010
Honghua International Co., Ltd.	chairman	Since 13 January 2004
Honghua Offshore Oil & Gas Equipment (Jiangsu) Co., Ltd.	chairman	Since 8 June 2009
	general manager	Since 8 June 2009 until 25 September 2011
Shanghai Honghua Offshore Oil & Gas Equipment Co., Ltd.	executive director	Since 9 September 2009
Honghua (China) Investment Co., Ltd.	chairman, and general manager	Since 14 January 2010
Newco (H.K.) Limited	director	Since 15 April 2008 until 22 September 2009
Honghua Oil & Gas Engineering Services Co., Ltd.	director	Since 14 April 2009
Alpha Advance Limited	director	Since 10 July 2009
Honghua America, LLC.	chairman	Since 11 October 2004
Egyptian Petroleum HH Rigs Manufacturing CO.S.A.E.	director	Since 26 April 2007
Sichuan Hongcheng Business Trading Co., Ltd. (was dissolved on 8 August 2011)	executive director	Since 16 April 2008 until 8 August 2011
HS OFFSHORE PTE. LTD	director	Since 27 July 2011
Gansu Hongteng Oil & Gas Equipment Manufacturing Co., Ltd.	director	Since 28 December 2011

Mr. Zhang graduated from the Sichuan Petroleum Administration Vocational University in 1982, with a diploma in machinery manufacture, design and equipment. He graduated from the Party Institute of Sichuan Provincial Committee Correspondence College in 1998, with a degree in Economics and Management. In 2004 he then obtained a senior engineer qualification granted by the Committee for Evaluation of Senior Technical Positions of the China National Petroleum Corp.. He has been receiving special subsidies granted by the State Council of the PRC government since February 2007, for his significant contribution to the development of machinery engineering in the PRC.

Mr. Zhang is particularly involved in enhancing the Company's technological innovation. Mr. Zhang is responsible for the development of the ZJ70LC drilling rig. He is also responsible for the development of the digitally-controlled VFD rig (DBS), the first of its kind in China. The DBS has been included in the State Critical Technological Equipment Innovation Research Project (國家重大技術裝備創新研製項目), the State Key New Products (國家重點新產品) and the National Torch Plan Project (國家級火炬計劃項目). In 2005, Mr. Zhang was awarded the Sichuan Province Prize for Outstanding Talent in Innovation (四川省第三屆傑出創新人才獎), by the Sichuan Provincial Party Committee and the Sichuan Provincial People's Government. In 2007, he was granted the May 1 Labor Medal of Sichuan Province (四川省五一勞動獎章) by the Sichuan Provincial Federation of Trade Unions in 2007. Mr. Zhang was rewarded as Leading Entrepreneur of Foreign Trading and Export Enterprises in Sichuan for 2009.

Mr. Ren Jie (任杰先生), aged 45, has been an Executive Director of the Company since 18 January 2008. He is also a Vice-president of the Company. In 1990, Mr. Ren earned a Bachelor's Degree in mining machinery from Southwest Petroleum University, located in Sichuan Province, specializing in petroleum and natural gas. In 1995, Mr. Ren obtained an engineering qualification, granted by the China National Petroleum Corp., Sichuan Petroleum Administration. In November 2007, he also became a member of the 5th Edition Committee of the Oil Field Equipment Journal. Mr. Ren is employed as an senior engineer by Honghua Company.

In the early stages of Honghua Company, Mr. Ren successfully designed a rotary table transmission unit, a drawworks bevel gear box, and universal shaft equipment for the ZJ70LC drilling rigs, which contributed greatly to the development of the Company. Mr. Ren, together with his research and development team, also successfully developed a set of digitally-controlled VFD rigs, after the development of the first digitally controlled VFD rig (DBS).

Positions held by Mr. Ren in the Company's subsidiaries are set forth in the table below.

Subsidiary	**Position**	**Term of Office**
Honghua Holdings Limited	director	Since 18 August 2006
Sichuan Honghua Petroleum Equipment Co., Ltd.	director	Since 31 December 1997
Honghua International Co., Ltd.	director	Since 13 January 2004
	general manager	Since 24 April 2008
Sichuan Honghua Youxin Petroleum Machinery Co., Ltd.	director	Since 8 December 2006 until 1 August 2009
Honghua Offshore Oil & Gas Equipment (Jiangsu) Co., Ltd.	director	Since 8 June 2009
Chengdu Hongtian Electric Drive Engineering Co., Ltd.	director	Since 1 August 2009
Honghua (China) Investment Co., Ltd.	director	Since 14 January 2010
	deputy general manger	Since 30 June 2010
Newco (H.K.) Limited	director	Since 22 June 2008
	chairman, and general manager	Since 22 September 2009
Alpha Advanced Limited	director	Since 10 July 2009
Russia Honghua Co., Ltd.	director	Since 26 June 2008
Egyptian Petroleum HH Rigs Manufacturing CO. S.A.E.	director	Since 7 August 2009
Honghua America, LLC.	director	Since 10 October 2008
Sichuan Honghua International (H.K.) Limited	director	Since 25 June 2010

Mr. Liu Zhi (劉智先生), aged 48, has been an Executive Director of the Company since 26 May 2008. He is also a Vice-president of the Company. Mr. Liu graduated from Southwest Petroleum University in 2003, with a Master's Degree in oil and gas storage and transportation. He was an engineer and a head of workshop of South-Sichuan Mining Area of Sichuan Petroleum Bureau since 1981 to 1994. Mr. Liu was the factory director of Guanghan Petroleum Machinery Main Factory of Sichuan Petroleum Administration from 1994 to 2000. Mr. Liu has contributed to the expansion of Honghua Group's markets inside and outside of China.

Positions held by Mr. Liu in the Company's subsidiaries are set forth in the table below.

Subsidiary	**Position**	**Term of Office**
Honghua Holdings Limited	director	Since 26 May 2008
Honghua Offshore oil & gas equipment (Jiangsu) Co., Ltd.	director	Since 8 June 2009
Honghua Oil & Gas Engineering Services Co., Ltd.	director	Since 14 April 2009
	chairman	Since 21 July 2009
Alpha Advance Limited	chairman	Since 31 August 2009
Hi Tech Drilling Company Limited	chairman	Since 8 February 2010
Egyptian Petroleum HH Rig Manufacturing Co. S.A.E.	director	Since 26 April 2007 until 7 August 2009
Sichuan Honghua Petroleum Equipment Co., Ltd.	director	Since 26 May 2008 until 18 January 2010
	managing deputy general manager	Since 27 April 2008 until 18 January 2010
Honghua International Co., Ltd.	director	Since 13 January 2004 until 1 August 2009
Chengdu Hongtian Electric Drive Engineering Co., Ltd.	director	Since 8 December 2006 until 1 August 2009
Honghua (China) Investment Co., Ltd.	director	Since 14 January 2010
	deputy general manager	Since 30 June 2010
Honghua Oil & Gas Engineering and Technology Services (Sichuan) Co., Ltd.	chairman and general manager	Since 30 December 2010

NON-EXECUTIVE DIRECTORS

Mr. Huang Dongyang (黃東陽先生), aged 51, has been a Non-executive Director of the Company since 14 April 2010. He was a director of Honghua Holdings Limited, Honghua Company as well as Honghua Offshore Oil & Gas Equipment (Jiangsu) Co., Ltd. respectively from 13 April 2010 to 24 January 2011. He was a director of Honghua (China) Investment Co., Ltd. from 4 May 2010 to 24 January 2011. Mr. Huang has been the Managing Director of China Ocean Oilfields Services (H.K.) Ltd. ("COOS") since April 2009, and was the Deputy Manager of COOS from 2007 to 2009. From 2006 to 2007, he was the Manager of Logistics Department of COOS, and from 2002 to 2006, he was the Deputy Manager of Hui Zhou Petrochemicals Services Company, CNOOC Nanhai East Corporation. From September 1978 to July 1982, Mr. Huang studied Theoretical Physics at Xiamen University and obtained Bachelor's degree of science in 1982. From March 1985 to July 1986, Mr. Huang further studied English Language in College of Foreign Language at Sun Yat-Sen University. Mr Huang has been a senior engineer since February 1995.

Mr. Siegfried Meissner, aged 59, has been a Non-executive Director of the Company since 26 May 2008. Mr. Meissner graduated from the Technical University of Clausthal-Zellerfeld, Germany as Dipl. Berging., specialized in drilling, reservoir and production engineering in 1982. Since 1993, Mr. Meissner joined the Nabors Group as President of Nabors Drilling International Limited. Mr. Meissner has been a director of Nabors International Management Limited since 29 December 2004.

INDEPENDENT NON-EXECUTIVE DIRECTORS

Mr. Liu Xiaofeng (劉曉峰先生), aged 49, has been an Independent Non-executive Director of the Company since 18 January 2008. He is currently a managing director of China Resources Capital Holdings Company Limited, and an Independent Non-executive Director of CNPC (Hong Kong) Limited and Haier Electronics Group Co., Ltd., both of which are publicly-listed companies on the Stock Exchange. He has over 17 years of experience in corporate finance and has worked with various international financial institutions since 1993, including NM Rothschild & Sons, JP Morgan, and DBS. Mr. Liu obtained a Master's degree and a Ph.D. from the Faculty of Economics, University of Cambridge in 1988 and 1993 respectively, a Master of Science degree in Development Studies from the University of Bath, England, in 1987, and a Bachelor of Economics degree from Sichuan Finance College (Southwest University of Finance and Economics, China) in 1983.

Mr. Qi Daqing (齊大慶先生), aged 48, has been an Independent Non-executive Director of the Company since 18 January 2008. Mr. Qi is a Professor of Accounting and Associate Dean at Cheung Kong Graduate School of Business (CKGSB). He taught at the School of Accounting, The Chinese University of Hong Kong, from 1996 to 2002. His research interests primarily focus on financial reporting and strategy execution. He has published many articles in accounting and finance journals, and he has extensive executive training and consulting experience in accounting and corporate finance.

His clients include:

Type of client	Name of client	Duration of service
Government:	Shanghai Municipal Government	2000–2001
	Ministry of Information Industries of PRC	1998–2000
Private Sector:	Huawei Technologies Co., Ltd.	2006
	Lenovo Group Limited	2004–2005
	Digital China Holdings Limited	2004
	Siemens Ltd., China	2002
	China Telecommunications Corporation	2001
	Nokia (China) Investment Co., Ltd.	1999–2001

He received his Ph.D. in Accounting from Michigan State University in 1996, his MBA from the University of Hawaii at Manoa in 1992, and his Bachelor's Degrees in Biophysics and International Journalism from Fudan University in 1985 and 1987, respectively. Mr. Qi is not a certified public accountant; he became a member of the American Accounting Association in 1996. With over ten years of experience as a Professor of Accounting, a Ph.D in Accounting, an MBA and extensive executive training and consulting experience in accounting and corporate finance, Mr. Qi's experience means that he has the requisite expertise as required by the Listing Rules. Therefore, whilst Mr. Qi does not hold formal accounting professional qualifications, he meets the criteria for accounting and related financial management expertise as required by Rule 3.10(2) of the Listing Rules.

Mr. Qi is currently an independent non-executive director and chairman of the audit committee of Sohu (a NASDAQ listed company), Focus Media Holding Limited (a NASDAQ listed company), Sino Media Holding Limited (a HKSE listed company), AutoNavi Holdings Limited (a NASDAQ listed company), China Huiyuan Juice Group Limited (a HKSE listed company), Daqo New Energy Co., Ltd. (a NYSE listed company) and Bona Film Group (a NASDAQ listed company) respectively. He is an independent director, member of the audit committee of China Vanke Co., Ltd (a SZSE listed company). He is directly involved in the formulation of accounting policies and audit processes of the above-mentioned companies.

Mr. Tai Kwok Leung, Alexander (戴國良先生), aged 54, has been an Independent Non-executive Director of the Company since 18 January 2008. Mr. Tai graduated from Victoria University of Wellington in New Zealand with a degree in Bachelor of Commerce and Administration in 1982 and became an associate member of the Hong Kong Institute of Certified Public Accountants in 1983. Mr. Tai has extensive accounting, corporate finance and investment experience in Hong Kong and overseas. Mr. Tai is a shareholder and an executive director of Invest Captial Asia Limited (formerly kmown as "Access Capital Limited"), a licensed corporation under the SFO to conduct Type 1 (dealing in securities), Type 4 (advising on securities), Type 6 (advising on corporate finance) and Type 9 (asset management) regulated activities. Mr. Tai currently is an independent non-executive director of Luk Fook Holdings (International) Limited and First Credit Holdings Limited.

Mr. Chen Guoming (陳國明先生), aged 49, has been an Independent Non-executive Director of the Company since 18 January 2008. In 1982, Mr. Chen graduated from the Mechanical Department of the East China Petroleum Institute with a Bachelor's Degree, and then worked as an assistant engineer in the Lanzhou General Machinery Plant from 1982 to 1983. He earned his Master's degree in 1986, from the Beijing Graduate School of East China Petroleum Institute. He then worked as a teacher in this Institute and was then promoted to Associate Professor and Professor in 1992 and 1995, respectively. He was a visiting scholar at the University of California, Berkeley, from 1996 to 1997. He obtained his Ph.D. degree in 1999, and was employeed as Ph.D. candidate supervisor in 2000. He is now a Professor and a Ph.D. candidate supervisor in the Department of Mechanical and Electrical Engineering, China University of Petroleum. Currently, Mr. Chen is the Chief Officer of Shandong Key Laboratory of Petroleum Mechanical Engineering and the Research Centre of Security technique of the Offshore Oil & Gas Equipment; a member of the Quality & Reliability Committee of China Petroleum Society, the Offshore Engineering Committee of China Naval Architects and Marine Engineers' Society and China Mechanical Engineering Society; and a member of the Editorial Committee of the Journal of Petroleum Science, the Journal of Oil Mining Field Machinery and the Journal of China University of Petroleum (Natural Science Edition). He has been receiving special subsidies granted by the State Council of the PRC government (政府特殊津貼) since August 2005, for his significant contribution to the development of higher education in China, and was awarded the National Labor Day Medal in 2007.

Mr. Shi Xingquan (史興全先生), aged 69, has been an Independent Non-executive Director of the Company since 14 April 2009. Mr. Shi is a senior engineer in professor level. Mr. Shi graduated from the Northeastern Petroleum College in 1965 and is a well-known petroleum engineering expert. Mr. Shi has been appointed as the vice president of PetroChina Company Limited from 1999 until 2003. Mr. Shi was awarded the National Technology Advancement Award (First Prize) by the National Science and Technology Council of the PRC in 1997. In 2003, Mr. Shi was awarded the National Scientific and Technological Progress Award (First Prize) by State Council of the PRC. Mr. Shi was also granted the Middle-aged and Young Experts of the State with Outstanding Contribution by Ministry of Personnel of the PRC.

Mr. Guo Yanjun (郭燕軍先生), aged 59, has been an Independent Non-executive Director of the Company since 20 June 2011. In 1982, Mr. Guo graduated with a Diploma in Law from China People's University in 1984. Mr Guo is an independent non-executive director of Z-Obee Holdings Limited (a company listed on HKSE and Singapore Exchange Limited) and Strong Petrochemical Holdings Limited (a HKSE listed company). Mr. Guo has extensive entrepreneurship experiences and experience of corporate operation and management. Mr. Guo is currently the chairman of Beijing Junxinda Economic Development Co., Ltd., CNHK Media Limited, CNHK Energy Limited and CNHK Publication Limited respectively.

Mr. Wang Li (王礫先生), aged 41, was appointed as an Independent Non-executive Director of the Company on 18 January 2008 and resigned with effect from 20 June 2011. Mr. Wang graduated from China University of Political Science and Law in 1992 with a Bachelor's Degree in Civil Law and in 2001 received a Master's Degree in International Law from Napier University Edinburgh. Mr. Wang also studied law in international business and international electronic business at Asia Economy Management College of the University of California in 1996. Mr. Wang specializes in legal services in finance, stock exchange, real estate and international business. His clients include, among others, Bank of China (Chengdu branch), Citigroup Global Markets Asia Ltd. and Construction Bank of China (International Division of Sichuan Branch). Mr. Wang is a director of the Sichuan Lawyers Association and a partner of Beijing Guantao Law Firm Sichuan Office.

SENIOR MANAGEMENT

Mr. Zhao Ping (趙平先生), aged 55, has been a Vice-president of the Company since 27 April 2008. He has been a director of Honghua Company since 18 January 2010, and has been the chairman of Honghua Company since 1 January 2012. He was the general manager of Honghua Company from 18 January 2010 to 31 December 2011. Mr. Zhao was one of the initial founders of Sichuan Honghua Youxin Petroleum Machinery Co., Ltd., and has been the chairman and general manager of Sichuan Honghua Youxin Petroleum Machinery Co., Ltd. since 2000. Mr. Zhao established the corporate operation system and improved the construction of regulations of Sichuan Honghua Youxin Petroleum Machinery Co., Ltd.. From 1972 to 1999, Mr Zhao worked in South-Sichuan Mining Area of Sichuan Petroleum Bureau. He was the head of Quality Management Office since 1993, and the director of Workshop No.1 from 1994 to 1996, and was the Deputy Factory Director from 1997 to 1999. Mr. Zhao graduated from of Machinery Department of Southwest Petroleum University, majoring in Petroleum & Minerals Machinery and is a qualified engineer.

Mr. Zhang Cong (張聰先生), aged 56, has been a Vice-president of the Company since 27 April 2008, and has been the chairman and general manager of Chengdu Hongtian Electric Drive Engineering Co., Ltd. since June 2001. He has been a director of Honghua International Co., Ltd since 1 August 2009, and has been the general manager of Honghua Offshore Oil & Gas Equipment (Jiangsu) Co., Ltd. and Shanghai Honghua Offshore Oil & Gas Equipment Co., Ltd. since 26 September 2011. Mr. Zhang was one of the initial founders of Chengdu Hongtian Electric Drive Engineering Co., Ltd.. Mr. Zhang has helped Chengdu Hongtian Electric Drive Engineering Co., Ltd. to sell DBS digital VFD system to major oil fields in China and a large number of products to the overseas market. In December 2006, Mr. Zhang was awarded "The Fourth session Excellent Start in Undertaking Entrepreneur of Chengdu". Mr. Zhang was a cadre in South-Sichuan Mining Area of Sichuan Petroleum Bureau from September 1985 to September 1994 and was the Manager and Director of Luzhou Huayou Compressed Gas Co., Ltd. form September 1994 to June 2001. Mr. Zhang graduated from Sichuan Radio TV University, majoring in electronic technology and is a qualified engineer.

Mr. Liu Gangqiang (劉剛強先生), aged 42, has been the Secretary of the Board of Directors and a Joint Company Secretaries of the Company since 21 January 2008. He has been the Secretary of the board of directors of Honghua Company from March 2004 to January 2011. Mr. Liu is designated as the Chief Operational officer of Honghua Holdings Limited since September 2009. He is mainly responsible for reorganization and listing preparation of the Company, capital operation, securities market related affairs, corporate finance, financial information management, internal audit and supervision affairs, capital market compliance and production operations legal affairs, intellectual property protection, investor and shareholder relations, government and regulatory authority coordination, and day-to-day administration of the Board of Directors etc..

From February 2003 to September 2003, Mr. Liu conducted research on the development of state-owned enterprises, in the Work Technology Center of the Sichuan State-Owned Enterprise Supervisory Committee. From October 2000 to September 2003, he was an assistant general manager of Sichuan Aerospace High-tech Co., Ltd., and the general manager of Aerospace Network Communications System Engineering Co., Ltd.. From September 1997 to October 2000, he served as an economist in Sichuan Trust & Investment Co., Ltd., and was engaged in securities analysis, investment financing, capital planning, asset management and legal affairs. From September 1991 to May 1994, he was a technician at Beijing Yanshan Petroleum & Chemicals Co., Ltd.. Mr. Liu graduated from Chengdu Science and Technology University (now Sichuan University), with a Bachelor's Degree in high polymer material and engineering, in 1991. He earned a Master's degree in Economics from Southwest University of Finance and Economics in 1997. In 2003, he received a Ph.D. in Economics from Southwest University of Finance and Economics.

Mr. Feng Shangfei (馮尚飛先生), aged 38, has been the Human Resources Director of the Company and Honghua (China) Investment Co., Ltd. since 1 June 2011, and was appointed as the general manager of Honghua Company with effect from 1 January 2012. Mr. Feng graduated from Shangdong University (formerly known as Shangdong Industry University) with a Bachelor's Degree of engineering in 1995, majoring in mechanical design and manufacture. He earned a Master's degree of Psychology from Beijing Normal University in 2000. Mr. Feng has over 10 years of experience in personnel, administration, corporate culture, senior management of large enterprise. For the period from October 2009 to March 2011, Mr. Feng worked for Anton Oilfield Services (Group) Ltd. as the Human Resources Director. For the period From April 2006 to September 2009, he worked for ENN Energy Holdings Limited, served as Human Resources Director of the LNG Division, vice president of human resources of overseas business department and general manager of Vietnamese company. For the period from October 2000 to March 2005, Mr. Feng worked for Linuo Group Holdings Co.,Ltd.. For the period from July 1995 to October 2000, he was a lecturer of Shandong University.

Mr. Chung Kai Cheong (鍾啓昌先生), aged 34, has been the Financial Controller of the Company, Honghua Holdings Limited and Honghua (China) Investment Co., Ltd. since 1 June 2011. Mr. Chung joined the Group in August 2008 as a director of financial centre of the Company. Mr. Chung has over 10 years of experience in accounting and auditing at international accounting firms and listed company. Mr. Chung also worked for KPMG from December 2003 to July 2008 with the then latest position as an Audit Manager. He also worked for BDO Limited (formerly known as BDO McCabe Lo & Co.) for the period from June 2000 to December 2003 with the then latest position as a Senior Associate. Mr. Chung obtained a Bachelor's Degree majoring in accountancy from The City University of Hong Kong in September 2000. He is currently an associate member of the Hong Kong Institute of Certified Public Accountants.

Ms. Lu Hong (魯紅女士), aged 42, was appointed as financial controller of Honghua Company from May 2007 to January 2011, and was the Financial Controller and the Qualified Accountant of the Company from June 2007 to 31 May 2011. She was the chief financial officer of Honghua Holdings Limited from 8 September 2009 to 31 May 2011. Before the Company's Listing, Ms. Lu was responsible for the financial and accounting work concerning the Listing. Upon the Company's Listing, Ms. Lu is responsible for all the financial and accounting work of the Company and its subsidiaries. Ms. Lu was the company secretary, qualified accountant and assistant financial controller of Guangdong Nanyue Logistics Co., Ltd., a company listed on the Stock Exchange, from February 2005 to December 2006. She is a Certified Public Accountant in China, a Certified Public Accountant in Hong Kong, and has obtained a fellowship from the Association of Chartered Certified Accountants (FCCA). Ms. Lu graduated from China University of Geosciences, Beijing, with a Master's Degree in 1994.

Mr. Chen Zhen (陳臻先生), aged 45, was appointed as a Human Resources Officer of the Company from 18 January 2010 to 31 May 2011. Mr. Chen became Human Resource Department Director of the Company in January 2008. In October 2003, Mr. Chen joined in Honghua Company as the general manger assistant. As a primary founder of Human Resource Department of Sichuan Honghua Petroleum Equipment Co., Ltd, he performed as Human Resource Department director from January 2004 to January 2010. He joined Deyang Daily Newspaper in July 1990. Since then, he served as journalist, editor, director, and editorial member respectively. Mr. Chen is proficient in government regulation. He has a profound understanding of different classes of the society and strength in communication and in reconciling conflicts among various individuals. Mr. Chen graduated from Peking University with Bachelor for Psychology in 1987, and he also achieved Master of Philosophy in 1990. In 1998, he achieved chief editor certification authorized by Sichuan Province Personnel Department.

Ms. Corinna Leung (梁慧嫻女士), aged 44, has been a Joint Company Secretaries of the Company since 21 January 2008. She is a senior manager of the corporate services department of Tricor Services Limited. She is an associate with the Institute of Chartered Secretaries and Administrators and the Hong Kong Institute of Chartered Secretaries. She provides corporate services to companies that are listed on the Main Board, Growth Enterprise Market of the Stock Exchange and private companies. She acts as the joint company secretary of SBI Holdings, Inc. (stock code: 6488), a company listed on the Stock Exchange and Beijing Jingneng Clean Energy Co., Limited (stock code: 00579), a company listed on the Stock Exchange.

CORPORATE GOVERNANCE REPORT

The Board presents this Corporate Governance Report in the Group's annual report for the year ended 31 December 2011.

The Company's corporate governance policies and practices are applied and implemented in the manners as stated in the following Corporate Governance Report:

CORPORATE GOVERNANCE PRACTICES OF THE COMPANY

The Group is committed to achieving high standards of corporate governance to safeguard the interests of Shareholders and to enhance corporate value and accountability.

The Group strives to maintain high standards of corporate governance to enhance Shareholder value and safeguard Shareholder interests. The Group's corporate governance principles emphasize a quality Board, effective internal controls and accountability to Shareholders.

The Board believes that good corporate governance practices are increasingly important for maintaining and promoting Shareholder value and investor confidence.

The Company has applied the principles as set out in the Code on Corporate Governance Practices ("CG Code") contained in Appendix 14 of the Listing Rules.

The CG Code sets out the principles of good corporate governance and two levels of corporate governance practices:

a) code provisions, which listed issuers are expected to comply with or to give considered reasons for any deviation; and

b) recommended best practices for guidance only, which listed issuers are encouraged to comply with or to give considered reasons for deviation.

The Company's corporate governance practices are based on the principles, code provisions and certain recommended best practices as set out in the CG Code.

The Company has complied with most of the code provisions as set out in the CG Code throughout the year ended 31 December 2011, save for certain deviations from the code provisions in respect of separation of roles of Chairman and President (Chief Executive Officer), details of which will be explained below.

The Company reviews its corporate governance practices regularly to ensure compliance with the CG Code.

The Company is committed to enhance its corporate governance practices appropriate to the conduct and growth of its business and to review its corporate governance practices from time to time to ensure that they comply with the statutory and professional standards and align with the latest developments.

THE BOARD OF DIRECTORS

RESPONSIBILITIES

The Board is responsible for leadership and control of the Company and oversees the Group's businesses, strategic decisions and performance. The senior management was delegated the authority and responsibility by the Board for the day-to-day management and operations of the Group. In addition, the Board has also established Board committees and has delegated to these Board committees various responsibilities as set out in their terms of reference.

All Directors have carried out duties in good faith, in compliance with the standards of applicable laws and regulations, and act in the interests of the Company and its Shareholders at all times.

BOARD COMPOSITION

The Board currently comprises 11 members, consisting of 3 Executive Directors, 2 Non-executive Directors and 6 Independent Non-executive Directors.

The Company has met the recommended best practice under the CG Code for the Board to have at least one-third of its membership comprising Independent Non-executive Directors.

The Board comprises the following Directors:

Executive Directors:

Zhang Mi	*(Chairman and President (Chief Executive Officer, "CEO"), Chairman of Strategic Investment and Risk Control Committee, Chairman of Nomination Committee and Member of Remuneration Committee)*
Ren Jie	*(Vice-President and Member of Strategic Investment and Risk Control Committee)*
Liu Zhi	*(Vice-President and Member of Strategic Investment and Risk Control Committee)*

Non-executive Directors:

Siegfried Meissner	
Huang Dongyang	*(Member of Strategic Investment and Risk Control Committee)*

Independent Non-executive Directors:

Liu Xiaofeng	*(Chairman of Remuneration Committee, Chairman of Corporate Governance Committee, Member of Audit Committee and Nomination Committee)*
Qi Daqing	*(Chairman of Audit Committee and Member of Remuneration Committee, Corporate Governance Committee and Nomination Committee)*
Tai Kwok Leung Alexander	*(Member of Audit Committee and Corporate Governance Committee)*
Chen Guoming	*(Member of Audit Committee and Corporate Governance Committee)*
Shi Xingquan	*(Member of Audit Committee, Corporate Governance Committee and Strategic Investment and Risk Control Committee)*
Guo Yanjun	*(Member of Audit Committee and Corporate Governance Committee) (Appointed with effect from 20 June 2011)*
Wang Li	*(Member of Audit Committee, Corporate Governance Committee and Strategic Investment and Risk Control Committee) (Resigned with effect from 20 June 2011)*

None of the members of the Board is related to one another.

During the year ended 31 December 2011, the Board at all times met the requirements of the Listing Rules relating to the appointment of at least three Independent Non-executive Directors with at least one Independent Non-executive Director possessing appropriate professional qualifications or accounting or related financial management expertise.

The Company has received written annual confirmation from each Independent Non-executive Director of his independence pursuant to the requirements of the Listing Rules. The Company considers all Independent Non-executive Directors to be independent in accordance with the independence guidelines as set out in the Listing Rules.

The Non-executive Directors bring a wide range of business and financial expertise, experience and independent judgement to the Board. Through active participation in Board meetings, taking the lead in managing issues involving potential conflict of interests and serving on Board committees, all Non-executive Directors make various contributions to the effective direction of the Company.

All Directors, Including Non-executive Directors and Independent Non-executive Directors, have brought a wide spectrum of valuable business experience, knowledge and professionalism to the Board for its efficient and effective functioning. Independent Non-executive Directors are invited to serve respectively on the Audit, Remuneration, Corporate Governance, Strategic Investment and Risk Control and Nomination Committees of the Company.

CHAIRMAN AND PRESIDENT (CHIEF EXECUTIVE OFFICER "CEO")

Provision A.2.1 of the CG Code stipulates that the roles of Chairman and CEO should be separated and should not be performed by the same individual.

Mr. Zhang Mi is the Chairman and President (CEO) of the Company. He is one of the founders of the Group and possesses with knowledge and experience of the industry and the related industries. The Board believes that vesting the roles of both Chairman and President (CEO), Mr. Zhang Mi provides the Company with strong and consistent leadership and allows for effective and efficient planning and implementation of business decisions and strategies.

The Board is of the view that it is in the best interests of the Group to have the 2 roles performed by Mr. Zhang Mi so that the Board can have the benefit of a chairman who is knowledgeable about the business of the Group and is most capable to guide discussions and brief the Board in a timely manner on pertinent issues and developments to facilitate open dialogue between the Board and the management.

The Company will continue to review the effectiveness of the Group's corporate governance structure and consider whether any changes, including the separation of the roles of Chairman and President (CEO), are necessary.

APPOINTMENT AND RE-ELECTION OF DIRECTORS

Each of the Directors is engaged on a service contract for a term of not exceeding 3 years. The appointment may be terminated by not less than 3 months' written notice except for Mr. Siegfried Meissner whose appointment may be terminated by not less than 1 month's written notice.

In accordance with the Company's Articles of Association, all Directors are subject to retirement by rotation at least once every three years and any new Director appointed to fill a casual vacancy or as an addition to the Board shall submit himself/herself for re-election by Shareholders at the first general meeting after appointment.

The procedures and process of appointment, re-election and removal of Directors are laid down in the Company's Articles of Association. The Nomination Committee newly established on 17 January 2012 will be responsible for reviewing the Board composition, developing and formulating the relevant procedures for nomination and appointment of Directors, monitoring the appointment and succession planning of Directors and assessing the independence of Independent Non-executive Directors.

During the year ended 31 December 2011 and before the establishment of the Nomination Committee, the Board has reviewed its own structure, size and composition regularly to ensure that it has a balance of expertise, skills and experience appropriate for the requirements of the business of the Company. Where vacancies on the Board exist, the Board would carry out the selection process by making reference to the skills, experience, professional knowledge, personal integrity and time commitments of the proposed candidates, the Company's needs and other relevant statutory requirements and regulations.

At 2012 annual general meeting, Mr. Ren Jie, Mr. Siegfried Meissner, Mr. Qi Daqing, Mr. Shi Xingquan and Mr. Guo Yanjun, will retire by rotation and being eligible, offer themselves for re-election.

The Company's circular for the 2012 annual general meeting shall contain detailed information of the Directors' standing for re-election.

TRAINING INDUCTION AND CONTINUING DEVELOPMENT OF DIRECTORS

Each newly appointed Director would receive a comprehensive, formal and tailor made induction on the first occasion of his/her appointment, so as to ensure that he/she has adequate understanding of the business and operations and governance of the Company and that he/she is fully aware of his/her responsibilities and obligations under the Listing Rules and relevant statutory requirements.

The Directors are continually updated with the legal and regulatory developments and the business and market changes to facilitate the discharge of their responsibilities. Continuing briefing and professional development for Directors will be arranged where necessary.

BOARD MEETINGS

Board Practices and Conduct of Meetings

Annual meeting schedules and draft agenda of each meeting are normally made available to Directors in advance.

Notice of regular Board meetings are served to all Directors at least 14 days before the meeting. For other Board and committee meetings, reasonable notice is generally given.

Board papers together with all appropriate, complete and reliable information are sent to all Directors at least 3 days before each Board meeting or committee meeting to keep Directors apprised of the latest developments and financial position of the Company and to enable them to make informed decisions. The Board and each Director also have separate and independent access to the senior management where necessary.

The senior management would attend all regular Board meetings and where necessary, other Board and committee meetings, to advise on business developments, financial and accounting matters, statutory and regulatory compliance, corporate governance and other major aspects of the Company.

The Company Secretary is responsible to take and keep minutes of all Board meetings and committee meetings. Draft minutes are normally circulated to Directors for comment within a reasonable time after each meeting and the final versions are open for Directors' inspection.

The Company's Articles of Association contain provisions requiring Directors to abstain from voting and not to be counted in the quorum at meetings for approving transactions in which such Directors or any of their associates have a material interest.

Directors' Attendance Records

During the year ended 31 December 2011, four regular Board meetings were held at approximately quarterly intervals for reviewing and approving the financial and operating performance, and considering and approving the overall strategies and policies of the Company.

The attendance records of each Director at the meetings of the Board, the Audit Committee, the Remuneration Committee, the Corporate Governance Committee and the Strategic Investment and Risk Control Committee during the year ended 31 December 2011 are set out below:

	Attendance/Number of Meetings				
Name of Director	**Board**	**Audit Committee**	**Remuneration Committee**	**Corporate Governance Committee**	**Strategic Investment and Risk Control Committee**
Zhang Mi	05/05	—	01/01	—	01/01
Ren Jie	05*/05	—	—	—	01/01
Liu Zhi	05/05	—	—	—	01/01
Siegfried Meissner	0/05	—	—	—	—
Huang Dongyang	05*/05	—	—	—	0/01
Liu Xiaofeng	05/05	02/02	01/01	02/02	—
Qi Daqing	05**/05	02/02	01/01	02/02	—
Tai Kwok Leung, Alexander	05/05	02/02	—	02/02	—
Chen Guoming	05/05	02/02	—	02/02	—
Shi Xingquan	05/05	02/02	—	02/02	01/01
Guo Yanjun *(appointed with effect from 20 June 2011)*	01/02	01/01	—	01/01	—
Wang Li *(resigned with effect from 20 June 2011)*	02/02	01/01	—	01/01	01/01

* Director had appointed proxy to attend 1 meeting

** Director had appointed proxy to attend 2 meetings

MODEL CODE FOR SECURITIES TRANSACTIONS

The Company has adopted its own code of conduct regarding Directors' dealings in the Company's securities (the "Company Code") on terms no less exacting than the Model Code for Securities Transactions by Directors of Listed Issuers (the "Model Code") as set out in Appendix 10 to the Listing Rules.

Specific enquiry has been made of all the Directors and the Directors have confirmed that they have complied with the Company Code and the Model Code throughout the year ended 31 December 2011.

The Company has also established written guidelines on no less exacting terms than the Model Code (the "Employees Written Guidelines") for securities transactions by employees who are likely to be in possession of unpublished price-sensitive information of the Company.

No incidence of non-compliance of the Employees Written Guidelines by the employees was noted by the Company.

DELEGATION BY THE BOARD

The Board reserves for its decision all major matters of the Company, including the approval and monitoring of all policy matters, overall strategies and budgets, internal control and risk management systems, material transactions (in particular those that may involve conflict of interests), financial information, appointment of Directors and other significant financial and operational matters.

All Directors have full and timely access to all relevant information as well as the advice and services of the Company Secretary, with a view to ensuring that Board procedures and all applicable rules and regulations are complied with. Each Director is normally able to seek independent professional advice in appropriate circumstances at the Company's expense, upon making request to the Board.

The day-to-day management, administration and operation of the Company are delegated to the President (Chief Executive Officer) and the senior management. The delegated functions and responsibilities are periodically reviewed. Approval has to be obtained from the Board prior to any significant transactions entered into by the aforementioned officers.

The Board has established 5 committees, namely, the Remuneration Committee, the Audit Committee, the Corporate Governance Committee, the Strategic Investment and Risk Control Committee and the Nomination Committee (which was formed on 17 January 2012) for overseeing particular aspects of the Company's affairs. All Board committees of the Company are established with defined written terms of reference which are available to Shareholders upon request.

The Board also has the full support of the CEO and the senior management to discharge its responsibilities.

REMUNERATION OF DIRECTORS AND SENIOR MANAGEMENT

REMUNERATION COMMITTEE

The Remuneration Committee comprises 3 members, Liu Xiaofeng (Chairman), Zhang Mi and Qi Daqing, the majority of them are Non-executive Directors.

The primary objectives of the Remuneration Committee include the following:

- To make recommendations on the establishment of procedures for developing remuneration policy and structure of the Directors and the senior management, such policy shall ensure that no Director or any of his/her associates will participate in deciding his/her own remuneration;

- To make recommendations on the remuneration packages of the Non-executive Directors to the Board;

- To review and approve the remuneration packages of the Executive Directors and the senior management by reference to the performance of the individual and the Company as well as market practice and conditions; and

- To review and approve the compensation arrangements for the Executive Directors and the senior management in connection with (i) any loss or termination of their office or appointment and (ii) any dismissal or removal of directors for misconduct to ensure such arrangements are determined in accordance with contractual terms and that such compensation is reasonable and appropriate.

The Remuneration Committee normally meets at least once a year for reviewing the remuneration policy and structure and determining the annual remuneration packages of the Executive Directors and the senior management and other related matters.

The Remuneration Committee held a meeting during the year ended 31 December 2011 and the attendance records are set out under “Directors’ Attendance Records” on page 34.

REMUNERATION POLICY

The Group’s remuneration policy takes into account the employees role structure, their job duties, individual capacities and experience, and market value in the labour market in order to establish a competitive and fair remuneration system. In terms of long term incentives, the Company has adopted a share option scheme and a Restricted Share Award Scheme for eligible participants, details of which are set out under the paragraph “Share Option Scheme” and “Restricted Share Award Scheme” in the Report of the Directors.

REMUNERATION OF DIRECTORS

The basis of determining the emolument of Directors is on various considerations, including Directors' capability, knowledge and experience, participation to the Board, job duties and responsibilities and is also made reference to the market practices and conditions. The remuneration of the Executive Directors is based on their administrative management positions. Independent Non-executive Directors are entitled to a fixed emolument package. Non-executive Directors may be entitled to a fixed emolument under the service contract.

ACCOUNTABILITY AND AUDIT

DIRECTORS' RESPONSIBILITIES FOR FINANCIAL REPORTING IN RESPECT OF FINANCIAL STATEMENTS

The Directors acknowledge their responsibility for preparing the financial statements of the Company for the year ended 31 December 2011.

The Board is responsible for presenting a balanced, clear and understandable assessment of annual and interim reports, price-sensitive announcements and other disclosures required under the Listing Rules and other statutory and regulatory requirements.

The management provides such explanation and information to the Board so as to enable the Board to make an informed assessment of the financial statements and position of the Company, and to approve the financial statements accordingly.

INTERNAL CONTROLS

During the Year under review, the Board, through the Audit Committee, has conducted a review of the effectiveness of the internal control system of the Company including the adequacy of resources, qualifications and experience of staff of the Company's accounting and financial reporting function, and their training programmes and budget.

The Board is responsible for maintaining an adequate internal control system to safeguard Shareholder investments and Company assets and with the support of the Audit Committee, reviewing the effectiveness of such system on an annual basis.

The internal control system of the Group is designed to facilitate effective and efficient operations, to ensure reliability of financial reporting and compliance with applicable laws and regulations, to identify and manage potential risks and to safeguard assets of the Group. The senior management shall review and evaluate the control process and monitor any risk factors on a regular basis, and report to the Audit Committee on any findings and measures to address the variances and identified risks.

During the Year under review, the Company engaged external professional auditors to initiate an independent review covering the financial, operational, compliance and risk management aspects of the finance and major operational functions of the Group. Report from the external professional auditors were presented to and reviewed by the Audit Committee.

AUDIT COMMITTEE

The Audit Committee comprises 6 Independent Non-executive Directors, namely, Qi Daqing (Chairman), Liu Xiaofeng, Tai Kwok Leung, Alexander, Chen Guoming, Shi Xingquan and Guo Yanjun (who has been appointed with effect from 20 June 2011 to replace Wang Li who has resigned with effect from 20 June 2011), including 3 Independent Non-executive Directors who possess the appropriate professional qualifications or accounting or related financial management expertise.

The main duties of the Audit Committee include the following:

- To review the financial statements and reports and consider any significant or unusual items raised by the staff responsible for the accounting and financial reporting function or external auditors before submission to the Board;

- To review the relationship with the external auditors by reference to the work performed by the auditors, their fees and terms of engagement, and make recommendations to the Board on the appointment, re-appointment and removal of external auditors; and

- To review the adequacy and effectiveness of the Company's financial reporting system, internal control system and risk management system and associated procedures.

The Audit Committee provides supervision on the internal control system of the Group and reports to the Board on any material issues, and makes recommendations to the Board.

During the Year under review, the Audit Committee has reviewed the Group's annual results and annual report for the year ended 31 December 2011, the financial reporting and compliance procedures, the report from the management on the Company's internal control and risk management systems and processes, and the re-appointment of the external auditors.

The Audit Committee held two meetings during the year ended 31 December 2011 and the attendance records are set out under "Directors' Attendance Records" on page 34.

CORPORATE GOVERNANCE COMMITTEE

The Corporate Governance Committee comprises all the 6 Independent Non-executive Directors, namely Liu Xiaofeng (Chairman), Qi Daqing, Tai Kwok Leung Alexander, Chen Guoming, Shi Xingquan and Guo Yanjun (who has been appointed with effect from 20 June 2011 to replace Wang Li who has resigned with effect from 20 June 2011).

The main duties of the Corporate Governance Committee include the following:

- To review the compliance of the corporate governance issues of the Company pursuant to the Listing Rules and other applicable rules and regulations;
- To review the corporate governance report to be included in the annual report and interim report of the Company; and
- To review the corporate governance policy and practices of the Company.

The Corporate Governance Committee normally meets at least twice a year for reviewing the compliance of the corporate governance issues, the corporate governance report and the corporate governance policy. The Corporate Governance Committee held two meetings during the year ended 31 December 2011 and the attendance records are set out under "Directors' Attendance Records" on page 34.

STRATEGIC INVESTMENT AND RISK CONTROL COMMITTEE

The Strategic Investment and Risk Control Committee comprises 5 members, namely Zhang Mi (Chairman), Liu Zhi, Ren Jie, Huang Dongyang and Shi Xingquan. Wang Li was member of the Strategic Investment and Risk Control Committee and has resigned with effect from 20 June 2011.

The main duties of the Strategic Investment and Risk Control Committee include the following:

- To review the investment strategies of the Company;
- To review the risk control of the Company; and
- To recommend investment strategies and risk control policy and practices to the Board.

The Strategic Investment and Risk Control Committee normally meets at least once a year for reviewing the investment and risk control issues. The Strategic Investment and Risk Control Committee held one meeting during the year ended 31 December 2011 and the attendance records are set out under "Directors' Attendance Records" on page 34.

NOMINATION COMMITTEE

The Nomination Committee was formed on 17 January 2012 and comprises 3 members, namely Zhang Mi (Chairman), Qi Daqing and Liu Xiaofeng.

The principal duties of the Nomination Committee include the following:

- To review the structure, size and composition of the Board and make recommendations regarding any proposed changes to the Board to complement the Company's corporate strategy;
- To develop and formulate relevant procedures for nomination and appointment of Directors;
- To identify suitable candidates for appointment as Directors;
- To make recommendations to the Board on appointment or re-appointment of and succession planning for Directors; and
- To assess the independence of Independent Non-executive Directors.

The Nomination Committee did not meet during the year ended 31 December 2011 as it was only formed on 17 January 2012.

EXTERNAL AUDITORS AND AUDITORS' REMUNERATION

The statement of the external auditors of the Company about their reporting responsibilities for the financial statements is set out in the "Independent Auditor's Report" on pages 61 to 62.

During the year ended 31 December 2011, the remuneration paid to the Company's auditors, Messrs KPMG, is set out below:

Category of Services	**Fees (in Renminbi)**
Audit Services	1,850,000
Non-audit Services	
— Reviewing interim financial information	650,000
Total	2,500,000

COMMUNICATIONS WITH SHAREHOLDERS AND INVESTORS

The general meetings of the Company provide a forum for communication between the Board and the Shareholders. The Chairman of the Board as well as chairmen of the Remuneration Committee, the Audit Committee, the Corporate Governance Committee and the Nomination Committee or, in their absence, other members of the respective committees normally attend the annual general meeting and other relevant Shareholders' meetings to answer questions at Shareholders' meetings. Notices to Shareholders for annual general meetings and all other general meetings will be sent to the Shareholders before such meetings pursuant to the requirement of the Listing Rules.

To promote effective communication, the Company maintains a website at http://www.hh-gltd.com, where up-to-date information and updates on the Company's business operations and developments, financial information, corporate governance practices and other information are available for public access. Investors may write directly to the Company at its principal place of business in Hong Kong or via email to ir@hhcp.com.cn for any inquiries.

SHAREHOLDERS' RIGHTS

To safeguard Shareholders' interests and rights, separate resolutions are proposed for each substantially separate issue at Shareholders' meetings, including the election of individual Directors.

All resolutions put forward at Shareholders' meetings will be taken by poll pursuant to the Listing Rules and the poll results will be posted on the websites of the Company and of the Stock Exchange after Shareholders' meeting.

REPORT OF THE DIRECTORS

The Board presents this annual report, together with the audited consolidated financial statements of the Group for the year ended 31 December 2011.

PRINCIPAL ACTIVITIES

The Company is an investment holding company. The Group principally engages in research, design, manufacture, setting and sale of land rigs and related parts and components, design and manufacture of the offshore drilling module. Meanwhile it also provides technical support services and drilling engineering service for clients. During the Year, the nature of principal activities of the Group has no substantial change.

RESULTS AND DISTRIBUTION

The results of the Group for the year ended 31 December 2011 are set out in the Financial Statements on pages 63 to 148 of this annual report.

The Board recommended a final dividend of HK$0.04 per Share for the year ended 31 December 2011.

SHARE CAPITAL

Changes in the share capital of the Company during the Year are set out in Note 30 to the Financial Statements.

PRE-EMPTIVE RIGHT

There is no provision of pre-emptive right under the Articles of Association and the laws of the Cayman Islands stipulating that the Company shall offer new Shares to existing Shareholders in proportion.

PURCHASE, SALE OR REPURCHASE OF THE LISTED SECURITIES OF THE COMPANY

The Company did not purchase, sell or repurchase any of its Shares during the year ended 31 December 2011.

RESERVES

As of 31 December 2011, the Group has a total of approximately RMB3,759 million worth of reserve. Details of movements in the reserves of the Group during the Year are set out in the consolidated statement of changes in equity in the Financial Statements.

SUBSIDIARIES

Details of the Company's principal subsidiaries as of 31 December 2011 are set out in Note 15 to the Financial Statements.

SIGNIFICANT CONTRACT

No contract of significance was entered into between the Company and its any subsidiaries and the Controlling Shareholders.

DIRECTORS

The Directors of the Company during the Year and as of the date of this annual report are:

EXECUTIVE DIRECTORS

Mr. Zhang Mi[2,4,6]	(Chairman, appointed on 18 January 2008)
Mr. Ren Jie[4]	(Appointed on 18 January 2008)
Mr. Liu Zhi[4]	(Appointed on 26 May 2008)

NON-EXECUTIVE DIRECTORS

Mr. Siegfried Meissner	(Appointed on 26 May 2008)
Mr. Huang Dongyang[4]	(Appointed on 14 April 2010)

INDEPENDENT NON-EXECUTIVE DIRECTORS

Mr. Liu Xiaofeng[1,2,3,6]	(Appointed on 18 January 2008)
Mr. Qi Daqing[1,2,3,6]	(Appointed on 18 January 2008)
Mr. Tai Kwok Leung, Alexander[1,3]	(Appointed on 18 January 2008)
Mr. Chen Guoming[1,3]	(Appointed on 18 January 2008)
Mr. Shi Xingquan[1,3,4]	(Appointed on 14 April 2009)
Mr. Guo Yanjun[1,3,5]	(Appointed on 20 June 2011)
Mr. Wang Li[1,3,4]	(Appointed on 18 January 2008 and resigned on 20 June 2011)

Notes:

1. Audit Committee Members
2. Remuneration Committee Members
3. Corporate Governance Committee Members
4. Strategic Investment and Risk Control Committee Members
5. Mr. Guo Yanjun has been appointed as the member of Audit Committee and Corporate Governance Committee of the Company with effect from 20 June 2011
6. Nomination Committee has been formed on 17 January 2012

In accordance with the Articles of Association, one third of the Directors (or closest to but not less than one third if the number of Directors is not three or a multiple of three) shall retire from office by rotation at each annual general meeting and each Director is required to retire at least once every three years and any Director appointed by the board shall hold office only until the next general meeting and shall then be eligible for re-election at the meeting. Mr. Ren Jie, Mr. Siegfried Meissner, Mr. Qi Daqing, Mr. Shi Xingquan and Mr. Guo Yanjun will retire from office by rotation at the forthcoming annual general meeting and will be eligible for re-election.

According to the independent guidelines under the Listing Rules, the Company has received the annual confirmation of their independence from each Independent Non-executive Director, and the Company still considers such Directors as independent.

DIRECTORS' SERVICE CONTRACTS

Each of the Directors of the Company is engaged on a service contract for a term of not exceeding 3 years. The appointment may be terminated by not less than 3 months' written notice, except for Mr. Siegfried Meissner whose appointment may be terminated by not less than 1 month's written notice. The Directors shall retire by rotation and be eligible for re-election subject to the Articles of Association of the Company.

None of the Directors has a service contract with the Company which is not determinable by the Company within one year without payment of compensation, other than statutory compensation.

DIRECTORS' INTERESTS IN CONTRACTS

Save as disclosed under the paragraph "Continuing connected transactions" below, none of the Directors directly or indirectly had any material interest in the contracts of significance in relation to the Group's business to which the Company or its holding company or any of its subsidiaries was a party at the end of the year or at any time during the Year.

REMUNERATION FOR DIRECTORS AND SENIOR MANAGEMENT

For the year ended 31 December 2011, details of remuneration for the Directors and Senior Management are set out in Notes 8 and 9 to the Financial Statements.

DIRECTORS' AND CHIEF EXECUTIVES' INTERESTS AND/OR SHORT POSITIONS IN THE SHARES AND UNDERLYING SHARES OF THE COMPANY OR ANY ASSOCIATED CORPORATION

At 31 December 2011, the interests and short positions of each Director and Chief Executive in the Shares and underlying Shares of the Company and its associated corporations (within the meaning of the SFO), as recorded in the register required to be kept by the Company under Section 352 of Part XV of the SFO or as notified to the Company and the Stock Exchange pursuant to the Model Code contained in Appendix 10 to the Listing Rules were as follows:

A) ORDINARY SHARES OF HK$0.1 EACH OF THE COMPANY

	Long/ Short position	Nature of interest	Number of shares held	% of the issued share capital of the Company
Mr. Zhang Mi	Long	Personal interest, corporate interest and settlor of a discretionary trust	1,572,181,037(1)(5)	48.77%
Mr. Ren Jie	Long	Personal interest, corporate interest and settlor of a discretionary trust	1,572,181,037(2)(5)	48.77%
Mr. Liu Zhi	Long	Corporate interest and settlor of a discretionary trust	1,572,181,037(3)(5)	48.77%
Mr. Guo Yanjun (appointed as Independent Non-Executive Director with effect from 20 June 2011)	Long	Corporate interest	2,100,000(4)	0.07%

(1) Zhang Mi individually owns 900,000 Shares. Yi Langlin, spouse of Zhang Mi owns 2,156,000 Shares. Zhang Mi is a member of the Concert Group. He is the settlor of a discretionary trust, The ZYL Family Trust, whose trustee, through Wealth Afflux Limited, holds the entire issued share capital of Ally Smooth Investments Limited, which in turn is the beneficial owner of 36% of the issued share capital of Ample Chance International Limited, which in turn is the beneficial owner of the entire issued share capital of Ally Giant Limited which holds 1,337,727,837 Shares. The Trustee of The ZYL Family Trust owns 103,800,000 Shares.

Ren Jie, another member of the Concert Group and the settlor of a discretionary trust, The RJDJ Victory Trust, individually owns 169,000 Shares. The Trustee of The RJDJ Victory Trust owns 23,103,200 Shares. The Trustee of a discretionary trust, The LZWM Family Trust, whose settlor is Liu Zhi, another member of the Concert Group, owns 17,750,000 Shares. The Trustee of a discretionary trust, The FBX Family Trust, whose settlor is Fan Bing, another member of the Concert Group, owns 12,341,000 Shares. The Trustee of a discretionary trust, The ZHH Family Trust, whose settlor is Zuo Huixian, another member of the Concert Group, owns 12,244,400 Shares. The Trustee of a discretionary trust, The Hong Xu Family Trust, whose settlor is Zhang Xu, another member of the Concert Group, owns 11,737,400 Shares. The Trustee of a discretionary trust, The LXYY Family Trust, whose settlor is Liu Xuetian (deceased), another member of the Concert Group, owns 10,452,400 Shares. The other members of the Concert Group totally own 39,799,800 Shares.

(2) Ren Jie individually owns 169,000 Shares. Ren Jie is a member of the Concert Group. He is the settlor of a discretionary trust, The RJDJ Victory Trust, whose trustee, through Mowbray Worldwide Limited, holds approximately 41.34% of the issued share capital of Charm Moral International Limited, which in turn is the beneficial owner of approximately 19.09% of the issued share capital of Ample Chance International Limited, which in turn is the beneficial owner of the entire issued share capital of Ally Giant Limited which holds 1,337,727,837 Shares. The Trustee of The RJDJ Victory Trust owns 23,103,200 Shares.

Zhang Mi, another member of the Concert Group and the settlor of a discretionary trust, The ZYL Family Trust, individually owns 900,000 Shares. The Trustee of The ZYL Family Trust owns 103,800,000 Shares. Yi Langlin, spouse of Zhang Mi owns 2,156,000 Shares. The Trustee of a discretionary trust, The LZWM Family Trust, whose settlor is Liu Zhi, another member of the Concert Group, owns 17,750,000 Shares. The Trustee of a discretionary trust, The FBX Family Trust, whose settlor is Fan Bing, another member of the Concert Group, owns 12,341,000 Shares. The Trustee of a discretionary trust, The ZHH Family Trust, whose settlor is Zuo Huixian, another member of the Concert Group, owns 12,244,400 Shares. The Trustee of a discretionary trust, The Hong Xu Family Trust, whose settlor is Zhang Xu, another member of the Concert Group, owns 11,737,400 Shares. The Trustee of a discretionary trust, The LXYY Family Trust, whose settlor is Liu Xuetian (deceased), another member of the Concert Group, owns 10,452,400 Shares. The other members of the Concert Group totally own 39,799,800 Shares.

(3) Liu Zhi is a member of the Concert Group. He is the settlor of a discretionary trust, The LZWM Family Trust, whose trustee, through Ecotech Enterprises Corporation, holds approximately 29.33% of the issued share capital of Charm Moral International Limited, which in turn is the beneficial owner of approximately 19.09% of the issued share capital of Ample Chance International Limited, which in turn is the beneficial owner of the entire issued share capital of Ally Giant Limited which holds 1,337,727,837 Shares. The Trustee of The LZWM Family Trust owns 17,750,000 Shares.

Zhang Mi and Ren Jie, the other two members of the Concert Group, collectively hold 1,069,000 Shares. The Trustees of the two discretionary trusts, whose settlors are Zhang Mi and Ren Jie respectively, collectively own 126,903,200 Shares. Yi Langlin, spouse of Zhang Mi owns 2,156,000 Shares. The Trustee of a discretionary trust, The FBX Family Trust, whose settlor is Fan Bing, another member of the Concert Group, owns 12,341,000 Shares. The Trustee of a discretionary trust, The ZHH Family Trust, whose settlor is Zuo Huixian, another member of the Concert Group, owns 12,244,400 Shares. The Trustee of a discretionary trust, The Hong Xu Family Trust, whose settlor is Zhang Xu, another member of the Concert Group, owns 11,737,400 Shares. The Trustee of a discretionary trust, The LXYY Family Trust, whose settlor is Liu Xuetian (deceased), another member of the Concert Group, owns 10,452,400 Shares. The other members of the Concert Group totally own 39,799,800 Shares.

(4) Guo Yanjun owns 2,100,000 Shares through his directly wholly-owned company, Long Apex Limited.

(5) Concert Group is defined in the prospectus of the Company dated 25 February 2008.

B) SHARE OPTIONS OF THE COMPANY

	Long/Short position	Number of options held — Personal interest	Number of options held — Interest of the Concert Group
Mr. Zhang Mi	Long	13,837,000	26,353,000
Mr. Ren Jie	Long	5,687,000	34,503,000
Mr. Liu Zhi	Long	5,173,000	35,017,000
Mr. Qi Daqing	Long	2,000,000	—
Mr. Liu Xiaofeng	Long	2,000,000	—
Mr. Tai Kwok Leung, Alexander	Long	1,700,000	—
Mr. Chen Guoming	Long	1,500,000	—
Mr. Shi Xingquan	Long	1,500,000	—

	Long/Short position	Number of options held — Personal interest	Number of options held — Interest of the Concert Group
Mr. Guo YanJun (appointed as Independent Non-Executive Director with effect from 20 June 2011)	Long	850,000	—
Mr. Wong Li (resigned as Independent Non-Executive Director with effect from 20 June 2011)	Long	750,000	—

Saved as disclosed above, at 31 December 2011, none of the Directors and Chief Executives (including their spouse and children under 18 years of age) had any interest in, or had been granted, or exercised, any rights to subscribe for Shares (or warrants or debentures, if applicable) of the Company and its associated corporations required to be disclosed pursuant to the SFO.

SUBSTANTIAL SHAREHOLDERS' INTERESTS OR/AND SHORT POSITIONS IN THE SHARES AND UNDERLYING SHARES OF THE COMPANY

The register of substantial shareholders required to be kept under section 336 of Part XV of the SFO shows that, at 31 December 2011, the Company had been notified of the following substantial shareholders' interests and short positions, being 5% or more of the Company's issued share capital. These interests are in addition to those disclosed above in respect of the Directors and Chief Executives of the Company.

		Number of shares held						
		Personal interest						
Name	Long/Short Position	Share option	Shares Interest	Corporate interest	Corporate interest and settlor of a discretionary trust	Interest of the Concert Group	Total	% of the issued share capital of the Company
Ally Giant Limited	Long	–	1,337,727,837	–	–	274,643,200	1,612,371,037(1)	50.01%
Ample Chance International Limited	Long	–	–	1,337,727,837	–	274,643,200	1,612,371,037(2)	50.01%
Wealth Afflux Limited	Long	–	–	1,337,727,837	–	274,643,200	1,612,371,037(3)	50.01%
Ally Smooth Investments Limited	Long	–	–	1,337,727,837	–	274,643,200	1,612,371,037(3)	50.01%
Equity Trustee Limited	Long	–	–	–	1,558,722,237	–	1,558,722,237 (3)(5)(6)(9)(10)(14)(20)(22)	48.35%
Charm Moral International Limited	Long	–	–	1,337,727,837	–	274,643,200	1,612,371,037(4)	50.01%
Mowbray Worldwide Limited	Long	–	–	1,337,727,837	–	274,643,200	1,612,371,037(5)	50.01%
Ecotech Enterprises Corporation	Long	–	–	1,337,727,837	–	274,643,200	1,612,371,037(6)	50.01%
Mr. Zheng Yong	Long	2,085,000	11,549,000	1,337,727,837	–	261,009,200	1,612,371,037(7)	50.01%
Beauty Clear Holdings Limited	Long	–	–	1,337,727,837	–	274,643,200	1,612,371,037(8)	50.01%
Mr. Zuo Huixian	Long	1,734,000	–	–	1,349,972,237	260,664,800	1,612,371,037(9)	50.01%
Vast & Fast Corporation	Long	–	–	1,337,727,837	–	274,643,200	1,612,371,037(9)	50.01%
Mr. Zhang Xu	Long	1,833,000	–	–	1,349,465,237	261,072,800	1,612,371,037(10)	50.01%
Cavendish Global Corporation	Long	–	–	1,337,727,837	–	274,643,200	1,612,371,037(10)	50.01%
Elegant Scene International Limited	Long	–	–	1,337,727,837	–	274,643,200	1,612,371,037(11)	50.01%

Name	Long/ Short Position	Personal interest Share option	Personal interest Shares Interest	Corporate interest	Number of shares held Corporate interest and settlor of a discretionary trust	Interest of the Concert Group	Total	% of the issued share capital of the Company
Mr. Wang Jiangyang	Long	941,000	4,772,600	1,337,727,837	–	268,929,600	1,612,371,037(11)	50.01%
Mr. Chen Jun	Long	872,000	2,640,400	1,337,727,837	–	271,130,800	1,612,371,037(12)	50.01%
Believe Power International Limited	Long	–	–	1,337,727,837	–	274,643,200	1,612,371,037(13)	50.01%
Mr. Fan Bing	Long	1,744,000	–	–	1,350,068,837	260,558,200	1,612,371,037(14)	50.01%
Brondesbury Enterprises Limited	Long	–	–	1,337,727,837	–	274,643,200	1,612,371,037(14)	50.01%
Mr. Zhang Yanyong	Long	1,480,000	10,479,600	1,337,727,837	–	262,683,600	1,612,371,037(15)	50.01%
Mr. Ao Pei	Long	683,000	727,400	1,337,727,837	–	273,232,800	1,612,371,037(16)	50.01%
Mr. Tian Diyong	Long	550,000	416,400	1,337,727,837	–	273,676,800	1,612,371,037(17)	50.01%
Mr. Shen Dingjian	Long	262,000	798,000	1,337,727,837	–	273,583,200	1,612,371,037(18)	50.01%
Benefit Way International Limited	Long	–	–	1,337,727,837	–	274,643,200	1,612,371,037(19)	50.01%
Mr. Liu Xuetian (deceased)	Long	–	–	–	1,348,180,237	264,190,800	1,612,371,037(20)	50.01%
Dobson Global Inc.	Long	–	–	1,337,727,837	–	274,643,200	1,612,371,037(20)	50.01%
Ms. Qu Yihong	Long	–	–	1,348,180,237	–	264,190,800	1,612,371,037(21)	50.01%
Ms. Liu Ying	Long	–	–	1,348,180,237	–	264,190,800	1,612,371,037(21)	50.01%
Mr. Zhou Bing	Long	1,445,000	5,689,600	–	1,337,727,837	267,508,600	1,612,371,037(22)	50.01%
Darius Enterprises Limited	Long	–	–	1,337,727,837	–	274,643,200	1,612,371,037(22)	50.01%
Ms. Lv Lan	Long	519,000	1,006,800	1,337,727,837	–	273,117,400	1,612,371,037(23)	50.01%
Mr. Tian Yu	Long	515,000	1,148,000	1,337,727,837	–	272,980,200	1,612,371,037(24)	50.01%
Mr. Li Hanqiang	Long	345,000	600	1,337,727,837	–	274,297,600	1,612,371,037(25)	50.01%
Mr. Liu Yingguo	Long	242,000	448,000	1,337,727,837	–	273,953,200	1,612,371,037(26)	50.01%
Mrs. Liu Lulu	Long	243,000	123,400	1,337,727,837	–	274,276,800	1,612,371,037(27)	50.01%
China Ocean Oilfields Services (Hong Kong) Limited	Long	–	174,425,609	–	–	–	174,425,609(28)	5.41%
China National Offshore Oil Corporation	Long	–	–	174,425,609	–	–	174,425,609(28)	5.41%
Nabors Drilling International II Limited	Long	–	450,000,000	–	–	–	450,000,000(29)	13.96%
Nabors International Management Limited	Long	–	–	450,000,000	–	–	450,000,000(29)	13.96%
Nabors Global Holdings Limited	Long	–	–	450,000,000	–	–	450,000,000(29)	13.96%
Nabors Industries Ltd.	Long		–	450,000,000	–	–	450,000,000(29)	13.96%
Carlyle Offshore Partners II. Ltd	Long	–	–	166,841,887	–	–	166,841,887(30)	5.18
DBD Cayman, Ltd	Long	–	–	166,841,887	–	–	166,841,887(30)	5.18
TCG Holdings Cayman II, L.P.	Long	–	–	166,841,887	–	–	166,841,887(30)	5.18
The Capital Group Companies, Inc.	Long	–	–	163,256,000	–	–	163,256,000(31)	5.06%
Capital Group International, Inc.	Long	–	–	163,256,000	–	–	163,256,000(31)	5.06%
Yi Langlin	Long	–	2,156,000 1,610,215,037 (family interest)	–	–	–	1,612,371,037(32)	50.01%

(1) Ally Giant Limited is wholly-owned by Ample Chance International Limited and holds 1,337,727,837 Shares.

(2) Ample Chance International Limited is owned approximately 36% by Ally Smooth Investments Limited, approximately 19.09% by Charm Moral International Limited, approximately 18.51% by Beauty Clear Holdings Limited, approximately 12.71% by Believe Power International Limited, approximately 10.50% by Benefit Way International Limited and approximately 3.19% by a corporation.

(3) The entire issued share capital of Ally Smooth Investments Limited is owned by Wealth Afflux Limited, which in turn is held by Equity Trustee Limited as trustee of The ZYL Family Trust. The ZYL Family Trust is a discretionary trust established by Zhang Mi as settlor, with Equity Trustee Limited as trustee. The beneficiaries under The ZYL Family Trust are Zhang Mi and his family members. Zhang Mi is a member of the Concert Group.

(4) Charm Moral International Limited is owned approximately 41.34% by Mowbray Worldwide Limited, approximately 29.33% by Ecotech Enterprises Corporation and approximately 29.33% by Zheng Yong.

(5) Approximately 41.34% of the issued share capital of Charm Moral International Limited is owned by Mowbray Worldwide Limited, which in turn is held by Equity Trustee Limited as trustee of The RJDJ Victory Trust. The RJDJ Victory Trust is a discretionary trust established by Ren Jie as settlor, with Equity Trustee Limited as trustee. The beneficiaries under The RJDJ Victory Trust are Ren Jie and his family members. Ren Jie is a member of the Concert Group.

(6) Approximately 29.33% of the issued share capital of Charm Moral International Limited is held by Ecotech Enterprises Corporation, which in turn is held by Equity Trustee Limited as trustee of The LZWM Family Trust. The LZWM Family Trust is a discretionary trust, established by Liu Zhi as settlor, with Equity Trustee Limited as trustee. The beneficiaries under The LZWM Family Trust are Liu Zhi and his family members. Liu Zhi is a member of the Concert Group.

(7) Zheng Yong is the beneficial owner of approximately 29.33% of the issued share capital of Charm Moral International Limited, which is in turn the beneficial owner of approximately 19.09% of the issued share capital of Ample Chance International Limited. Zheng Yong is a member of the Concert Group.

(8) Beauty Clear Holdings Limited is owned approximately 23.63% by Vast & Fast Corporation, approximately 22.77% by Cavendish Global Corporation, approximately 5.76% by Elegant Scene International Limited, approximately 5.10% by Chen Jun, and a total of approximately 42.74% by 3 other shareholders.

(9) Approximately 23.63% of issued share capital of Beauty Clear Holdings Limited is owned by Vast & Fast Corporation, which in turn is held by Equity Trustee Limited as trustee of The ZHH Family Trust. The ZHH Family Trust is a discretionary trust, established by Zuo Huixian as settlor, with Equity Trustee Limited as trustee. The beneficiaries under The ZHH Family Trust are Zuo Huixian and his family members. Zuo Huixian is a member of the Concert Group.

(10) Approximately 22.77% of the issued share capital of Beauty Clear Holdings Limited is held by Cavendish Global Corporation, which in turn is held by Equity Trustee Limited as trustee of The Hong Xu Family Trust. The Hong Xu Family Trust is a discretionary trust, established by Zhang Xu as settlor, with Equity Trustee Limited as trustee. The beneficiaries under The Hong Xu Family Trust are Zhang Xu and his family members. Zhang Xu is a member of the Concert Group.

(11) Approximately 5.76% of the issued share capital of Beauty Clear Holdings Limited is held by Elegant Scene International Limited, which in turn is wholly-owned by Wang Jiangyang. Beauty Clear Holdings Limited is the beneficial owner of approximately 18.51% of the issued share capital of Ample Chance International Limited. Wang Jiangyang is a member of the Concert Group.

(12) Chen Jun is the beneficial owner of approximately 5.10% of the issued share capital of Beauty Clear Holdings Limited, which in turn is the beneficial owner of approximately 18.51% of the issued share capital of Ample Chance International Limited. Chen Jun is a member of the Concert Group.

(13) Believe Power International Limited is owned approximately 32.72% by Brondesbury Enterprises Limited, approximately 29.16% by Zhang Yanyong, approximately 5.53% by Ao Pei, approximately 2.85% by Tian Diyong, approximately 2.24% by Shen Dingjian, and a total of approximately 27.50% by 4 other shareholders.

(14) Approximately 32.72% of the issued share capital of Believe Power International Limited is held by Brondesbury Enterprises Limited, which in turn is held by Equity Trustee Limited as trustee of The FBX Family Trust. The FBX Family Trust is a discretionary trust, established by Fan Bing as settlor, with Equity Trustee Limited as trustee. The beneficiaries under The FBX Family Trust are Fan Bing and his family members. Fan Bing is a member of the Concert Group.

(15) Zhang Yanyong is the beneficial owner of approximately 29.16% of the issued share capital of Believe Power International Limited, which in turn is the beneficial owner of approximately 12.71% of the issued share capital of Ample Chance International Limited. Zhang Yanyong is a member of the Concert Group.

(16) Ao Pei is the beneficial owner of approximately 5.53% of the issued share capital of Believe Power International Limited, which in turn is the beneficial owner of approximately 12.71% of the issued share capital of Ample Chance International Limited. Ao Pei is a member of the Concert Group.

(17) Tian Diyong is the beneficial owner of approximately 2.85% of the issued share capital of Believe Power International Limited, which in turn is the beneficial owner of approximately 12.71% of the issued share capital of Ample Chance International Limited. Tian Diyong is a member of the Concert Group.

(18) Shen Dingjian is the beneficial owner of approximately 2.24% of the issued share capital of Believe Power International Limited, which in turn is the beneficial owner of approximately 12.71% of the issued share capital of Ample Chance International Limited. Shen Dingjian is a member of the Concert Group.

(19) Benefit Way International Limited is owned approximately 35.57% by Dobson Global Inc., approximately 19.36% by Darius Enterprises Limited, approximately 6.49% by Lv Lan, approximately 3.91% by Tian Yu, approximately 3.50% by Li Hangqiang, approximately 1.52% by Liu Yingyuo, approximately 1.22% by Liu Lulu and approximately 28.43% by 6 other shareholders.

(20) Approximately 35.57% of the issued share capital of Benefit Way International Limited is held by Dobson Global Inc., which in turn is held by Equity Trustee Limited as trustee of The LXYY Family Trust. The LXYY Family Trust is a discretionary trust, established by Liu Xuetian (deceased) as settlor, with Equity Trustee Limited as trustee. The beneficiaries under The LXYY Family Trust are Liu Xuetian (deceased) and his family members. Liu Xuetian (deceased) was a member of the Concert Group and passed away on 23 January 2008.

(21) Qu Yihong and Liu Ying, family members of Liu Xuetian (deceased), are deemed to be interested in 1,348,180,237 Shares as directors of Dobson Global Inc..

(22) Approximately 19.36% of the issued share capital of Benefit Way International Limited is held by Darius Enterprises Limited, which in turn is held by Equity Trustee Limited as trustee of The Fang Zhou Family Trust. The Fang Zhou Family Trust is a discretionary trust, established by Zhou Bing as settlor, with Equity Trustee Limited as trustee. The beneficiaries under The Fang Zhou Family Trust are Zhou Bing and his family members. Zhou Bing is a member of the Concert Group.

(23) Lv Lan is the beneficial owner of approximately 6.49% of the issued share capital of Benefit Way International Limited, which in turn is the beneficial owner of approximately 10.50% of issued share capital of Ample Chance International Limited. Lv Lan is a member of the Concert Group.

(24) Tian Yu is the beneficial owner of approximately 3.91% of the issued share capital of Benefit Way International Limited, which in turn is the beneficial owner of approximately 10.50% of issued share capital of Ample Chance International Limited. Tian Yu is a member of the Concert Group.

(25) Li Hanqiang is the beneficial owner of approximately 3.50% of the issued share capital of Benefit Way International Limited, which in turn is the beneficial owner of approximately 10.50% of issued share capital of Ample Chance International Limited. Li Hanqiang is a member of the Concert Group.

(26) Liu Yingyuo is the beneficial owner of approximately 1.52% of the issued share capital of Benefit Way International Limited, which in turn is the beneficial owner of approximately 10.50% of issued share capital of Ample Chance International Limited. Liu Yingguo is a member of the Concert Group.

(27) Liu Lulu is the beneficial owner of approximately 1.22% of the issued share capital of Benefit Way International Limited, which in turn is the beneficial owner of approximately 10.50% of issued share capital of Ample Chance International Limited. Liu Lulu is a member of the Concert Group.

(28) China Ocean Oilfields Services (Hong Kong) Limited holds 174,425,609 Shares. The issued share capital of China Ocean Oilfields Services (Hong Kong) Limited was beneficially owned approximately 99.35% by China National Offshore Oil Corporation and approximately 0.65% by Overseas Oil & Gas Corporation Limited.

(29) Nabors Drilling International II Limited ("NDIL II") holds 450,000,000 Shares. NDIL II is a direct, wholly owned subsidiary of Nabors International Management Limited ("NIML"). NIML is a direct, wholly owned subsidiary of Nabors Global Holdings Limited which is in turn wholly owned by Nabors Industries Ltd.

(30) Carlyle Offshore Partners II. Ltd. owns 100% of DBD Cayman Ltd., which in turn owns 100% of TCG Holdings CaymanII, L.P., which in turn is holding subsidiaries that hold 166,841,887 Shares.

(31) The Capital Group Companies holds 163,256,000 Shares. The Capital Group Companies, Inc is a direct, wholly owned subsidiary of Capital Group International, Inc.

(32) Yi Langlin, spouse of Zhang Mi, is deemed to be interested in 1,612,371,037 Shares.

Save as disclosed above, to the best of the Directors and the Chief Executives of the Company's knowledge, as at 31 December 2011, none of the persons, other than the Directors or the Chief Executives of the Company, had interests or short positions in the Shares and underlying Shares of the Company which would fall to be disclosed to the Company under the provisions of Divisions 2 and 3 of Part XV of the SFO or recorded in the register as required under Section 336 of the SFO.

SHARE OPTION SCHEME

(A) PRE-IPO SHARE OPTION SCHEME

The principal terms of Pre-IPO share option scheme have been approved by resolutions in writing by all the Shareholders on 21 January 2008. As at the date of this report, a total of 270 eligible participants have been conditionally granted share options to subscribe for an aggregate of 60,000,000 Shares at an exercise price of offer price of HK$3.83 per Share. As at 31 December 2011, none of the grantees has exercised the share options granted to him under the Pre-IPO share option scheme and 2,564,000 shares options have been lapsed.

Each share option granted under the Pre-IPO share option scheme is exercisable within a period of five years commencing from 7 March 2008 (the "Listing Date") and the vesting period is ten years from the date of grant. As at 31 December 2011, 80% of the total number of the share options granted (if not cancelled) or 48,000,000 share options can be exercised under the Pre-IPO share option scheme.

No further options were granted under Pre-IPO share option scheme on or after the Listing Date.

(B) SHARE OPTION SCHEME AFTER LISTING

Upon conditional approval by resolution in writing by all shareholders of the Company on 21 January 2008, the Company adopted a share option scheme (the "Share Option Scheme"). Details of the Share Option Scheme are as follows:

Purpose

The Company operates the Share Option Scheme for the purpose of providing incentive and rewards to participants who contribute to the success of the Group's operation and/or for the purpose that the Group may recruit or retain high calibre employees and attract people for the Group.

The Share Option Scheme may provide the participants with opportunity of holding the Shares of the Company individually, and (a) facilitate the participants to use their best effort to improve their performance and effectiveness; and (b) attract and retain participants who are significant to long term development and profitability of the Group.

Participants

(a) any Executive Director, employee or proposed employee (whether full time or part time) or any member of the Group; (b) any Non-executive Director (including Independent Non-executive Director) of any member of the Group; (c) any supplier of goods or services to any member of the Group; (d) any customer of any member of the Group; (e) any advisor, consultant, any person or entity with professional or other services who provides research, development or other technical support to any member of the Group; (f) any shareholder of any member of the Group or any holder of any securities issued by any member of the Group; (g) any joint venture, business or strategic alliance partner of any member of the Group; (h) discretionary trust whose discretionary objects are as follows: any Executive Director, employee or prospective employee (whether full time or part time) and any Non-executive Director (including Independent Non-executive Director) of any member of the Group, any supplier of goods or services to any member of the Group, any customer of any member of the Group, any advisor, consultant, any person or entity with professional or other services who provides research, development or other technical support to any member of the Group, any shareholder of any member of the Group or any holder of any securities issued by any member of the Group and any joint venture, business or strategic alliance partner of any member of the Group.

Total number of Shares available for issue under the Share Option Scheme and % of issued share capital as at the date of this annual report

The total number of Shares available for issue under the Share Option Scheme upon exercise of all outstanding share options granted and yet to be exercised (excluding share options lapsed in accordance with the terms of the Share Option Scheme) was 66,605,300 Shares, representing approximately 2.07% of the issued share capital of the Company as at the date of this annual report.

Maximum entitlement of each participant

The maximum number of Shares issued and to be issued upon exercise of the share options (including those already exercised and outstanding share options) granted to each eligible participant under the Share Option Scheme in any 12-month period (until date of grant of share options) is limited to 1% of the Shares of the Company in issue. Any further grant of share options in excess of this limit is subject to Shareholders' approval in a general meeting but the participant and its associates must abstain from voting at the meeting. In this case, the Company must dispatch a circular to Shareholders, containing identity of the participant, number of share options to be granted to the participant (and share options previously granted to this participant) and related terms and all other data as required by the Listing Rules. The number and terms of the share options to be granted to this participant (including exercise price) must be determined before approval by the Shareholders. In calculating the subscription price, the date on which Board meeting is held for proposed further grant of share options is deemed as date of grant.

The period in which Shares must be taken up for under the Share Option Scheme

Share option may be exercised at any time during the period expiring tenth anniversary from the date of grant of share option as determined by the Board of Directors, but subject to early termination provisions of the terms of Share Option Scheme.

The minimum period, if any, for which a share option must be held before it can be exercised

Unless otherwise determined by the Board and stated in the offer of grant of share options to the grantee, there is no minimum period for which a share option must be held before it can be exercised.

Amounts to be paid on acceptance of share options

Grantee of share option must pay HK$1.00 to the Company upon acceptance of share option offer.

Basis of determining the exercise price

The subscription price of the share option granted under the Share Option Scheme is solely determined and notified to the participants by the Board of Directors, but not less than the highest of (i) the closing price of the Company's Shares as stated in the daily quotations sheet of the Stock Exchange on the date of the grant; (ii) the average closing price of the Company's Shares as stated in the Stock Exchange's daily quotations sheet for the five trading days immediately preceding the date of the grant; and (iii) the nominal value of the Company's Shares as at date of grant.

Condition and Termination of the share options

The Share Option Scheme is conditional on the Listing Committee of the Stock Exchange granting approval of the listing of, and permission to deal in, the Shares which may fall to be issued pursuant to the exercise of share options granted under the Share Option Scheme. The Company (by virtue of resolutions of general meeting) or the Board may at any time terminate the operation of the Share Option Scheme, under which circumstance, there will be no new share options to be granted, but the share options granted before the termination will continue to be valid and exercisable under the provisions of the Share Option Scheme.

The remaining life of the Share Option Scheme

Subject to early termination of the Share Option Scheme pursuant to the terms thereof, the Share Option Scheme shall remain valid and effective for 10 years commencing on the date of its adoption on 21 January 2008.

On 15 April 2009, share options to subscribe for 60,000,000 Shares were granted to the eligible participants at an exercise price of HK$1.27 per Share under the Share Option Scheme. The share options are exercisable on or after 1 December 2009 by the grantees in the following manners: (1) up to 30% of the share options granted to each grantee from 1 December 2009 to 14 April 2010; (2) up to 60% of the share options granted to each grantee on or before 14 April 2011; (3) all the remaining share options granted to each grantee on or after 15 April 2011, and in each case, not later than 14 April 2009. The valid period of the share options is up to 14 April 2019.

On 11 October 2010, share options to subscribe for 2,200,000 Shares were granted to the grantees at an exercise price of HK$1.05 per Share under the Share Option Scheme. The share options are exercisable on or after 25 October 2010 by the grantees in the following manners: (1) up to 40% of the share options granted to each grantee from 25 October 2010 to 10 October 2011; (2) up to 70% of the share options granted to each grantee on or before 10 October 2012; (3) all the remaining share options granted to each grantee on or after 11 October 2012; and in each case, not later than 10 October 2020. The valid period of the share options is up to 10 October 2020.

On 20 June 2011, share options to subscribe for a total of 7,600,000 shares were granted to the grantees at an exercise price of HK$0.83 per Share under the Share Option Scheme. The exercise price of HK$0.83 represents the highest of (i) the closing price of HK$0.78 per Share as stated in the daily quotations sheet issued by the Stock Exchange on the date of grant of the share options, i.e. 20 June 2011 (the "Date of Grant"); (ii) the average closing price of HK$0.83 per Share as stated in the daily quotations sheets issued by the Stock Exchange for the five business days immediately preceding the Date of Grant; and (iii) the nominal value of Share, which is HK$0.10. The share options are exercisable on or after 19 July 2011 by the grantees with details as follows: (1) up to 30% of the share options granted to each grantee from 19 July 2011 to 19 June 2012; (2) up to 60% of the share options granted to each grantee on or before 19 June 2013; (3) all the remaining share options granted to each grantee on or after 20 June 2013; and in each case, not later than 19 June 2021. The valid period of the share options is up to 19 June 2021.

Particulars and movements of share options under the Share Option Scheme during the year ended 31 December 2011 were as follows:

NUMBER OF SHARE OPTIONS

Name or category of participant	Outstanding as at 01/01/2011	Granted during the year ended 31 December 2011	Exercised during the year ended 31 December 2011	Lapsed during the year ended 31 December 2011	Cancelled during the year ended 31 December 2011	Outstanding as at 31/12/2011	Date of grant (DD/MM/YY)	Exercise period (DD/MM/YY)	Exercise price per Share HK$	Price per share immediately preceding the grant date of share options HK$
Directors										
Mr. Zhang Mi	3,937,000	–	–	–	–	3,937,000	15/04/2009	01/12/2009-14/04/2019	1.27	1.29
Mr. Liu Zhi	2,373,000	–	–	–	–	2,373,000	15/04/2009	01/12/2009-14/04/2019	1.27	1.29
Mr. Ren Jie	2,587,000	–	–	–	–	2,587,000	15/04/2009	01/12/2009-14/04/2019	1.27	1.29
Mr. Chen Guoming	750,000	–	–	–	–	750,000	15/04/2009	01/12/2009-14/04/2019	1.27	1.29
	–	750,000	–	–	–	750,000	20/06/2011	19/07/2011-19/06/2021	0.83	0.79
Mr. Liu Xiaofeng	1,000,000	–	–	–	–	1,000,000	15/04/2009	01/12/2009-14/04/2019	1.27	1.29
	–	1,000,000	–	–	–	1,000,000	20/06/2011	19/07/2011-19/06/2021	0.83	0.79
Mr. Qi Daqing	1,000,000	–	–	–	–	1,000,000	15/04/2009	01/12/2009-14/04/2019	1.27	1.29
	–	1,000,000	–	–	–	1,000,000	20/06/2011	19/07/2011-19/06/2021	0.83	0.79
Mr. Tai Kwok Leung,	850,000	–	–	–	–	850,000	15/04/2009	01/12/2009-14/04/2019	1.27	1.29
Alexander	–	850,000	–	–	–	850,000	20/06/2011	19/07/2011-19/06/2021	0.83	0.79
Mr. Shi Xingquan	750,000	–	–	–	–	750,000	15/04/2009	01/12/2009-14/04/2019	1.27	1.29
	–	750,000	–	–	–	750,000	20/06/2011	19/07/2011-19/06/2021	0.83	0.79
Mr.Guo Yanjun (appointed as Independent Non-Executive Directors with effect from 20 June 2011)	–	850,000	–	–	–	850,000	20/06/2011	19/07/2011-19/06/2021	0.83	0.79
Mr. Wong Li (resigned as Independent Non-Executive Director with effect form 20 June 2011)	750,000	–	–	–	–	750,000	15/04/2009	01/12/2009-14/04/2019	1.27	1.29
Sub-total	13,997,000	5,200,000	–	–	–	19,197,000				
Substantial Shareholders										
Mr. Zheng Yong	695,000	–	–	–	–	695,000	15/04/2009	01/12/2009-14/04/2019	1.27	1.29
Mr. Zuo Huixian	674,000	–	–	–	–	674,000	15/04/2009	01/12/2009-14/04/2019	1.27	1.29
Mr. Zhang Xu	642,000	–	–	–	–	642,000	15/04/2009	01/12/2009-14/04/2019	1.27	1.29
Mr. Wang Jiangyang	301,000	–	–	–	–	301,000	15/04/2009	01/12/2009-14/04/2019	1.27	1.29
Mr. Chen Jun	332,000	–	–	–	–	332,000	15/04/2009	01/12/2009-14/04/2019	1.27	1.29
Mr. Fan Bing	569,000	–	–	–	–	569,000	15/04/2009	01/12/2009-14/04/2019	1.27	1.29
Mr. Zhang Yanyong	480,000	–	–	–	–	480,000	15/04/2009	01/12/2009-14/04/2019	1.27	1.29
Mr. Ao Pei	243,000	–	–	–	–	243,000	15/04/2009	01/12/2009-14/04/2019	1.27	1.29
Mr. Tian DiYong	195,000	–	–	–	–	195,000	15/04/2009	01/12/2009-14/04/2019	1.27	1.29
Mr. Shen Dingjian	87,000	–	–	–	–	87,000	15/04/2009	01/12/2009-14/04/2019	1.27	1.29
Mr. Zhou Bing	695,000	–	–	–	–	695,000	15/04/2009	01/12/2009-14/04/2019	1.27	1.29
Ms. Lv Lan	174,000	–	–	–	–	174,000	15/04/2009	01/12/2009-14/04/2019	1.27	1.29
Mr. Tian Yu	275,000	–	–	–	–	275,000	15/04/2009	01/12/2009-14/04/2019	1.27	1.29
Mr. Li Hanqiang	130,000	–	–	–	–	130,000	15/04/2009	01/12/2009-14/04/2019	1.27	1.29
Mr. Liu Yingguo	117,000	–	–	–	–	117,000	15/04/2009	01/12/2009-14/04/2019	1.27	1.29
Ms. Liu Lulu	108,000	–	–	–	–	108,000	15/04/2009	01/12/2009-14/04/2019	1.27	1.29
Sub-total	5,717,000	–	–	–	–	5,717,000				
Other										
Employee	38,520,900	–	–	1,312,600	–	37,208,300	15/04/2009	01/12/2009-14/04/2019	1.27	1.29
Employee	2,200,000	–	–	–	–	2,200,000	11/10/2010	25/10/2010-10/10/2020	1.05	1.01
Employee	–	2,400,000	–	–	–	2,400,000	20/06/2011	19/07/2011-19/06/2021	0.83	0.79
Sub-total	40,720,900	2,400,000		1,312,600		41,808,300				
Total	60,434,900	7,600,000		1,312,600		66,722,300				

RESTRICTED SHARE AWARD SCHEME

On 30 December 2011, the Board approved and adopted a restricted share award scheme in which Selected Participant(s) including any Employee or Director (including, without limitation, any Executive Directors, Non-executive Directors or Independent Non-executive Directors), any consultant or adviser (whether on any employment or contractual or honorary basis and whether paid or unpaid) of the Company or any member of the Group, who in the absolute opinion of the Board, have contributed to the Company or the Group. Pursuant to the Scheme Rules, existing Shares will be purchased by the Trustee from the market out of cash contributed by the Company and be held in trust for the relevant Selected Participant until such Shares are vested with the relevant Selected Participants in accordance with the Scheme Rules. The Scheme shall be effective for a term of 10 years commencing on the Adoption Date subject to any early termination as may be determined by the Board. The Board will implement the Scheme in accordance with the Scheme Rules including providing necessary funds to the Trustee to purchase for Shares up to 5% of the issued share capital of the Company from time to time. The Selected Participant is not entitled to receive any income or distribution, such as dividend derived from the Restricted Shares allocated to him, prior to the vesting of the Restricted Shares in the Selected Participants. The Trustee has not purchased any of the Company's Shares during the year ended 31 December 2011. An announcement regarding the Scheme was published on 30 December 2011 and capitalized terms used herein shall have the same expressions referred to in the aforesaid announcement.

CONTINUING CONNECTED TRANSACTIONS

During the Year, the Group has the following continuing connected transactions. For items 1 and 2, disclosure by way of announcement and independent shareholders' approval have been made and obtained in compliance with the requirements of Chapter 14A of the Listing Rules. For item 3, disclosure by way of announcement has been made in compliance with the requirements of Chapter 14A of the Listing Rules in relation to the Renewal Purchase Framework Agreement (as defined below).

1. SALES FRAMEWORK AGREEMENT ENTERED INTO WITH NABORS GROUP

Nabors Group comprises of Nabors Industries Ltd. and its subsidiaries. Nabors Group, through Nabors International II Limited, holds approximately 13.96% equity interest in the Company and hence is a connected person of the Company under Chapter 14A of the Listing Rules.

In order to expand the business with the Nabors Group, the Company and Nabors Ltd. Industries entered into a renewal sales framework agreement on 19 November 2010 (the "Renewal Sales Framework Agreement") for a term commencing from 1 January 2011 and ending on 31 December 2013 or when the Nabors Group and its associates ceased to be connected persons of the Company (whichever is the earlier). Pursuant to the Renewal Sales Framework Agreement, the Group shall sell to the Nabors Group certain types of drilling rigs and workover rigs and their parts and components, and provision by the Group to the Nabors Group of the after-sales services and assembly of drilling rigs. The approved annual caps of the Products and Services (as defined in the Renewal Sales Framework Agreement) shall not exceed US$300 million for each of the three years ending 31 December 2013 respectively.

During the Year, the total income received by the Group from the Nabors Group in respect of sales of the Products and provision of the Services amounted to approximately RMB299,829,253.

2. PURCHASES FRAMEWORK AGREEMENT ENTERED INTO WITH NABORS GROUP

In order to expand the business with the Nabors Group, the Company and Nabors Industries Ltd. entered into a renewal purchases framework agreement on 19 November 2010 (the "Renewal Purchases Framework Agreement") for a term commencing from 1 January 2011 and ending on 31 December 2013 or when the Nabors Group and its associates ceased to be connected persons of the Company (whichever is the earlier). Pursuant to the Renewal Purchases Framework Agreement, the Group shall purchase from the Nabors Group rig parts and components which mainly consist of top drives and provision by the Nabors Group to the Group of the after-sales services. The approved annual caps of the Products and Services (as defined in the Renewal Purchases Framework Agreement) shall not exceed US$40 million for each of the three years ending 31 December 2013 respectively.

During the Year, no purchases of the Products and Services was made by the Group from the Nabors Group.

3. PURCHASES FRAMEWORK AGREEMENT ENTERED INTO WITH HONTAI COMPANY

Hongtai Company is owned as to 73.125% by the spouses of the Concert Group, therefore Hongtai Company is a connected person of the Company according to Rule 14A. 11(4) of the Listing Rules.

Honghua Company entered into a purchase framework agreement on 16 December 2009 (the "Renewal Purchases Framework Agreement") for a term of three years commencing from 1 January 2010 and ending on 31 December 2012.

Pursuant to the Renewal Purchases Framework Agreement, Honghua Company shall purchase low value consumables, auxiliary accessories, tools, welding materials and work-protection items from Hongtai Company. It is expected that the maximum aggregate annual purchase price payable by Honghua Company to Hongtai Company under the Renewal Purchases Framework Agreement shall not exceed RMB28 million, RMB26 million and RMB26 million for each of the three financial years ending 31 December 2012 respectively.

During the Year, the total purchases made by the Group from Hongtai Company amounted to approximately RMB15,438,895.

Our Independent Non-executive Directors have reviewed the continuing connected transactions and confirmed that these transactions have been entered into:

(1) in the ordinary and usual course of the business of the Group;

(2) either on normal commercial terms or on terms no less favourable to the Group than terms available to or from independent third parties; and

(3) in accordance with the relevant agreements governing them on terms that are fair and reasonable and in the interest of the Shareholders as a whole.

The Company's auditors were engaged to report on the Group's continuing connected transactions in accordance with Hong Kong Standard on Assurance Engagements 3000 "Assurance Engagements Other Than Audits or Reviews of Historical Financial Information" and with reference to Practice Note 740 "Auditor's Letter on Continuing Connected Transactions under the Hong Kong Listing Rules" issued by the Hong Kong Institute of Certified Public Accountants. The auditors have issued their unqualified letter containing their findings and conclusions in respect of the continuing connected transactions disclosed by the Group in pages 56 to 58 of this annual report in accordance with Rule 14A.38 of the Listing Rules.

BANK LOANS

Details of our bank loans and other borrowings are set out in Note 23 to the Financial Statements.

USE OF PROCEEDS FROM INITIAL PUBLIC OFFERINGS

On 7 March 2008, the Company issued 833,360,000 ordinary shares at a price of HK$3.83 per Share on the main board of the Stock Exchange, raising a net capital (total capital net of underwriting fee and payables for Global Offering) of approximately HK$2.958 billion. In view of current economic and financial situations, and the resources price including land and steel have a big drop, the investment amount of the Group especially budgeted for the offshore equipment project is forecasted to decrease. In order to enhance operation flexibility of the Group, the Company changed the intended use of the net proceeds from IPO (the details are set out in the announcement published on 26 November 2008 and 3 December 2010). Therefore, as of 31 December 2011, the intended use of the net proceeds and the usage status are as follows:

(1) Proceeds of around 33% is to be used for construction of an offshore equipment base in the eastern coastal area of China, which will manufacture auto-lift drilling rigs, fixed drilling rigs & huge hardwares, including acquisition of leasehold coastal area land and coastlines of Shanghai or the nearby province, investment in R&D of new equipments and construction of new factory buildings. This part of fund around amount to around HK$975 million, among which HK$714 million has been utilized and HK$261 million is retained.

(2) Proceeds of around 12% is to be used for expansion of production capacity, and research and development of new land drilling rigs, among which HK$354 million has been utilized and HK$0 million is retained.

(3) Proceeds of around 20% million to be used for provision of products and services for expansion of hydrocarbon exploration, exploitation and sale, oil and gas engineering services, oil and gas resources exploration and development, and other businesses in the interests of the Group. This part of fund amounts to approximately HK$592 million, among which HK$104 million has been utilized and HK$488 million is retained.

(4) Other proceeds of HK$1,037 million is to be used for working capital and current expenditure, among which HK$1,037 million has been utilized.

As of 31 December 2011, the Group deposited the part of net proceeds which has not been immediately used for above-mentioned purposes as fixed or demand deposits.

FINANCIAL SUMMARY

Our financial summary for the past five years are set out in the section headed "Five-Year Financial Highlights" of this annual report.

STAFF RETIREMENT AND BENEFIT SCHEME

Details of the staff retirement and benefit scheme are set out in Notes 6(b), 25 & 26 to the Financial Statements.

FIXED ASSETS

Details of the changes of the fixed assets of the Group are set out in Note 12 to the Financial Statements.

MAJOR CUSTOMERS AND SUPPLIERS

1. During the Year, the Group's five largest customers accounted for approximately 53.9% of total purchases and the largest customer was PDVSA Servicios Petroleros, S.A., accounting for approximately 18.5% of revenue. The others in descending proportions were Eurasia Drilling Company Ltd. (EDC)., Andrews Techologies, Inc., Velesa Trading Limited and Geotools FZE, which accounting for approximately 13.1%, 9.9%, 6.3% and 6.1% respectively.

2. During the Year, the Group's five largest suppliers in total accounted for approximately 30.0% of total purchase, and the largest supplier was National Oilwell Varco, accounting for approximately 11.5% of total purchase. The others in descending proportions were Chengdu Zhongyeda Co., Ltd., China MCC20 Group Co., Ltd., Grand Rig International Limited, and Rongsheng Machinery Manufacture Ltd. of Huabei Oilfield, Hebei, which accounting for approximately 8.4%, 4.2%, 3.6% and 2.3% respectively.

3. None of the Directors of the Company, their associates or any Shareholder (which to the knowledge of the Directors owns more than 5% of the Company's share capital) had an interest in the above suppliers or customers.

ENTRUST DEPOSITS AND ENTRUST LOANS

As at 31 December 2011, the Company has no entrust deposits or entrust loans being placed with commercial banks or non-commercial banks and other finance institutions.

TAXATION POLICY

The details of the Group's applicable income taxation policy and payment of income tax are set out in Note 7 to the Financial Statements.

SUFFICIENCY OF PUBLIC FLOAT

Based on the information that is publicly available to the Company and within the knowledge of the Directors as at the date of this report, the Company has maintained sufficient public float since the Listing Date.

AUDITOR

A resolution to renew the appointment of KPMG as auditor of the Company will be proposed at the forthcoming annual general meeting of the Company.

By the order of the Board
Honghua Group Limited
Zhang Mi
Chairman

Hong Kong, 20 March 2012

INDEPENDENT AUDITOR'S REPORT

TO THE SHAREHOLDERS OF HONGHUA GROUP LIMITED

(Incorporated in the Cayman Islands with limited liability)

We have audited the consolidated financial statements of Honghua Group Limited (the "company") and its subsidiaries (together "the group") set out on pages 63 to 148, which comprise the consolidated and company balance sheets as at 31 December 2011, and the consolidated income statement, the consolidated statement of comprehensive income, the consolidated statement of changes in equity and the consolidated cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory information.

DIRECTORS' RESPONSIBILITY FOR THE CONSOLIDATED FINANCIAL STATEMENTS

The directors of the company are responsible for the preparation of consolidated financial statements that give a true and fair view in accordance with International Financial Reporting Standards issued by the International Accounting Standards Board and the disclosure requirements of the Hong Kong Companies Ordinance, and for such internal control as the directors determine is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

AUDITOR'S RESPONSIBILITY

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. This report is made solely to you, as a body, and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

We conducted our audit in accordance with Hong Kong Standards on Auditing issued by the Hong Kong Institute of Certified Public Accountants. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation of the consolidated financial statements that give a true and fair view in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the directors, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

OPINION

In our opinion, the consolidated financial statements give a true and fair view of the state of affairs of the company and of the group as at 31 December 2011 and of the group's profit and cash flows for the year then ended in accordance with International Financial Reporting Standards and have been properly prepared in accordance with the disclosure requirements of Hong Kong Companies Ordinance.

KPMG
Certified Public Accountants

8th Floor, Prince's Building
10 Chater Road
Central, Hong Kong

20 March 2012

CONSOLIDATED INCOME STATEMENT

For the year ended 31 December 2011 (Expressed in Renminbi)

	Note	2011 RMB'000	2010 RMB'000
Turnover	4(a)	**3,485,046**	1,877,931
Cost of sales		**(2,514,942)**	(1,497,453)
Gross profit		**970,104**	380,478
Other revenue	5	**27,444**	29,900
Other net income/(loss)	5	**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	6(a)	**(50,335)**	(59,441)
Share of profit from jointly controlled entities	16	**293**	2,801
Share of profit from an associate	17	**5,398**	—
Profit/(loss) before taxation	6	**199,212**	(176,443)
Income tax (expenses)/credit	7(a)	**(27,769)**	4,372
Profit/(loss) for the year		**171,443**	(172,071)
Attributable to:			
Equity shareholders of the company	10	**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	11	**RMB 0.0521**	RMB (0.0571)

The notes on pages 72 to 146 form part of these financial statements.

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

For the year ended 31 December 2011 (Expressed in Renminbi)

	Note	2011 RMB'000	2010 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)

The notes on pages 72 to 146 form part of these financial statements.

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	12	**678,597**	529,574
— Interests in leasehold land held for own use under operating leases	12	**181,189**	140,058
— Freehold land	12	**5,080**	5,339
	12	**864,866**	674,971
Deposits paid for acquisition of leasehold land		**192,830**	218,984
Construction in progress	13	**402,065**	77,144
Intangible assets	14	**235,994**	272,585
Interests in jointly controlled entities	16	**38,919**	41,868
Interest in an associate	17	**63,405**	—
Deferred tax assets	27(b)	**84,253**	69,341
Total non-current assets		**1,882,332**	1,354,893
Current assets			
Inventories	18	**1,544,127**	1,859,897
Trade and other receivables	19	**1,562,410**	1,217,108
Amounts due from related companies	33(b)	**64,854**	25,761
Current tax recoverable	27(a)	**34,418**	27,508
Other financial assets	20	**678,000**	473,680
Pledged bank deposits	21	**65,612**	29,072
Bank deposits maturing over three months		**9,100**	4,000
Cash and cash equivalents	22	**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	23	**499,738**	444,000
Amounts due to related companies	33(c)	**28,290**	48,206
Trade and other payables	24	**1,531,323**	1,209,911
Current tax payable	27(a)	**38,543**	11,196
Provision for product warranties	28	**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	23	**380,000**	182,318
Deferred tax liabilities	27(b)	**18,705**	12,486
Total non-current liabilities		**398,705**	194,804
Net assets		**4,174,858**	4,070,791

CONSOLIDATED BALANCE SHEET

At 31 December 2011 (Expressed in Renminbi)

	Note	**31 December 2011 RMB'000**	31 December 2010 RMB'000
Equity			
Share capital	30(c)	**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

Approved and authorised for issue by the board of directors on 20 March 2012

Zhang Mi
Director

Ren Jie
Director

The notes on pages 72 to 146 form part of these financial statements.

BALANCE SHEET

At 31 December 2011 (Expressed in Renminbi)

	Note	31 December 2011 RMB'000	31 December 2010 RMB'000
Non-current assets			
Intangible assets	14	**225,832**	272,585
Investments in subsidiaries	15	**2,580,003**	2,701,067
Total non-current assets		**2,805,835**	2,973,652
Current assets			
Other receivables		**118**	58
Cash and cash equivalents	22	**16,628**	19,890
Total current assets		**16,746**	19,948
Current liabilities			
Other payables	24	**21,582**	1,118
Amounts due to subsidiaries	29	**31,625**	28,699
Total current liabilities		**53,207**	29,817
Net current liabilities		**36,461**	9,869
Net assets		**2,769,374**	2,963,783
Equity	30(a)		
Share capital		**299,593**	299,593
Reserves		**2,469,781**	2,664,190
Total equity		**2,769,374**	2,963,783

Approved and authorised for issue by the board of directors on 20 March 2012

Zhang Mi
Director

Ren Jie
Director

The notes on pages 72 to 146 form part of these financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

For the year ended 31 December 2011 (Expressed in Renminbi)

		Attributable to equity shareholders of the company									
	Note	Share capital RMB'000 (note 30(c))	Share premium RMB'000 (note 30(d)(i))	Other reserve RMB'000 (note 30(d)(ii))	Capital reserve RMB'000 (note 30(d)(iii))	Surplus reserve RMB'000 (note 30(d)(iv))	Exchange reserve RMB'000 (note 30(d)(v))	Retained profits RMB'000	Sub-total RMB'000	Non-controlling interests RMB'000	Total equity RMB'000
At 1 January 2010		299,542	2,476,705	57,510	471,185	211,551	(77,742)	725,632	4,164,383	95,024	4,259,407
Capital injection by non-controlling interests		–	–	–	–	–	–	–	–	95	95
Acquisition of non-controlling interests	26	–	–	(38)	–	–	–	–	(38)	38	–
Equity-settled share-based transactions	26	–	–	–	17,574	–	–	–	17,574	–	17,574
Shares issued under share option schemes	26	51	814	–	(217)	–	–	–	648	–	648
Options lapsed under share option schemes		–	–	–	(224)	–	–	224	–	–	–
Total comprehensive income for the year		–	–	–	–	–	(34,872)	(184,165)	(219,037)	12,104	(206,933)
At 31 December 2010		299,593	2,477,519	57,472	488,318	211,551	(112,614)	541,691	3,963,530	107,261	4,070,791
At 1 January 2011		**299,593**	**2,477,519**	**57,472**	**488,318**	**211,551**	**(112,614)**	**541,691**	**3,963,530**	**107,261**	**4,070,791**
Capital injection by non-controlling interests		**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**5,886**	**5,886**
Equity-settled share-based transactions	26	**–**	**–**	**–**	**7,590**	**–**	**–**	**–**	**7,590**	**–**	**7,590**
Options lapsed under share option schemes	26	**–**	**–**	**–**	**(2,098)**	**–**	**–**	**2,098**	**–**	**–**	**–**
Total comprehensive income for the year		**–**	**–**	**–**	**–**	**–**	**(80,521)**	**167,984**	**87,463**	**3,128**	**90,591**
Appropriation to surplus reserve		**–**	**–**	**–**	**–**	**8,482**	**–**	**(8,482)**	**–**	**–**	**–**
At 31 December 2011		**299,593**	**2,477,519**	**57,472**	**493,810**	**220,033**	**(193,135)**	**703,291**	**4,058,583**	**116,275**	**4,174,858**

The notes on pages 72 to 146 form part of these financial statements.

CONSOLIDATED CASH FLOW STATEMENT

For the year ended 31 December 2011 (Expressed in Renminbi)

	Note	2011 RMB'000	2010 RMB'000
Operating activities			
Profit/(loss) before taxation		**199,212**	(176,443)
Adjustments for:			
Amortisation and depreciation			
— intangible assets		**34,741**	36,407
— leasehold land held for use under operating leases		**2,018**	1,771
— other fixed assets		**69,305**	51,498
Gain on other financial assets		**(20,687)**	(6,483)
Interest income		**(6,604)**	(17,208)
Interest expenses		**36,400**	36,746
Share of profit from jointly controlled entities		**(293)**	(2,801)
Share of profit from an associate		**(5,398)**	—
Loss on disposals of fixed assets		**474**	181
Gain on liquidation of a subsidiary		**(50,430)**	—
Equity-settled share-based payment expenses		**7,590**	17,574
Foreign exchange loss/(gain)		**10,762**	(12,033)
Operating profit/(loss) before change in working capital		**277,090**	(70,791)
Decrease in inventories		**213,674**	21,503
(Increase)/decrease in trade and other receivables		**(345,601)**	23,336
(Increase)/decrease in amounts due from related companies		**(39,093)**	5,347
(Increase)/decrease in pledged bank deposits		**(36,540)**	1,591
Increase in trade and other payables		**177,334**	235,350
(Decrease)/increase in amounts due to related companies		**(19,916)**	27,696
Increase in provision for product warranties		**5,505**	159
Cash generated from operations		**232,453**	244,191
Income tax paid		**(18,314)**	(25,955)
Net cash generated from operating activities		**214,139**	218,236

For the year ended 31 December 2011 (Expressed in Renminbi)

	Note	2011 RMB'000	2010 RMB'000
Investing activities			
Payment for addition of fixed assets (excluding interests in leasehold land)		**(104,576)**	(70,097)
Proceeds from disposals of fixed assets		**2,193**	373
Payment for construction in progress		**(222,385)**	(114,871)
Acquisition of interest in an associate		**(60,000)**	—
Payment for development project costs		**(10,234)**	—
Payment for acquisition of leasehold land		**(16,995)**	—
Interest received		**6,902**	29,596
Payment for purchase of other financial assets		**(1,879,380)**	(1,036,740)
Proceeds from sale of other financial assets		**1,695,747**	563,060
(Increase)/decrease in bank deposits maturing over three months		**(5,100)**	538,898
Net cash used in investing activities		**(593,828)**	(89,781)
Financing activities			
Proceeds from new bank loans		**829,183**	424,817
Repayment of bank loans		**(575,397)**	(1,096,359)
Proceeds from shares issued under share option schemes		**—**	648
Capital injection by non-controlling interests		**5,886**	97
Interest paid		**(15,226)**	(47,213)
Net cash generated from/(used in) financing activities		**244,446**	(718,010)
Net decrease in cash and cash equivalents		**(135,243)**	(589,555)
Cash and cash equivalents at 1 January		**1,002,727**	1,603,316
Effect of foreign exchange rate changes		**(15,637)**	(11,034)
Cash and cash equivalents at 31 December	22	**851,847**	1,002,727

The notes on pages 72 to 146 form part of these financial statements.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

1 GENERAL INFORMATION

Honghua Group Limited (the "company") was incorporated in the Cayman Islands on 15 June 2007 as an exempted company with limited liability under the Companies Law, Cap 22 (Law 3 of 1961, as consolidated and revised) of the Cayman Islands.

The consolidated financial statements for the year ended 31 December 2011 comprise the company and its subsidiaries (collectively referred to as the "group") and the group's interests in an associate and jointly controlled entities.

On 9 May 2011, the group completed the acquisition of 25.71% equity interests in Chengdu Jinkong Financial Leasing Co., Ltd ("Chengdu Jinkong") at a total consideration of RMB 60,000,000. Chengdu Jinkong is a limited liability company established in the People's Republic of China (the "PRC") engaged in the provision of lease financing.

On 26 July 2011, Honghua Holdings Limited ("Honghua Holdings") entered into an agreement with SBI Offshore Limited, an equipment manufacturing company listed in Singapore, to set up HS Offshore Pte Ltd ("HS Offshore") in which the Group held 70% equity interests. HS Offshore engaged primarily in the sales and manufacturing of equipment for the international marine/offshore industry and other marine/offshore related business.

On 5 December 2011, Sichuan Honghua Petroleum Equipment Co. Ltd. ("Honghua Company") entered into an agreement with Gansu Huateng Oil & Gas Equipment Manufacturing Co., Ltd ("Gansu Huateng") pursuant to which Honghua Company will establish Gansu Hongteng Oil & Gas Equipment Manufacturing Co., Ltd ("Gansu Hongteng"), and Gansu Hongteng will purchase certain assets from Gansu Huateng. Thereafter, Honghua Company and Gansu Huateng will make capital contribution towards Gansu Hongteng in cash and in assets respectively, as a result of which Honghua Company and Gansu Huateng will respectively own 70% and 30% of the equity interest in Gansu Hongteng. On 28 December 2011, Honghua Company established Gansu Hongteng in the PRC, the registered capital of which is RMB 42,000,000. As at 31 December 2011, Honghua Company had made capital injection of RMB 42,000,000 into Gansu Hongteng and held 100% of its equity interests.

On 8 August 2011, the group de-registered a wholly-owned subsidiary, Sichuan Hongcheng Business Trading Co., Ltd. The subsidiary had remained dormant and derived no revenue since its establishment through its de-registration.

The changes in composition of the group do not have a material effect on the results of operation and financial position of the group for the year presented.

2 SIGNIFICANT ACCOUNTING POLICIES

(a) Statement of compliance

These 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 Accounting Standards Board ("IASB") and the disclosure requirements of the Hong Kong Companies Ordinance. These 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. A summary of the significant accounting policies adopted by the group is set out below.

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 2(c) provides information on any changes in accounting policies resulting from the initial application of these developments to the extent that they are relevant to the group for the current and prior accounting periods reflected in these financial statements.

(b) Basis of preparation of the financial statements

The financial statements are presented in Renminbi ("RMB"), rounded to the nearest thousand yuan. Items included in the financial statements of each entity in the group are measured using the currency that best reflects the economic substance of the underlying events and circumstances relevant to that entity ("functional currency"). The company has its functional currency in Hong Kong dollars ("HKD"). Most of the companies comprising the group are operating in the PRC and their functional currency is RMB, hence, RMB is used as the presentation currency of the group.

The measurement basis used in the preparation of the financial statements is the historical cost basis except that the following assets and liabilities are stated at their fair value as explained in the accounting policies set out below:

— financial assets classified as available-for-sale (see note 2(f))

— derivative financial instruments (see note 2(g))

The preparation of financial statements in conformity with IFRSs requires management to make judgements, estimates and assumptions that affect the application of policies and reported amounts of assets, liabilities, income and expenses. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgements about carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates.

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

(b) Basis of preparation of the financial statements (continued)

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

Judgements made by management in the application of IFRSs that have significant effect on the financial statements and major sources of estimation uncertainty are discussed in note 3.

(c) 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 period.

- 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 in note 31 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.

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

(d) Subsidiaries and non-controlling interests

Subsidiaries are entities controlled by the group. Control exists when the group has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. In assessing control, potential voting rights that presently are exercisable are taken into account.

An investment in a subsidiary is consolidated into the consolidated financial statements from the date that control commences until the date that control ceases. Intra-group balances and transactions and any unrealised profits arising from intra-group transactions are eliminated in full in preparing the consolidated financial statements. Unrealised losses resulting from intra-group transactions are eliminated in the same way as unrealized gains but only to the extent that there is no evidence of impairment.

Non-controlling interests represent the equity in a subsidiary not attributable directly or indirectly to the company, and in respect of which the group has not agreed any additional terms with the holders of those interests which would result in the group as a whole having a contractual obligation in respect of those interests that meets the definition of a financial liability. For each business combination, the group can elect to measure any non-controlling interests either at fair value or at their proportionate share of the subsidiary's net identifiable assets.

Non-controlling interests are presented in the consolidated balance sheet within equity, separately from equity attributable to the equity shareholders of the company. Non-controlling interests in the results of the group are presented on the face of the consolidated income statement and the consolidated statement of comprehensive income as an allocation of the total profit or loss and total comprehensive income for the year between non-controlling interests and the equity shareholders of the company.

Changes in the group's interests in a subsidiary that do not result in a loss of control are accounted for as equity transactions, whereby adjustments are made to the amounts of controlling and non-controlling interests within consolidated equity to reflect the change in relative interests, but no adjustments are made to goodwill and no gain or loss is recognised.

When the group loses control of a subsidiary, it is accounted for as a disposal of the entire interest in that subsidiary, with a resulting gain or loss being recognised in profit or loss. Any interest retained in that former subsidiary at the date when control is lost is recognised at fair value and this amount is regarded as the fair value on initial recognition of a financial asset (see note 2(f)) or, when appropriate, the cost on initial recognition of an investment in an associate or jointly controlled entity (see note 2(e)).

In the company's balance sheet, an investment in a subsidiary is stated at cost less impairment losses (see note 2(l)).

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

(e) Associates and jointly controlled entities

An associate is an entity in which the group or company has significant influence, but not control or joint control, over its management, including participation in the financial and operating policy decisions.

A jointly controlled entity is an entity which operates under a contractual arrangement between the group and other parties, where the contractual arrangement establishes that the group and one or more of the other parties share joint control over the economic activity of the entity.

An investment in an associate or a jointly controlled entity is accounted for in the consolidated financial statements under the equity method and is initially recorded at cost, adjusted for any excess of the group's share of the acquisition-date fair values of the investee's identifiable net assets over the cost of the investment (if any). Thereafter, the investment is adjusted for the post acquisition change in the group's share of the investee's net assets and any impairment loss relating to the investment (see note 2(l)). Any acquisition-date excess over cost, the group's share of the post-acquisition, post-tax results of the investees and any impairment losses for the year are recognised in the consolidated income statement, whereas the group's share of the post-acquisition post-tax items of the investees' other comprehensive income is recognised in the consolidated statement of comprehensive income.

When the group's share of losses exceeds its interest in the associate or jointly controlled entity, the group's interest is reduced to nil and recognition of further losses is discontinued except to the extent that the group has incurred legal or constructive obligations or made payments on behalf of the associate or jointly controlled entity. For this purpose, the group's interest is the carrying amount of the investment under the equity method together with the group's long-term interests that in substance form part of the group's net investment in the associate or jointly controlled entity.

Unrealised profits and losses resulting from transactions between the group and its associates and jointly controlled entities are eliminated to the extent of the group's interest in the associate or jointly controlled entity, except where unrealised losses provide evidence of an impairment of the asset transferred, in which case they are recognised immediately in profit or loss.

When the group ceases to have significant influence over an associate or joint control over a jointly controlled entity, it is accounted for as a disposal of the entire interest in that associate or jointly controlled entity, with a resulting gain or loss being recognised in profit or loss. Any interest retained in that former associate or jointly controlled entity at the date when joint control is lost is recognised at fair value and this amount is regarded as the fair value on initial recognition of a financial asset or, when appropriate, the cost on initial recognition of an investment in an associate.

In the company's balance sheet, investments in associates and jointly controlled entities are stated at cost less impairment losses (see note 2(l)).

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

(f) Non-derivative financial assets

The group initially recognises loans and receivables and deposits on the date that they are originated. All other financial assets (including assets designated at fair value through profit or loss) are recognised initially on the trade date, which is the date that the group becomes a party to the contractual provisions of the instrument.

The group derecognises a financial asset when the contractual rights to the cash flows from the asset expire, or it transfers the rights to receive the contractual cash flows on the financial asset in a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred. Any interest in transferred financial assets that is created or retained by the group is recognised as a separate asset or liability.

Financial assets and liabilities mainly are offset and the net amount presented in the balance sheet when, and only when, the group has a legal right to offset the amounts and intends either to settle on a net basis or to realise the asset and settle the liability simultaneously.

The group classifies non-derivative financial assets into the following categories: financial assets at fair value through profit or loss, held-to-maturity financial assets, loans and receivables and available-for-sale financial assets.

Financial assets at fair value through profit or loss

A financial asset is classified at fair value through profit or loss if it is classified as held for trading or is designated as such upon initial recognition. Financial assets are designated at fair value through profit or loss if the group manages such investments and makes purchase and sale decisions based on their fair value in accordance with the group's documented risk management or investment strategy. Attributable transaction costs are recognised in profit or loss as incurred. Financial assets at fair value through profit or loss are measured at fair value, and changes therein are recognised in profit or loss.

Financial assets designated at fair value through profit or loss comprise equity securities that otherwise would have been classified as available for sale.

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

(f) Non-derivative financial assets (continued)

Held-to-maturity financial assets

If the group has the positive intent and ability to hold debt securities to maturity, then such financial assets are classified as held to maturity. Held-to-maturity financial assets are recognised initially at fair value plus any directly attributable transaction costs. Subsequent to initial recognition held-to-maturity financial assets are measured at amortised cost using the effective interest method, less any impairment losses. Any sale or reclassification of a more than insignificant amount of held-to-maturity investments not close to their maturity would result in the reclassification of all held-to-maturity investments as available for sale, and prevent the group from classifying investment securities as held to maturity for the current and the following two financial years.

Loans and receivables

Loans and receivables are financial assets with fixed or determinable payments that are not quoted in an active market. Such assets are recognised initially at fair value plus any directly attributable transaction costs. Subsequent to initial recognition, loans and receivables are measured at amortised cost using the effective interest method, less any impairment losses.

Loans and receivables comprise cash and cash equivalents (see note 2(q)), and trade and other receivables (see note 2(n)).

Available-for-sale financial assets

Available-for-sale financial assets are non-derivative financial assets that are designated as available for sale or are not classified in any of the above categories of financial assets.

Subsequent to initial recognition, they are measured at fair value and changes therein, other than impairment losses (see note 2(l)(i)) and foreign currency differences on available-for-sale debt instruments, are recognised in other comprehensive income and presented in the fair value reserve in equity. When an investment is derecognised, the gain or loss accumulated in equity is reclassified to profit or loss.

(g) Derivative financial instruments

Derivative financial instruments are recognised initially at fair value. At the end of each reporting period the fair value is remeasured. The gain or loss on remeasurement to fair value is recognised immediately in profit or loss.

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

(h) Fixed assets and depreciation

Items of fixed assets are stated in the balance sheet at cost less accumulated depreciation and impairment losses (see note 2(l)).

The cost of self-constructed items of fixed assets includes the cost of materials, direct labour, the initial estimate, where relevant, of the costs of dismantling and removing the items and restoring the site on which they are located, and an appropriate proportion of production overheads and borrowing costs (see note 2(w)).

Gains or losses arising from the retirement or disposal of a fixed asset are determined as the difference between the net disposal proceeds and the carrying amount of the asset and are recognised in profit or loss on the date of retirement or disposal.

Depreciation is calculated to write off the cost of items of fixed assets, less their estimated residual values, if any, using the straight-line method over their estimated useful lives as follows:

— Freehold land . . . . Not depreciated
— Leasehold land. . . . . Over the respective periods of the rights
— Buildings held for own use . . . . 20–35 years
— Plant and machinery. . . . . 5–10 years
— Fixtures, fittings and equipment . . . . 5–10 years
— Motor vehicles . . . . 5–6 years

Both the useful life of an asset and its residual value, if any, are reviewed annually.

(i) Construction in progress

Construction in progress represents fixed assets under construction and equipment pending installation, and is stated at cost less impairment losses (see note 2(l)). Cost comprises direct costs of construction. Capitalisation of these costs ceases and the construction in progress is transferred to fixed assets when substantially all of the activities necessary to prepare the assets for their intended use are complete.

No depreciation is provided in respect of construction in progress until it is substantially completed and ready for its intended use.

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

(j) Intangible assets

Expenditure on research activities is recognised as an expense in the period in which it is incurred. Expenditure on development activities is capitalised if the product or process is technically and commercially feasible and the group has sufficient resources and the intention to complete development. The expenditure capitalised includes the costs of materials, direct labour, and an appropriate proportion of overheads and borrowing costs, where applicable (see note 2(w)). Capitalised development costs are stated at cost less accumulated amortisation and impairment losses (see note 2(l)). Other development expenditure is recognised as an expense in the period in which it is incurred.

Other intangible assets represent the technology licences granted by the holding company and are stated in the balance sheet at cost less accumulated amortisation and impairment losses (see note 2(l)).

Amortisation of intangible assets with finite useful lives is charged to profit or loss on a straight-line basis over the assets' estimated useful lives. The following intangible assets with finite useful lives are amortised from the date they are available for use and their estimated useful lives are as follows:

— Capitalised development costs . . . . 10 years
— Technology licences . . . . 10 years

Both the period and method of amortisation are reviewed annually.

(k) Operating lease charges

Where the group has the use of assets held under operating leases, payments made under the leases are charged to profit or loss in equal instalments over the accounting periods covered by the lease terms, except where an alternative basis is more representative of the pattern of benefits to be derived from the leased asset. Lease incentives received are recognised in profit or loss as an integral part of the aggregate net lease payments made.

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

(l) Impairment of assets

(i) Impairment of investments in debt and equity securities and other receivables

Investments in debt and equity securities and other current and non-current receivables that are stated at cost or amortised cost or are classified as available-for-sale securities are reviewed at each balance sheet date to determine whether there is objective evidence of impairment. Objective evidence of impairment includes observable data that comes to the attention of the group about one or more of the following loss events:

— significant financial difficulty of the debtor;

— a breach of contract, such as default or delinquency in interest or principal payments;

— it becoming probable that the debtor will enter bankruptcy or other financial reorganisation;

— significant changes in the technological, market, economic or legal environment that have an adverse effect on the debtor; and

— a significant or prolonged decline in the fair value of an investment in an equity instrument below its cost.

If any such evidence exists, any impairment loss is determined and recognised as follows:

— For investments in subsidiaries, associates and jointly controlled entities (including those recognised using the equity method (see note 2(e)), the impairment loss is measured by comparing the recoverable amount of the investment with its carrying amount in accordance with note 2(l)(ii). The impairment loss is reversed if there has been a favourable change in the estimates used to determine the recoverable amount in accordance with note 2(l)(ii).

— For trade and other current receivables and other financial assets carried at amortised cost, the impairment loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the financial asset's original effective interest rate (i.e. the effective interest rate computed at initial recognition of these assets), where the effect of discounting is material. This assessment is made collectively where these financial assets share similar risk characteristics, such as similar past due status, and have not been individually assessed as impaired. Future cash flows for financial assets which are assessed for impairment collectively are based on historical loss experience for assets with credit risk characteristics similar to the collective group.

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

(l) Impairment of assets (continued)

(i) Impairment of investments in debt and equity securities and other receivables (continued)

If in a subsequent period the amount of an impairment loss decreases and the decrease can be linked objectively to an event occurring after the impairment loss was recognised, the impairment loss is reversed through profit or loss. A reversal of an impairment loss shall not result in the asset's carrying amount exceeding that which would have been determined had no impairment loss been recognised in prior years.

— For available-for-sale securities, the cumulative loss that has been recognised in the fair value reserve is reclassified to profit or loss. The amount of the cumulative loss that is recognised in profit or loss is the difference between the acquisition cost (net of any principal repayment and amortisation) and current fair value, less any impairment loss on that asset previously recognised in profit or loss.

Impairment losses recognised in profit or loss in respect of available-for-sale equity securities are not reversed through profit or loss. Any subsequent increase in the fair value of such assets is recognised in other comprehensive income.

Impairment losses in respect of available-for-sale debt securities are reversed if the subsequent increase in fair value can be objectively related to an event occurring after the impairment loss was recognised. Reversals of impairment losses in such circumstances are recognised in profit or loss.

Impairment losses are written off against the corresponding assets directly, except for impairment losses recognised in respect of trade debtors included within trade and other receivables, whose recovery is considered doubtful but not remote. In this case, the impairment losses for doubtful debts are recorded using an allowance account. When the group is satisfied that recovery is remote, the amount considered irrecoverable is written off against trade debtors directly and any amounts held in the allowance account relating to that debt are reversed. Subsequent recoveries of amounts previously charged to the allowance account are reversed against the allowance account. Other charges in the allowance account and subsequent recoveries of amounts previously written off directly are recognised in profit or loss.

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

(l) Impairment of assets (continued)

(ii) Impairment of other assets

Internal and external sources of information are reviewed at each balance sheet date to identify indications that the following assets may be impaired or an impairment loss previously recognised no longer exists or may have decreased:

— fixed assets;

— construction in progress;

— intangible assets; and

— deposits paid for acquisition of leasehold land.

If any such indication exists, the asset's recoverable amount is estimated.

— Calculation of recoverable amount

The recoverable amount of an asset is the greater of its fair value less costs to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. Where an asset does not generate cash inflows largely independent of those from other assets, the recoverable amount is determined for the smallest group of assets that generates cash inflows independently (i.e. a cash-generating unit).

— Recognition of impairment losses

An impairment loss is recognised in profit or loss if the carrying amount of an asset, or the cash-generating unit to which it belongs, exceeds its recoverable amount. Impairment losses recognised in respect of cash-generating units are allocated to reduce the carrying amount of the assets in the unit (or group of units) on a pro rata basis, except that the carrying value of an asset will not be reduced below its individual fair value less costs to sell, or value in use, if determinable.

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

(l) Impairment of assets (continued)

(ii) Impairment of other assets (continued)

— Reversals of impairment losses

An impairment loss is reversed if there has been a favourable change in the estimates used to determine the recoverable amount.

A reversal of an impairment loss is limited to the asset's carrying amount that would have been determined had no impairment loss been recognised in prior years. Reversals of impairment losses are credited to profit or loss in the year in which the reversals are recognised.

(m) Inventories

Inventories are carried at the lower of cost and net realisable value.

Cost is calculated using the weighted average cost formula and comprises all costs of purchase, costs of conversion and other costs incurred in bringing the inventories to their present location and condition.

Net realisable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale.

When inventories are sold, the carrying amount of those inventories is recognised as an expense in the period in which the related revenue is recognised. The amount of any write-down of inventories to net realisable value and all losses of inventories are recognised as an expense in the period the write-down or loss occurs. The amount of any reversal of any write-down of inventories is recognised as a reduction in the amount of inventories recognised as an expense in the period in which the reversal occurs.

(n) Trade and other receivables

Trade and other receivables are initially recognised at fair value and thereafter stated at amortised cost using the effective interest method, less allowance for impairment of doubtful debts (see note 2(l)), except where the receivables are interest-free loans made to related parties without any fixed repayment terms or the effect of discounting would be immaterial. In such cases, the receivables are stated at cost less allowance for impairment of doubtful debts.

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

(o) Interest-bearing borrowings

Interest-bearing borrowings are recognised initially at fair value less attributable transaction costs. Subsequent to initial recognition, interest-bearing borrowings are stated at amortised cost with any difference between the amount initially recognised and redemption value being recognised in profit or loss over the period of the borrowings, together with any interest and fees payable, using the effective interest method.

(p) Trade and other payables

Trade and other payables are initially recognised at fair value and are subsequently stated at amortised cost unless the effect of discounting would be immaterial, in which case they are stated at cost.

(q) Cash and cash equivalents

Cash and cash equivalents comprise cash at bank and on hand, demand deposits with banks and other financial institutions, and short-term, highly liquid investments that are readily convertible into known amounts of cash and which are subject to an insignificant risk of changes in value, having been within three months of maturity at acquisition.

(r) Employee benefits

(i) Short term employee benefits and contributions to defined contribution retirement plans

Salaries, annual bonuses, paid annual leave, contributions to defined contribution retirement plans and the cost of non-monetary benefits are accrued in the year in which the associated services are rendered by employees. Where payment or settlement is deferred and the effect would be material, these amounts are stated at their present values.

(ii) Share-based payments

The fair value of share options granted to employees is recognised as an employee cost with a corresponding increase in a capital reserve within equity. The fair value is measured at grant date using the binomial option price model, taking into account the terms and conditions under which the options were granted. Where the employees have to meet vesting conditions before becoming unconditionally entitled to the options, the total estimated fair value of the options is spread over the vesting period, taking into account the probability that the options will vest.

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

(r) Employee benefits (continued)

(ii) Share-based payments (continued)

During the vesting period, the number of share options that is expected to vest is reviewed. Any resulting adjustment to the cumulative fair value recognised in prior years is charged/credited to the profit or loss for the year of the review, unless the original employee expenses qualify for recognition as an asset, with a corresponding adjustment to the capital reserve. On the vesting date, the amount recognised as an expense is adjusted to reflect the actual number of options that vest (with a corresponding adjustment to the capital reserve) except where forfeiture is only due to not achieving vesting conditions that relate to the market price of the company's shares. The equity amount is recognised in the capital reserve until either the option is exercised (when it is transferred to the share premium account) or the option expires (when it is released directly to retained profits).

Share-based payment transactions in which the company grants share options to subsidiaries' employees are accounted for as an increase in value of investment in subsidiary in the company's balance sheet which is eliminated on consolidation.

(s) Income tax

Income tax for the year comprises current tax and movements in deferred tax assets and liabilities. Current tax and movements in deferred tax assets and liabilities are recognised in profit or loss except to the extent that they relate to items recognised in other comprehensive income or directly in equity, in which case the relevant amounts of tax are recognised in other comprehensive income or directly in equity, respectively.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the balance sheet date, and any adjustment to tax payable in respect of previous years.

Deferred tax assets and liabilities arise from deductible and taxable temporary differences respectively, being the differences between the carrying amounts of assets and liabilities for financial reporting purposes and their tax bases. Deferred tax assets also arise from unused tax losses and unused tax credits.

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

(s) Income tax (continued)

Apart from certain limited exceptions, all deferred tax liabilities, and all deferred tax assets to the extent that it is probable that future taxable profits will be available against which the asset can be utilised, are recognised. Future taxable profits that may support the recognition of deferred tax assets arising from deductible temporary differences include those that will arise from the reversal of existing taxable temporary differences, provided those differences relate to the same taxation authority and the same taxable entity, and are expected to reverse either in the same period as the expected reversal of the deductible temporary difference or in periods into which a tax loss arising from the deferred tax asset can be carried back or forward. The same criteria are adopted when determining whether existing taxable temporary differences support the recognition of deferred tax assets arising from unused tax losses and credits, that is, those differences are taken into account if they relate to the same taxation authority and the same taxable entity, and are expected to reverse in a period, or periods, in which the tax loss or credit can be utilised.

The amount of deferred tax recognised is measured based on the expected manner of realisation or settlement of the carrying amount of the assets and liabilities, using tax rates enacted or substantively enacted at the balance sheet date. Deferred tax assets and liabilities are not discounted.

The carrying amount of a deferred tax asset is reviewed at each balance sheet date and is reduced to the extent that it is no longer probable that sufficient taxable profits will be available to allow the related tax benefit to be utilised. Any such reduction is reversed to the extent that it becomes probable that sufficient taxable profits will be available.

Current tax balances and deferred tax balances, and movements therein, are presented separately from each other and are not offset. Current tax assets are offset against current tax liabilities, and deferred tax assets against deferred tax liabilities, if the group has the legally enforceable right to set off current tax assets against current tax liabilities and the following additional conditions are met:

— in the case of current tax assets and liabilities, the group intends either to settle on a net basis, or to realise the asset and settle the liability simultaneously; or

— in the case of deferred tax assets and liabilities, if they relate to income taxes levied by the same taxation authority on either:

  — the same taxable entity; or

  — different taxable entities, which, in each future period in which significant amounts of deferred tax liabilities or assets are expected to be settled or recovered, intend to realise the current tax assets and settle the current tax liabilities on a net basis or realise and settle simultaneously.

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

(t) Financial guarantees issued, provisions and contingent liabilities

(i) Financial guarantees issued

Financial guarantees are contracts that require the issuer (i.e. the guarantor) to make specified payments to reimburse the beneficiary of the guarantee (the "holder") for a loss the holder incurs because a specified debtor fails to make payment when due in accordance with the terms of a debt instrument.

Where the group issues a financial guarantee, the fair value of the guarantee (being the transaction price, unless the fair value can otherwise be reliably estimated) is initially recognised as deferred income within trade and other payables. Where consideration is received or receivable for the issuance of the guarantee, the consideration is recognized in accordance with the group's policies applicable to that category of asset. Where no such consideration is received or receivable, an immediate expense is recognised in profit or loss on initial recognition of any deferred income.

The amount of the guarantee initially recognised as deferred income is amortised in profit or loss over the term of the guarantee as income from financial guarantees issued. In addition, provisions are recognised in accordance with note 2(t) (ii) if and when (i) it becomes probable that the holder of the guarantee will call upon the group under the guarantee, and (ii) the amount of that claim on the group is expected to exceed the amount currently carried in trade and other payables in respect of that guarantee i.e. the amount initially recognised, less accumulated amortisation.

(ii) Other provisions and contingent liabilities

Provisions are recognised for liabilities of uncertain timing or amount when the group or the company has a legal or constructive obligation arising as a result of a past event, it is probable that an outflow of economic benefits will be required to settle the obligation and a reliable estimate can be made. Where the time value of money is material, provisions are stated at the present value of the expenditure expected to settle the obligation.

Where it is not probable that an outflow of economic benefits will be required, or the amount cannot be estimated reliably, the obligation is disclosed as a contingent liability, unless the probability of outflow of economic benefits is remote. Possible obligations, whose existence will only be confirmed by the occurrence or non-occurrence of one or more future events are also disclosed as contingent liabilities unless the probability of outflow of economic benefits is remote.

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

(u) Revenue recognition

Revenue is measured at the fair value of the consideration received or receivable. Provided it is probable that the economic benefits will flow to the group and the revenue and costs, if applicable, can be measured reliably, revenue is recognised in profit or loss as follows:

(i) Sale of goods

Revenue from the sale of goods is recognised when the customer has accepted the related risks and rewards of ownership. Revenue excludes value-added tax or other sales taxes and is after deduction of any trade discounts.

(ii) Interest income

Interest income is recognised as it accrues using the effective interest method.

(iii) Government grants

Government grants are recognised in the balance sheet initially when there is reasonable assurance that they will be received and that the group will comply with the conditions attaching to them. Grants that compensate the group for expenses incurred are recognised as revenue in profit or loss on a systematic basis in the same periods in which the expenses are incurred. Grants that compensate the group for the cost of an asset are deducted from the carrying amount of the asset and consequently are effectively recognised in profit or loss over the useful life of the asset by way of reduced depreciation expense.

(iv) Rendering of drilling services

Revenue from services rendered is recognised in profit or loss in proportion to the stage of completion of the transaction at the reporting date. The stage of completion is assessed by reference to surveys of work performed.

(v) Rendering of repairing services

Revenue is recognised when the service has been rendered.

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

(v) Translation of foreign currencies

Foreign currency transactions during the year are translated at the foreign exchange rates ruling at the transaction dates. Monetary assets and liabilities denominated in foreign currencies are translated at the foreign exchange rates ruling at the balance sheet date. Exchange gains and losses are recognised in profit or loss.

Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated using the foreign exchange rates ruling at the transaction dates.

The results of operations outside the PRC are translated into the presentation currency at the exchange rates approximating the foreign exchange rates ruling at the transaction dates. Balance sheet items are translated into the presentation currency at the closing foreign exchange rates ruling at the balance sheet date. The resulting exchange differences are recognized in other comprehensive income and accumulated separately in equity in the exchange reserve.

On disposal of an operation outside the PRC, the cumulative amount of the exchange differences relating to that operation is reclassified from equity to profit or loss when the profit or loss on disposal is recognised.

(w) Borrowing costs

Borrowing costs that are directly attributable to the acquisition, construction or production of an asset which necessarily takes a substantial period of time to get ready for its intended use or sale are capitalised as part of the cost of that asset. Other borrowing costs are expensed in the period in which they are incurred.

The capitalisation of borrowing costs as part of the cost of a qualifying asset commences when expenditure for the asset is being incurred, borrowing costs are being incurred and activities that are necessary to prepare the asset for its intended use or sale are in progress. Capitalisation of borrowing costs is suspended or ceases when substantially all the activities necessary to prepare the qualifying asset for its intended use or sale are interrupted or complete.

(x) Warranty costs

A provision for warranties is recognised when the underlying products are sold. The provision is based on historical warranty data and a weighting of all possible outcomes against their associated probabilities.

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

(y) Related parties

(a) A person, or a close member of that person's family, is related to the group if that person:

(i) has control or joint control over the group;

(ii) has significant influence over the group; or

(iii) is a member of the key management personnel of the group or the group's parent.

(b) An entity is related to the group if any of the following conditions applies:

(i) The entity and the group are members of the same group (which means that each parent, subsidiary and fellow subsidiary is related to the others).

(ii) One entity is an associate or joint venture of the other entity (or an associate or joint venture of a member of a group of which the other entity is a member).

(iii) Both entities are joint ventures of the same third party.

(iv) One entity is a joint venture of a third entity and the other entity is an associate of the third entity.

(v) The entity is a post-employment benefit plan for the benefit of employees of either the group or an entity related to the group.

(vi) The entity is controlled or jointly controlled by a person identified in (a).

(vii) A person identified in (a)(i) has significant influence over the entity or is a member of the key management personnel of the entity (or of a parent of the entity).

Close members of the family of a person are those family members who may be expected to influence, or be influenced by, that person in their dealings with the entity.

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

(z) Segment reporting

Operating segments, and the amounts of each segment item reported in the financial statements, are identified from the financial information provided regularly to the group's most senior executive management for the purposes of allocating resources to, and assessing the performance of, the group's various lines of business and geographical locations.

Individually material operating segments are not aggregated for financial reporting purposes unless the segments have similar economic characteristics and are similar in respect of the nature of products and services, the nature of production processes, the type or class of customers, the methods used to distribute the products or provide the services, and the nature of the regularly environment. Operating segments which are not individually material may be aggregated if they share a majority of these criteria.

3 SIGNIFICANT ACCOUNTING ESTIMATES AND JUDGEMENTS

Key sources of estimation uncertainty

Note 26 contains information about the assumptions relating to the determination of fair value of share options granted. Other sources of estimation uncertainties are as follows:

(a) Impairments

(i) Impairment of trade and other receivables

Trade and other receivables are reviewed periodically to assess whether impairment losses exist and if they exist, the amounts of the impairment losses are estimated based on historical loss experience for trade and other receivables with similar credit risk. The methodology and assumptions used in estimating future cash flows are reviewed regularly to reduce any difference between the loss estimates and actual amounts.

3 SIGNIFICANT ACCOUNTING ESTIMATES AND JUDGEMENTS (continued)

(a) Impairments (continued)

(ii) Impairment of intangible assets, fixed assets and construction in progress

If circumstances indicate that the carrying value of intangible assets, fixed assets and construction in progress may not be recoverable, these assets may be considered impaired, and an impairment loss may be recognised in accordance with IAS 36 "Impairment of Assets". The carrying amounts of these assets are reviewed periodically in order to assess whether the recoverable amounts have declined below the carrying amounts. These assets are tested for impairment whenever events or changes in circumstances indicate that their recorded carrying amounts may not be recoverable. When such a decline has occurred, the carrying amount is reduced to recoverable amount. The recoverable amount is the greater of the net selling prices and the value in use. It is difficult to estimate precisely selling prices because quoted market prices for the group's assets are not readily available. In determining that value in use, expected cash flows generated by the assets are discounted to their present value, which requires significant judgement relating to revenue and amount of operating costs. The group uses all readily available information in determining an amount that is a reasonable approximation of recoverable amount, including estimates based on reasonable and supportable assumptions and projections of revenue and amount of operating costs.

(b) Write down of inventories

The group determines the write down for obsolescence of inventories. These estimates are made with reference to aged inventories analyses, projections of expected future saleability of goods and management experience and judgement. Based on this review, write down of inventories will be made when the carrying amounts of inventories decline below their estimated net realisable value. Due to changes in market conditions, actual saleability of goods may be different from estimation and profit or loss could be affected by differences in this estimation.

(c) Inventory provision due to cancellation of order

Generally, the group produces drilling rigs based on the signed contracts with customers. As a result of the recent economic turmoil, customers may cancel the contracts and any cancellation of order might lead to obsolescence of inventories. In preparing the financial statements for the year ended 31 December 2011, the directors of the company have reviewed the status of all contracts on hand and considered that a provision for inventory provision in this regard is not necessary.

(d) Warranty provision

The group makes provisions under the warranties it gives on sale of its drilling rigs taking into account the group's recent claim experience. Any increase or decrease in the provision would affect profit or loss in future years.

3 SIGNIFICANT ACCOUNTING ESTIMATES AND JUDGEMENTS (continued)

(e) Depreciation and amortisation

Property, plant and equipment are depreciated on a straight-line basis over the estimated useful lives, after taking into account the estimated residual value. Intangible assets are amortised on a straight-line basis over the estimated useful lives. The group reviews the estimated useful lives of the assets regularly in order to determine the amount of depreciation and amortisation expenses to be recorded during any reporting period. The useful lives are based on the group's historical experience with similar assets and taking into account anticipated technological changes. The depreciation and amortisation expenses for future periods are adjusted if there are significant changes from previous estimates.

(f) Provision for deferred tax

Determining income tax provisions involves judgement on the future tax treatment of certain transactions. The management evaluates tax implications of transactions and tax provisions are set up accordingly. The tax treatment of such transactions is reconsidered periodically to take into account all changes in tax legislation. Deferred tax assets are recognised for tax losses not yet used and temporary deductible differences. As those deferred tax assets can only be recognised to the extent that it is probable that future taxable profit will be available against which the unused tax credits can be utilised, management's judgement is required to assess the probability of future taxable profits. Management's assessment is constantly reviewed and additional deferred tax assets are recognised if it becomes probable that future taxable profits will allow the deferred tax asset to be recovered.

4 TURNOVER AND SEGMENT REPORTING

(a) 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.

For the year ended 31 December 2011, the group's customer base includes three customers (2010: three customers) with whom transactions representing 19%, 13% and 10% (2010: 16%, 15% and 10%) of the group's revenue respectively. In 2011, turnover from sales of drilling rigs and related parts and components to these customers, amounted to approximately RMB645 million, RMB455 million and RMB346 million (2010: RMB299 million, RMB285 million and RMB195 million) respectively which arose in Americas, Europe and Central Asia.

4 TURNOVER AND SEGMENT REPORTING (continued)

(b) 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.

(i) 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.

4 TURNOVER AND SEGMENT REPORTING (continued)

(b) Segment reporting (continued)

(i) *Segment results, assets and liabilities* (continued)

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

4 TURNOVER AND SEGMENT REPORTING (continued)

(b) Segment reporting (continued)

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

	2011 RMB'000	2010 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

4 TURNOVER AND SEGMENT REPORTING (continued)

(b) Segment reporting (continued)

(iii) 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 OTHER REVENUE AND OTHER NET INCOME/(LOSS)

	2011 RMB'000	2010 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)

On 8 August 2011, the group de-registered a wholly-owned subsidiary, Sichuan Hongcheng Business Trading Co., Ltd. The subsidiary had remained dormant and derived no revenue since its establishment through its de-registration. The cumulative exchange differences were reclassified from equity to profit and loss upon the liquidation of that subsidiary.

6 PROFIT/(LOSS) BEFORE TAXATION

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

	2011 RMB'000	2010 RMB'000
(a) Net finance expenses		
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%).

	2011 RMB'000	2010 RMB'000
(b) Staff costs		
Contributions to defined contribution retirement schemes	**44,079**	35,997
Equity-settled share based payment expenses (note 26)	**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 6(b).

7 INCOME TAX EXPENSES/(CREDIT)

(a) Taxation in the consolidated income statement represents:

	2011 **RMB'000**	2010 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 (note 27(b))	**(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) 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.

7 INCOME TAX EXPENSES/(CREDIT) (continued)

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

(ii) PRC (continued)

(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.

7 INCOME TAX EXPENSES/(CREDIT) (continued)

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

(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 recognised 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.

(c) Reconciliation between tax expenses/(credit) and accounting profit/(loss) at applicable tax rates:

	2011 **RMB'000**	2010 RMB'000
Profit/(loss) before taxation	**199,212**	(176,443)
Notional tax on profit/(loss) before taxation, calculated at the rates applicable to profits/(losses) in the countries concerned	**33,140**	(39,004)
Tax effect of non-deductible expenses	**2,544**	19,282
Tax effect of non-taxable income	**(7,966)**	(703)
Withholding tax on expected profits distribution from PRC subsidiaries	**6,409**	1,947
(Over)/under-provision in respect of prior years	**(6,358)**	596
Under-provision of deferred tax assets in respect of prior years	**–**	(5,797)
Effect of preferential tax rate on loss	**–**	19,307
Actual tax expenses/(credit)	**27,769**	(4,372)

8 DIRECTORS' REMUNERATION

Details of directors' remuneration are set out below:

	2011					
	Fees RMB'000	Basic salaries, allowances and other benefits in kind RMB'000	Contributions to defined contribution retirement scheme RMB'000	Discretionary bonuses RMB'000	Equity-settled share based payment expenses RMB'000	Total RMB'000
Chairman and Executive Director						
Zhang Mi	–	950	27	1,756	807	3,540
Executive Directors						
Ren Jie	–	486	26	1,074	291	1,877
Liu Zhi	–	469	28	694	264	1,455
Non-executive Directors						
Siegfried Meissner	–	–	–	–	–	–
Huang Dongyang	–	–	–	–	–	–
Independent Non-executive Directors						
Qi Daqing	166	–	–	–	142	308
Liu Xiaofeng	166	–	–	–	142	308
Chen Guoming	83	–	–	–	118	201
Wang Li (resigned on 20 June 2011)	39	–	–	–	9	48
Tai Kwok Leung, Alexander	124	–	–	–	121	245
Shi Xingquan	83	–	–	–	106	189
Guo Yanjun (appointed on 20 June 2011)	66	–	–	–	50	116
Total	727	1,905	81	3,524	2,050	8,287

8 DIRECTORS' REMUNERATION (continued)

	2010					
	Fees RMB'000	Basic salaries, allowances and other benefits in kind RMB'000	Contributions to defined contribution retirement scheme RMB'000	Discretionary bonuses RMB'000	Equity-settled share based payment expenses RMB'000	Total RMB'000
Chairman and Executive Director						
Zhang Mi	–	765	23	–	2,196	2,984
Executive Directors						
Ren Jie	–	477	23	196	851	1,547
Liu Zhi	–	436	23	159	773	1,391
Non-executive Directors						
Siegfried Meissner	–	–	–	–	–	–
Xiang Qingsheng (resigned on 14 April 2010)	–	–	–	–	–	–
He Sean Xing (resigned on 14 April 2010)	–	–	–	–	–	–
Huang Dongyang	–	–	–	–	–	–
Independent Non-executive Directors						
Qi Daqing	174	–	–	–	120	294
Liu Xiaofeng	174	–	–	–	120	294
Chen Guoming	87	–	–	–	90	177
Wang Li	87	–	–	–	90	177
Tai Kwok Leung, Alexander	131	–	–	–	102	233
Liu Yinchun (resigned on 14 April 2010)	25	–	–	–	26	51
Shi Xingquan	87	–	–	–	90	177
Total	765	1,678	69	355	4,458	7,325

During the year, no amount was paid or payable by the group to the directors or any of the five highest paid individuals set out in note 9 below as an inducement to join or upon joining the group or as compensation for loss of office. Except for Siegfried Meissner who has waived to receive his remuneration amounting to RMB124,455 (2010: Nil), there was no arrangement under which a director waived or agreed to waive any remuneration during the year (2010: Nil).

9 INDIVIDUAL WITH HIGHEST EMOLUMENTS

The five highest paid individuals of the group include three directors during the year ended 31 December 2011 (2010: three) whose emoluments are disclosed in note 8. Details of remuneration paid to the remaining two (2010: two) highest individuals of the group are as follows:

	2011 **RMB'000**	2010 RMB'000
Basic salaries, allowances and other benefits in kind	**1,046**	2,480
Discretionary bonuses	**1,803**	705
Contributions to defined contribution retirement schemes	**38**	27
Share-based payments	**385**	184
	3,272	3,396

The emoluments of these two individuals with highest emoluments are within the following bands:

	2011	2010
HKD1,500,001 to HKD2,000,000	**1**	1
HKD2,000,001 to HKD2,500,000	**1**	1

10 PROFIT/(LOSS) ATTRIBUTABLE TO EQUITY SHAREHOLDERS OF THE COMPANY

The consolidated profit attributable to equity shareholders of the company includes a loss of RMB62,864,000 (2010: loss of RMB44,972,000) which has been dealt with in the financial statements of the company.

(Expressed in Renminbi unless otherwise indicated)

11 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.

12 FIXED ASSETS

(a) The group

	Freehold land RMB'000	Interests in leasehold land held for own use under operating leases RMB'000	Buildings held for own use RMB'000	Plant and machinery RMB'000	Fixtures, fittings and equipment RMB'000	Motor vehicles RMB'000	Total RMB'000
Cost:							
At 1 January 2010	5,504	147,605	252,804	131,680	116,836	39,249	693,678
Additions	–	–	11,112	23,027	31,536	4,422	70,097
Transfer from construction in progress (note 13)	–	–	94,219	1,509	2,356	–	98,084
Disposals	–	–	–	(80)	(1,580)	(70)	(1,730)
Exchange difference	(165)	–	(1,270)	(182)	(66)	(60)	(1,743)
At 31 December 2010	5,339	147,605	356,865	155,954	149,082	43,541	858,386
Accumulated amortisation and depreciation:							
At 1 January 2010	–	5,776	31,558	40,106	40,000	14,159	131,599
Charge for the year	–	1,771	14,538	13,579	17,472	5,909	53,269
Written back on disposals	–	–	–	(37)	(1,089)	(50)	(1,176)
Exchange difference	–	–	(130)	(96)	(33)	(18)	(277)
At 31 December 2010	–	7,547	45,966	53,552	56,350	20,000	183,415
Net book value:							
At 31 December 2010	5,339	140,058	310,899	102,402	92,732	23,541	674,971

12 FIXED ASSETS (continued)

(a) The group (continued)

	Freehold land RMB'000	Interests in leasehold land held for own use under operating leases RMB'000	Buildings held for own use RMB'000	Plant and machinery RMB'000	Fixtures, fittings and equipment RMB'000	Motor vehicles RMB'000	Total RMB'000
Cost:							
At 1 January 2011	5,339	147,605	356,865	155,954	149,082	43,541	858,386
Additions	–	43,149	3,489	143,242	27,175	6,680	223,735
Transfer from construction in progress (note 13)	–	–	40,309	2,911	3,103	–	46,323
Disposals	–	–	(348)	(324)	(4,868)	(573)	(6,113)
Exchange difference	(259)	–	(2,616)	(3,479)	(354)	(256)	(6,964)
At 31 December 2011	5,080	190,754	397,699	298,304	174,138	49,392	1,115,367
Accumulated amortisation and depreciation:							
At 1 January 2011	–	7,547	45,966	53,552	56,350	20,000	183,415
Charge for the year	–	2,018	18,108	23,114	21,455	6,628	71,323
Written back on disposals	–	–	(33)	(123)	(2,854)	(435)	(3,445)
Exchange difference	–	–	(286)	(382)	(84)	(40)	(792)
At 31 December 2011	–	9,565	63,755	76,161	74,867	26,153	250,501
Net book value:							
At 31 December 2011	5,080	181,189	333,944	222,143	99,271	23,239	864,866

12 FIXED ASSETS (continued)

(b) The analysis of net book value of properties is as follows:

	The group	
	2011	2010
	RMB'000	RMB'000
Outside Hong Kong		
— freehold	**5,080**	5,339
— medium-term leases	**515,133**	450,957
	520,213	456,296
Representing:		
Freehold land	**5,080**	5,339
Buildings held for own use	**333,944**	310,899
Interest in leasehold land held for own use under operating leases	**181,189**	140,058
	520,213	456,296

13 CONSTRUCTION IN PROGRESS

	The group	
	2011	2010
	RMB'000	RMB'000
At 1 January	**77,144**	59,144
Additions	**371,444**	116,199
Transfer to fixed assets (note 12)	**(46,323)**	(98,084)
Exchange difference	**(200)**	(115)
At 31 December	**402,065**	77,144

14 INTANGIBLE ASSETS

	The group			The company
	Technical know-how RMB'000	Development cost RMB'000	Total RMB'000	Technical know-how RMB'000
Cost:				
At 1 January 2010	367,914	—	367,914	367,914
Exchange difference	(12,368)	—	(12,368)	(12,368)
At 31 December 2010	355,546	—	355,546	355,546
At 1 January 2011	355,546	—	355,546	355,546
Addition through internal development	—	10,234	10,234	—
Exchange difference	(16,797)	—	(16,797)	(16,797)
At 31 December 2011	338,749	10,234	348,983	338,749
Accumulated amortisation:				
At 1 January 2010	49,055	—	49,055	49,055
Charge for the year	36,407	—	36,407	36,407
Exchange difference	(2,501)	—	(2,501)	(2,501)
At 31 December 2010	82,961	—	82,961	82,961
At 1 January 2011	82,961	—	82,961	82,961
Charge for the year	34,669	72	34,741	34,669
Exchange difference	(4,713)	—	(4,713)	(4,713)
At 31 December 2011	112,917	72	112,989	112,917
Net book value:				
At 31 December 2011	225,832	10,162	235,994	225,832
At 31 December 2010	272,585	—	272,585	272,585

The amortisation charge for the year is included in "general and administrative expenses" in the consolidated income statement.

15 INVESTMENTS IN SUBSIDIARIES

	The company 2011 RMB'000	2010 RMB'000
Unlisted equities, at cost	**202,675**	212,725
Cumulative fair value of share options granted to employees of subsidiaries	**84,907**	82,251
Long-term receivable from subsidiaries	**2,292,421**	2,406,091
	2,580,003	2,701,067

The long-term receivable from subsidiaries is unsecured, interest-free and has no fixed terms of repayment. The company has given undertaking not to demand for repayment within one year from the balance sheet date.

Details of the principal subsidiaries at 31 December 2011 are set out below:

Name of the company	Place of incorporation/ establishment and operation	Issued and paid-up capital	Attributable equity interest Direct	Attributable equity interest Indirect	Principal activities
Honghua Holdings (宏華控股有限公司)	Hong Kong	HKD1	100%	–	Investment holding
Honghua Company (四川宏華石油設備有限公司) (notes (ii), (iii))	The PRC	RMB750,000,000	–	100%	Manufacturing of petroleum equipment
Hongtian Company (成都宏天電傳工程 有限公司) (notes (i), (iii))	The PRC	RMB17,500,000	–	80%	Manufacturing of panel of drilling rigs
Youxin Company (四川宏華友信石油機械有限公司) (notes (i), (iii))	The PRC	RMB11,760,000	–	80%	Manufacturing of parts of drilling rigs
Honghua International Co., Ltd (四川宏華國際科貿有限公司) (notes (i), (iii))	The PRC	RMB51,200,000	–	85%	Trading of drilling rigs and related parts

(Expressed in Renminbi unless otherwise indicated)

15 INVESTMENTS IN SUBSIDIARIES (continued)

Name of the company	Place of incorporation/ establishment and operation	Issued and paid-up capital	Attributable equity interest		Principal activities
			Direct	Indirect	
Honghua America (宏華美國有限責任公司)	US	USD800,000	–	85%	Trading of drilling rigs and related parts
Golden Coast Company (宏華金海岸設備有限公司)	United Arab Emirates	AED1,000,000	–	100%	Trading of drilling rigs and related parts
Newco (H.K.) Limited (新順(香港)有限公司)	Hong Kong	HKD1,000	–	100%	Trading of drilling rigs and related parts
Honghua Offshore Oil and Gas Equipment (Jiangsu) Co., Ltd (宏華海洋油氣裝備(江蘇)有限公司) (notes (ii), (iii))	The PRC	USD29,980,000	–	100%	Manufacturing of offshore drilling platform and related products
Shanghai Honghua Offshore Oil and Gas Equipment Co., Ltd (上海宏華海洋油氣裝備有限公司) (notes (i), (iii))	The PRC	RMB10,000,000	–	100%	Research and development
Russia Honghua (俄羅斯宏華有限公司)	Russia Federation	RUB10,000	–	100%	Trading of drilling rigs and related parts

Notes:

(i) These entities are domestic limited liability companies established in the PRC.

(ii) These entities are wholly-owned foreign invested enterprises established in the PRC.

(iii) The official names of these companies are in Chinese. The English translation of the company name is for reference only.

16 INTERESTS IN JOINTLY CONTROLLED ENTITIES

	The group 2011 RMB'000	2010 RMB'000
Share of net assets	**38,919**	41,868

Details of the group's interests in jointly controlled entities are as follows:

Name of company	Place of establishment	Issued capital	Paid up capital	Group's effective interest held by a subsidiary	Principal activities
Egyptian Petroleum HH Rigs Manufacturing Co. S.A.E. ("HH Egyptian Company")	Egypt	USD18,000,000	USD15,450,000	50%	Manufacturing and sale of drilling rigs, parts and components
Honghua — Ukraine Limited	Ukraine	Ukraine Hryvnia 51,500	Ukraine Hryvnia 51,500	50%	Trading of drilling rigs, parts and components

Summary financial information on the jointly controlled entities — group's effective interest

	The group 2011 RMB'000	2010 RMB'000
Non-current assets	**53,622**	57,991
Current assets	**62,908**	64,444
Current liabilities	**(67,753)**	(33,651)
Non-current liabilities	**(9,858)**	(46,916)
	38,919	41,868
Income	**45,576**	50,712
Expenses	**(45,283)**	(47,911)
Profit for the year	**293**	2,801

17 INTEREST IN AN ASSOCIATE

	The group	
	2011	2010
	RMB'000	RMB'000
Share of net assets	**63,405**	—

Particulars of the associate, which is an unlisted corporate entity, are as follows:

Name of company	Place of establishment	Issued capital	Paid up capital	Group's effective interest held by a subsidiary	Principal activities
Chengdu Jinkong (成都金控融資租賃有限公司)	The PRC	RMB233,330,000	RMB233,330,000	25.71%	Lease financing

Summary financial information on the associate:

	Assets RMB'000	Liabilities RMB'000	Equity RMB'000	Revenues RMB'000	Profit RMB'000
2011					
100 per cent	777,659	523,193	254,466	52,599	20,997
Group's effective interest	193,768	130,363	63,405	13,526	5,398

18 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

18 INVENTORIES (continued)

(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

19 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 (note 19(b))	**(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.

19 TRADE AND OTHER RECEIVABLES (continued)

(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. Further details on the group's credit policy are set out in note 31(a).

(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 (see note 2(l)).

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

19 TRADE AND OTHER RECEIVABLES (continued)

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

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 recognized. 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
	RMB'000	RMB'000
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 19(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.

20 OTHER FINANCIAL ASSETS

As at 31 December 2011, other financial assets consisted of principal-protected structural deposits placed in several commercial banks in the PRC.

21 PLEDGED BANK DEPOSITS

The deposits are pledged to banks as security against bills payable (see note 24) and letters of credit issued to the group.

22 CASH AND CASH EQUIVALENTS

	The group		The company	
	2011	2010	**2011**	2010
	RMB'000	RMB'000	**RMB'000**	RMB'000
Cash at bank and in hand	**851,847**	1,002,727	**16,628**	19,890

As at 31 December 2011, deposits that were placed with banks in the PRC and included in the cash and cash equivalents above amounted to RMB708,511,005 (2010: RMB787,052,676). Remittance of funds out of the PRC is subject to the exchange restrictions imposed by the PRC government.

23 INTEREST-BEARING BORROWINGS

The interest bearing borrowings were secured as follows:

	The group	
	2011	2010
	RMB'000	RMB'000
Bank loans — secured	**13,232**	13,908
Bank loans — unsecured	**866,506**	612,410
Total	**879,738**	626,318

Interest-bearing borrowings of RMB13,232,000 (2010: RMB13,908,000) as at 31 December 2011 were secured by all assets of a subsidiary with an aggregate carrying value of RMB328,934,000 (2010: RMB322,125,000).

23 INTEREST-BEARING BORROWINGS (continued)

The interest-bearing borrowings were repayable as follows:

	The group	
	2011	2010
	RMB'000	RMB'000
Within 1 year	**499,738**	444,000
After 1 year but within 2 years	**150,000**	30,000
After 2 years but within 5 years	**230,000**	152,318
	380,000	182,318
Total	**879,738**	626,318

Certain banking facilities of the group are subject to the fulfilment of covenants as are commonly found in lending arrangements with financial institutions. If the group breaches the covenants, the drawn down facilities would become payable on demand. The group regularly monitors its compliance with these covenants. Further details of the group's management of liquidity risk are set out in note 31(b). As at 31 December 2011 and 2010, none of the covenants relating to drawn down facilities had been breached.

24 TRADE AND OTHER PAYABLES

	The group		The company	
	2011	2010	**2011**	2010
	RMB'000	RMB'000	**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	**21,582**	1,118
	1,531,323	1,209,911	**21,582**	1,118

Bills payable as at 31 December 2010 and 2011 were secured by certain pledged bank deposits as disclosed in note 21. All of the trade and other payables are expected to be settled or recognised as income within one year or are repayable on demand.

24 TRADE AND OTHER PAYABLES (continued)

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

25 EMPLOYEE RETIREMENT BENEFITS

Defined contribution schemes

Pursuant to the relevant labour rules and regulations in the PRC, the PRC subsidiaries now comprising the group participates in defined contribution retirement benefit schemes (the "Schemes") organised by the PRC municipal government authorities whereby the group is required to make contributions to the Schemes at the rate of 20% to 22% (2010: 20% to 22%) of the standard wages determined by the relevant authorities in the PRC during the year ended 31 December 2011. The local government authority is responsible for the entire pension obligations payable to retired employees.

The group operates a Mandatory Provident Fund Scheme ("the MPF scheme") under the Hong Kong Mandatory Provident Fund Schemes Ordinance for employees employed under the jurisdiction of the Hong Kong Employment Ordinance. The MPF scheme is a defined contribution retirement scheme administered by independent trustees. Under the MPF Scheme, the group and its employees are each required to make contributions to the scheme at 5% of the employees' relevant income, subject to a cap of monthly relevant income of HKD20,000. Contributions to the scheme vest immediately.

The group has no other material obligation for the payment of pension benefits associated with the Schemes and the MPF scheme beyond the annual contributions described above. The group has no material obligation for the payment of overseas pension benefits.

26 EQUITY-SETTLED SHARE BASED PAYMENTS

(a) Pre-IPO Share Option Scheme

(i) The company adopted a pre-IPO share option scheme ("the Pre-IPO Option Scheme") on 21 January 2008 whereby employees of the group were given the rights to subscribe for shares in the company. 60,000,000 shares were granted on 21 January 2008.

(ii) Each 20% of options granted under the Pre-IPO Option Scheme will vest each year commencing from the listing date and the options are exercisable for a period of ten years. The group has no legal or constructive obligation to repurchase or settle the options in cash. Any vested option will be lapsed if not exercised by the employees in one month after they left the group.

(iii) The number and weighted average exercise prices of share options granted under Pre-IPO Option Scheme are as follows:

	2011		2010	
	Exercise price	**Number of options ('000 shares)**	Exercise price	Number of options ('000 shares)
Outstanding at the beginning of the year	**HKD3.83**	**59,085**	HKD3.83	59,329
Forfeited during the year	**HKD3.83**	**(389)**	HKD3.83	(104)
Lapsed during the year	**HKD3.83**	**(1,352)**	HKD3.83	(140)
Outstanding at the end of the year	**HKD3.83**	**57,344**	HKD3.83	59,085
Exercisable at the end of the year	**HKD3.83**	**45,875**	HKD3.83	35,463

The options outstanding at 31 December 2011 had a weighted average remaining contractual life of 6.08 years (2010: 7.08 years).

26 EQUITY-SETTLED SHARE BASED PAYMENTS (continued)

(b) Share Option Scheme

(i) The company also adopted a share option scheme ("the Share Option Scheme") on 21 January 2008 for any eligible employees of the entities within the group. The terms and conditions of the grants that existed during the year are as follows, whereby all options are settled by physical delivery of shares:

	Number of options ('000 shares)		Vesting conditions	Contractual life of options
Options granted:				
— on 15 April 2009	60,000	(i)	30% on 1 December 2009	10 years
		(ii)	30% on 14 April 2010	
		(iii)	40% on 15 April 2011	
— on 11 October 2010	2,200	(i)	40% on 25 October 2010	10 years
		(ii)	30% on 11 October 2011	
		(iii)	30% on 11 October 2012	
— on 11 June 2011	7,600*	(i)	30% on 19 June 2011	10 years
		(ii)	30% on 19 June 2012	
		(iii)	40% on 20 June 2013	
Total share options	69,800			

* 5,200,000 shares are granted to the directors of the group.

26 EQUITY-SETTLED SHARE BASED PAYMENTS (continued)

(b) Share Option Scheme (continued)

(ii) The number and weighted average exercise prices of share options are as follows:

	2011 Weighted average exercise price	**2011** Number of options ('000 shares)	2010 Weighted average exercise price	2010 Number of options ('000 shares)
Outstanding at the beginning of the year	**HKD1.26**	**60,435**	HKD1.27	59,291
Granted during the year	**HKD0.83**	**7,600**	HKD1.05	2,200
Exercised during the year	**HKD1.27**	**—**	HKD1.27	(579)
Forfeited during the year	**HKD1.27**	**(119)**	HKD1.27	(309)
Lapsed during the year	**HKD1.27**	**(1,193)**	HKD1.27	(168)
Outstanding at the end of the year	**HKD1.21**	**66,723**	HKD1.26	60,435
Exercisable at the end of the year	**HKD1.25**	**60,742**	HKD1.26	35,447

The options outstanding at 31 December 2011 had an exercise price in the range of HKD0.83 to HKD1.27 (2010: HKD1.05 to HKD1.27) and a weighted average remaining contractual life of 7.59 years (2010: 8.33 years).

The weighted average share price at the date of exercise for share options exercised during the year ended 31 December 2010 was HKD1.71.

(c) Fair value of share options and assumptions

The fair value of services received in return for share options granted is measured by reference to the fair value of share options granted. The estimate of the fair value of the share options granted is measured based on a Binomial Option Pricing Model. The contractual life of the share option is used as an input into this model. Expectations of early exercise are incorporated into the Binomial Option Pricing Model.

The expected volatility is based on the historic volatility (calculated based on the weighted average remaining life of the share options), adjusted for any expected changes to future volatility based on publicly available information. Changes in the subjective input assumptions could materially affect the fair value estimated.

26 EQUITY-SETTLED SHARE BASED PAYMENTS (continued)

(c) Fair value of share options and assumptions (continued)

Fair value of share options and assumptions

	Share options granted in	
	2011	2010
Fair value at measurement date	**HKD0.39**	HKD0.37
Share price	**HKD0.78**	HKD1.05
Exercise price	**HKD0.83**	HKD1.05
Expected volatility (expressed as weighted average volatility used in the modelling under Binomial Lattice Model)	**58.2%**	47.8%
Option life (expressed as weighted average life used in the modelling under Binomial Option Pricing Model)	**10 years**	10 years
Expected dividends	**0.000%**	0.000%
Risk-free interest rate	**2.261%**	2.039%

27 INCOME TAX IN THE BALANCE SHEET

(a) Current taxation in the balance sheet represents:

	The group	
	2011	2010
	RMB'000	RMB'000
Income tax		
Provision for income tax	**42,630**	12,801
Income tax paid	**(18,142)**	(16,675)
	24,488	(3,874)
Balance of income tax recoverable in respect of prior years	**(20,363)**	(12,438)
	4,125	(16,312)
Represented:		
Current tax recoverable	**(34,418)**	(27,508)
Current tax payable	**38,543**	11,196
	4,125	(16,312)

27 INCOME TAX IN THE BALANCE SHEET (continued)

(b) Deferred taxation

The components of deferred tax assets/(liabilities) recognised in the group's balance sheet and the movements during the year are as follows:

	Write-down inventories RMB'000	Provision for product warranties RMB'000	Insurance premium paid RMB'000	Unrealised profit on inventories RMB'000	Allowance for doubtful debts RMB'000	Withholding tax on dividends RMB'000	Accruals RMB'000	Tax losses RMB'000	Total RMB'000
Deferred tax arising from:									
At 1 January 2010	10,439	1,947	(4,078)	12,998	18,240	(6,336)	5,748	–	38,958
Credited/(charged) to profit or loss (note 7(a))	4,550	413	(253)	773	–	(1,947)	(5,748)	19,981	17,769
Exchange difference	–	–	128	–	–	–	–	–	128
At 31 December 2010	14,989	2,360	(4,203)	13,771	18,240	(8,283)	–	19,981	56,855
At 1 January 2011	**14,989**	**2,360**	**(4,203)**	**13,771**	**18,240**	**(8,283)**	**–**	**19,981**	**56,855**
Credited/(charged) to profit or loss (note 7(a))	**3,774**	**583**	**–**	**5,841**	**2,416**	**(6,409)**	**1,906**	**392**	**8,503**
Exchange difference	**–**	**–**	**190**	**–**	**–**	**–**	**–**	**–**	**190**
At 31 December 2011	**18,763**	**2,943**	**(4,013)**	**19,612**	**20,656**	**(14,692)**	**1,906**	**20,373**	**65,548**

	The group	
	2011	2010
	RMB'000	RMB'000
Deferred tax assets recognised on the balance sheet	**84,253**	69,341
Deferred tax liabilities recognised on the balance sheet	**(18,705)**	(12,486)
	65,548	56,855

28 PROVISION FOR PRODUCT WARRANTIES

	The group	
	2011	2010
	RMB'000	RMB'000
At 1 January	**15,738**	15,579
Provision made	**26,912**	26,593
Utilised during the year	**(21,407)**	(26,434)
At 31 December	**21,243**	15,738

Under the terms of the group's sales arrangements, the group will rectify any product defects arising within the period specified in the respective sales contracts. The provision is based on estimates made from historical warranty data associated with similar products. The group expects to incur most of the liability over the next year.

29 AMOUNTS DUE FROM/(TO) SUBSIDIARIES

The amounts due from/(to) subsidiaries are unsecured, interest-free and have no fixed repayment terms.

30 CAPITAL, RESERVES AND DIVIDENDS

(a) Movements in components of equity

The reconciliation between the opening and closing balances of each component of the group's consolidated equity is set out in the consolidated statement of changes in equity. Details of changes in the company's individual components of equity between the beginning and the end of the year are set out below:

The company

	Note	Share capital RMB'000 (note 30(c))	Share premium RMB'000 (note 30(d)(i))	Other reserve RMB'000 (note 30(d)(ii))	Capital reserve RMB'000 (note 30(d)(iii))	Exchange reserve RMB'000 (note 30(d)(v))	Accumulated losses RMB'000	Total RMB'000
At 1 January 2010		299,542	2,476,705	389,691	72,475	(136,374)	(8,116)	3,093,923
Total comprehensive income for the year		–	–	–	–	(103,390)	(44,972)	(148,362)
Equity-settled share-based transactions	26	–	–	–	17,574	–	–	17,574
Shares issued under share option schemes	26	51	814	–	(217)	–	–	648
Options lapsed under share option schemes	26	–	–	–	(224)	–	224	–
At 31 December 2010		299,593	2,477,519	389,691	89,608	(239,764)	(52,864)	2,963,783
At 1 January 2011		**299,593**	**2,477,519**	**389,691**	**89,608**	**(239,764)**	**(52,864)**	**2,963,783**
Total comprehensive income for the year		**–**	**–**	**–**	**–**	**(139,135)**	**(62,864)**	**(201,999)**
Equity-settled share-based transactions	26	**–**	**–**	**–**	**7,590**	**–**	**–**	**7,590**
Options lapsed under share option schemes	26	**–**	**–**	**–**	**(2,098)**	**–**	**2,098**	**–**
At 31 December 2011		**299,593**	**2,477,519**	**389,691**	**95,100**	**(378,899)**	**(113,630)**	**2,769,374**

30 CAPITAL, RESERVES AND DIVIDENDS (continued)

(b) Dividends

Dividends payable to equity shareholders of the company attributable to the year:

	2011 RMB'000	2010 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.

(c) Share capital

Authorised and issued share capital

	2011 **Number of shares**	**Amount '000**	2010 Number of shares	Amount '000
Authorised:				
Ordinary shares of HKD0.1 each	**10,000,000,000**	**HKD1,000,000**	10,000,000,000	HKD1,000,000
Equivalent to:		**RMB968,739**		RMB968,739
Ordinary shares, issued and fully paid:				
		RMB'000		RMB'000
At 1 January	**3,223,798,400**	**299,593**	3,223,219,100	299,542
Shares issued under share option schemes (note 26(b)(ii))	**–**	**–**	579,300	51
At 31 December	**3,223,798,400**	**299,593**	3,223,798,400	299,593

30 CAPITAL, RESERVES AND DIVIDENDS (continued)

(d) Nature and purpose of reserves

(i) Share premium

The application of the share premium account is governed by the Companies Law (Revised) of the Cayman Islands. The fund in the share premium account of the company is distributable to the shareholders of the company provided that immediately following the date on which the dividend is proposed to be distributed, the company will be in a position to pay off its debts as they fall due in the ordinary course of business.

(ii) Other reserve

The other reserve represents the difference between the nominal value of share of the subsidiaries acquired over the nominal value of the shares issued by the company in exchange, the difference between acquisitions of non-controlling interests and entities under common control over the consideration given and the contribution of technology licenses by shareholder.

(iii) Capital reserve

Capital reserve represents the value of employee services in respect of share options granted under the Pre-IPO Options Scheme and the Share Option Scheme as set out in note 26 and waiver of debts by the immediate holding company.

(iv) Surplus reserve

Pursuant to applicable PRC regulations, PRC entity is required to appropriate 10% of its profit-after-tax (after offsetting prior year losses) to the reserve until such reserve reaches 50% of the registered capital. The transfer to the reserve must be made before distribution of dividends to shareholders. The surplus reserve can be utilised, upon approval by the relevant authorities, to offset accumulated losses or to increase registered capital of the PRC subsidiaries, provided that the balance after such issue is not less than 50% of its registered capital.

(v) Exchange reserve

The exchange reserve comprises all foreign exchange differences arising from the translation of the financial statements of operations outside the PRC which are dealt with in accordance with the accounting policies as set out in note 2(v).

30 CAPITAL, RESERVES AND DIVIDENDS (continued)

(e) Distributability of reserves

The company's reserves available for distribution to its shareholders comprise share premium net of accumulated losses which amounted to RMB2,363,889,000 as at 31 December 2011 (2010: RMB2,424,655,000). Under the Companies Law (Revised) of the Cayman Islands, the share premium of the company is available for paying distributions or dividends to shareholders subject to the provisions of its memorandum and articles of association and provided that immediately following the payment of distribution or dividends, the company is able to pay its debts as they fall due in the ordinary course of business. In accordance with the company's articles of association, distributions shall be payable out of the profits or other reserves, including the share premium account, of the company.

(f) Capital management

The group's primary objectives when managing capital are to safeguard the group's ability to continue as a going concern, so that it can continue to provide returns for shareholders and to maintain an optimal capital structure to reduce the cost of capital.

The group's capital structure is regularly reviewed and managed in accordance with the capital management practices of the group and in light of changes in economic conditions affecting the group, to the extent that these do not conflict with the directors' fiduciary duties towards the group.

Consistent with the industry practice, the group's capital structure is monitored on the basis of a net debt-to-capital ratio. For this purpose, net debt is defined as interest-bearing borrowings, trade and other payables and amounts due to related parties plus unaccrued proposed dividends of the group. The total capital is referred as shareholders' equity in the consolidated balance sheet.

During 2011, the group's strategy, which was unchanged from 2010, was to maintain sufficient capital to cover any net debt position by adjusting the amount of dividends paid to shareholders or issue new shares. The net debt-to-equity ratios as at 31 December 2011 and 2010 are 0.62 and 0.48 respectively.

Neither the company nor any of its subsidiaries is subject to externally imposed capital requirements.

31 FINANCIAL RISK MANAGEMENT AND FAIR VALUE

Exposure to credit, liquidity, interest rate, currency and business risks arises in the normal course of the group's business. The group's exposure to these risks and financial risk management policies and practices used by the group to manage these risks are described below.

(a) Credit risk

In respect of trade and other receivables, individual credit evaluations are performed on all customers requiring credit over a certain amount. These evaluations focus on the customer's past history of making payments when due and current ability to pay, and take into account information specific to the customer as well as pertaining to the economic environment in which the customer operates. 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. The group negotiates with those debtors with overdue balances to agree a repayment schedule by both parties and regularly evaluates the credit quality of its debtors to assess the necessity to revise the credit term. Debtors with balances that are more than 24 months past due are requested to settle all outstanding balances before any further credit is granted.

The group's exposure to credit risk is influenced mainly by the individual characteristics of each customer rather than the industry or country in which the customers operate and therefore significant concerns of credit risk primarily due to significant exposure to individual customers. At the balance sheet date, 30% (2010: 16%) and 51% (2010: 41%) of the total trade and other receivables was due from the group's largest debtor and the five largest debtors respectively.

Except for the financial guarantee given by the group as set out in note 36(b), the group does not provide any other guarantees which would expose the group or the company to credit risk. The maximum exposure to credit risk in respect of the financial guarantee at the balance sheet date is disclosed in note 36(b).

The credit risk on cash at bank and pledged bank deposits is limited as the counterparties are banks with sound credit standing. Majority of the group's cash at bank and pledged bank deposits were deposited at the state-owned commercial banks in the PRC.

31 FINANCIAL RISK MANAGEMENT AND FAIR VALUE (continued)

(b) Liquidity risk

Individual operating entities within the group are responsible for their own cash management, including the short term investment of cash surpluses and the raising of loans to cover expected cash demands, subject to approval by the company's management when the borrowings exceed certain predetermined levels of authority.

The group's policy is to regularly monitor its liquidity requirements and its compliance with lending covenants, to ensure that it maintains sufficient reserves of cash and adequate committed lines of funding from major financial institutes to meet its liquidity requirements in the short and long term.

The contractual undiscounted cash flows of the interest-bearing borrowings (including interest payments computed using contractual rates or, if floating, based on rates current at the balance sheet date) and earliest date the group can be required to pay are as follows:

The group

	2011 **RMB'000**	2010 RMB'000
Within 1 year	**535,668**	468,400
More than 1 year but less than 2 years	**156,134**	38,017
More than 2 years but less than 5 years	**239,329**	155,526
Total contractual undiscounted cash outflow	**931,131**	661,943
Balance sheet carrying value	**879,738**	626,318

Same as above, the group's and the company's other financial liabilities are required to be settled within one year or on demand and the total contractual undiscounted cash flows of these financial liabilities approximate to their carrying amounts on the balance sheets.

31 FINANCIAL RISK MANAGEMENT AND FAIR VALUE (continued)

(c) Interest rate risk

The group has interest-bearing assets carrying at floating rate as set out in the table below. The group's policy is to manage its interest rate risk to ensure there are no undue exposures to significant interest rate movements. The group does not use derivative financial instruments to hedge its fixed rate debt obligations. Most of the interest-bearing borrowings of the group as of 31 December 2011 are variable rate instruments. The group's management consider that the net exposure on interest rate risk is not significant and the increase in interest rates at the balance sheet date would not significantly affect the group's profit or loss.

(i) Interest rate profile

The following table details the interest rate profile of the group's and the company's interest-bearing assets and liabilities at the balance sheet date.

	The group			
	2011		2010	
	Effective interest rate %	**Amount RMB'000**	Effective interest rate %	Amount RMB'000
Fixed rate borrowings:				
Interest-bearing borrowings	**6.50%–7.70%**	**143,232**	3.80%–6.50%	614,087
Variable rate borrowings:				
Interest-bearing borrowings	**2.29%–7.22%**	**736,506**	2.34%–2.35%	12,231
Interest-bearing assets:				
Pledged bank deposits	**0–3.30%**	**65,612**	0–1.98%	29,072
Bank deposits maturing over three months	**3.00%–3.30%**	**9,100**	0.28%–2.25%	4,000
Cash and cash equivalents	**0.00%–0.70%**	**851,847**	0.00%–0.50%	1,002,727

	The company			
	2011		2010	
	Effective interest rate %	**Amount RMB'000**	Effective interest rate %	Amount RMB'000
Interest-bearing assets:				
Cash and cash equivalents	**0.00%**	**16,628**	0.00%	19,890

31 FINANCIAL RISK MANAGEMENT AND FAIR VALUE (continued)

(c) Interest rate risk (continued)

(ii) Sensitivity analysis

At 31 December 2011, it is estimated that a general change of 50 basis points in interest rates, with all other variables held constant, would increase/decrease the group's profit after tax by approximately RMB2,967,000 (2010: loss after tax RMB1,653,000).

The sensitivity analysis above indicates the instantaneous change in the group's profit after tax (and retained profits) that would arise assuming that the change in interest rates had occurred at the balance sheet date and had been applied to re-measure those financial instruments held by the group which expose the group to fair value interest rate risk at the balance sheet date. In respect of the exposure to cash flow interest rate risk arising from floating rate non-derivative instruments held by the group at the balance sheet date, the impact on the group's profit after tax (and retained profits) is estimated as an annualised impact on interest expense or income of such a change in interest rates. The analysis is performed on the same basis for 2010.

(d) Currency risk

The group is exposed to currency risk primarily through sales and purchases that are denominated in United States dollars ("USD") and Euros ("EUR"). The movements of USD and EUR will affect the revenue and costs of some production materials, spare parts and equipment purchases. The group minimises the currency risk by requesting deposits from customers and converting most of these deposits into RMB.

The group's investments in certain companies incorporated outside the PRC also expose the group to foreign currency risk mainly resulting from fluctuation of USD.

An appreciation of RMB against USD or EUR may have the effect of rendering exports from the group in the PRC more expensive and less competitive than products from other countries.

RMB is not freely convertible into foreign currencies. All foreign exchange transactions involving RMB must take place through the People's Bank of China or other institutions authorized to buy and sell foreign currencies. The exchange rate adopted for the foreign exchange transactions are the rates of exchange quoted by the commercial banks that are based on the middle price quoted by People's Bank of China and determined largely by supply and demand.

The following table details the group's and the company's exposure at the balance sheet date to currency risk arising from recognised assets or liabilities denominated in a currency other than the functional currency of the entity to which they relate. For presentation purposes, the amounts of the exposure are shown in RMB, translated using the spot rate at the year-end date.

31 FINANCIAL RISK MANAGEMENT AND FAIR VALUE (continued)

(d) Currency risk (continued)

The group

	Exposure to foreign currencies (expressed in RMB'000) 2011	
	USD	**EUR**
Cash and cash equivalents	**138,954**	**7,780**
Trade and other receivables	**756,511**	**59,436**
Interest-bearing borrowings	**(117,719)**	**—**
Trade and other payables	**(301,491)**	**—**
Overall net exposure	**476,255**	**67,216**

	Exposure to foreign currencies (expressed in RMB'000) 2010	
	USD	EUR
Cash and cash equivalents	148,733	907
Trade and other receivables	715,689	119,046
Interest-bearing borrowings	(99,341)	—
Trade and other payables	(224,426)	—
Overall net exposure	540,655	119,953

31 FINANCIAL RISK MANAGEMENT AND FAIR VALUE (continued)

(d) Currency risk (continued)

Sensitivity analysis

The following table indicates the instantaneous change in the group's profit after tax (and retained profits) that would arise if foreign exchange rates to which the group has significant exposure at the balance sheet date had changed at that date, assuming all other risk variables remained constant.

	The group					
	2011			2010		
	Weakening/ (Strengthening) of RMB against these currencies	Increase/ (Decrease) on profit after tax RMB'000	Increase/ (Decrease) on retained profits RMB'000	Weakening/ (strengthening) of RMB against these currencies	Increase/ (Decrease) on loss after tax RMB'000	Increase/ (Decrease) on retained profits RMB'000
USD	5%	12,039	12,039	5%	(26,059)	26,059
	(5%)	(12,039)	(12,039)	(5%)	26,059	(26,059)
EUR	5%	2,764	2,764	5%	(4,997)	4,997
	(5%)	(2,764)	(2,764)	(5%)	4,997	(4,997)

Results of the analysis as presented in the above table represent an aggregation of the instantaneous effects on each of the group entities' profit/loss after tax and equity measured in the respective functional currencies, translated into RMB at the exchange rate ruling at the balance sheet date for presentation purposes.

The sensitivity analysis assumes that the change in foreign exchange rates had been applied to re-measure those financial instruments held by the group which expose the group to foreign currency risk at the balance sheet date, including inter-company payables and receivables within the group which are denominated in a currency other than the functional currencies of the lender or the borrower. The analysis excludes differences that would result from the translation of the financial statements of foreign operations into the group's presentation currency. The analysis is performed on the same basis for 2010.

31 FINANCIAL RISK MANAGEMENT AND FAIR VALUE (continued)

(e) Fair values

The following methods and assumptions were used to estimate the fair value for each of the following classes of financial assets and liabilities:

(i) Cash and cash equivalents, pledged bank deposits, trade and other receivables and trade and other payables

The carrying values of these financial assets and liabilities approximate their fair value because of their short maturities.

(ii) Interest-bearing borrowings

The carrying amounts of interest-bearing borrowings approximate their fair value because the borrowing rates were similar to rates currently available for bank loans with similar terms and maturity.

(iii) Other financial assets

Other financial assets mainly consists of available-for-sale financial assets, which do not have quoted market price.

The group's management determines the fair value of the investments in other financial assets as at balance sheet date using certain unobservable inputs and consider that their respective fair value approximate their investments costs.

(iv) Amounts due from/to related companies

The amounts due from/to related companies are interest-free and have no fixed repayment terms. Given these terms, it is not meaningful to disclose fair values.

(f) Business risk

The group's revenue is generated mainly from the sale of drilling rigs and related parts and components. The revenue from the sale of drilling rigs and related parts and components used in the oil exploration and production industry is dependent on the exploration and development capital expenditures of oil producers and drilling services providers, which in turn is largely dependent on current prices of, and future trends in, global oil prices. The demand for oil exploration and development related services and the number of worldwide active rigs increase and decrease with fluctuations in the price of oil. Given the group's heavy reliance on customers in the oil drilling industry, the group's revenue could be highly sensitive to fluctuations in global oil prices.

32 COMMITMENTS

(a) Capital commitments

Capital commitments outstanding at 31 December 2011 not provided for in the financial statements were as follows:

	The group	
	2011	2010
	RMB'000	RMB'000
Contracted for	**355,533**	87,763
Authorised but not contracted for	**1,244,058**	1,823,486
	1,599,591	1,911,249

(b) Operating lease commitments

At 31 December 2011, the total future minimum lease payments under non-cancellable operating leases are payable as follows:

	The group	
	2011	2010
	RMB'000	RMB'000
Within 1 year	**4,399**	3,101
After 1 year but within 5 years	**5,064**	4,710
After 5 years	**8,566**	9,121
	18,029	16,932

The group is the lessee in respect of a number of properties held under operating leases. The leases typically run for an initial period of one to fifteen years. None of the leases includes contingent rentals.

33 MATERIAL RELATED PARTY TRANSACTIONS

In addition to the related party information disclosed elsewhere in the financial statements, the group entered into the following material related party transactions.

(a) During the year, the directors are of the view that the following companies are related parties of the group:

Name of party	Relationship
Guanghan Hongtai Business Trading Co. Ltd (廣漢市宏泰商貿有限公司) ("Hongtai Company")	Hongtai Company is a party which spouses of certain directors and management have equity interest.
NCE Management, LLC ("NCE Management")	NCE Management is a party which certain management of Honghua America have equity interest.
Luzhou City Jianming Decorating Design Company (瀘州市劍鳴裝飾設計公司) ("Luzhou Jianming Company")	Luzhou Jianming Company is a party which the brother of the spouse of a director of a group's subsidiary is the legal representative.
Guanghan Huite Fluid Appendix Co. Ltd (廣漢市惠特液壓附件有限公司) ("Guanghan Huite Company")	Guanghan Huite Company is a party which the brother of a director of a group's subsidiary has equity interest.
Chengdu Juzhong Technology Co., Ltd (成都巨中科技有限公司) ("Chengdu Juzhong Company")	Chengdu Juzhong Company is a party which the brother-in-law and brother-in-law's wife of a director of a group's subsidiary have equity interest.
HH Egyptian Company	Jointly controlled entity
Honghua — Ukraine Limited	Jointly controlled entity
Chengdu Jinkong	Associate

33 MATERIAL RELATED PARTY TRANSACTIONS (continued)

(b) Particulars of significant transactions between the group and the above related parties during the relevant period are as follows:

	The group	
	2011	2010
	RMB'000	RMB'000
Purchases of parts and components		
Hongtai Company	**15,442**	13,582
Chengdu Juzhong Company	**560**	848
Luzhou Jianming Company	**669**	917
Guanghan Huite Company	**809**	895
	17,480	16,242
Financial guarantees issued (see note 36(b))		
Chengdu Jinkong	**25,710**	—
Sale of drilling rigs, parts and components		
HH Egyptian Company	**63,529**	689

The directors of the company are of the opinion that the above related party transactions were conducted on normal commercial terms and in the ordinary course of business.

(c) Amounts due from related parties

	The group	
	2011	2010
	RMB'000	RMB'000
Trade		
HH Egyptian Company	**59,950**	23,009
Non-trade		
NCE Management	**2,167**	2,013
HH Egyptian Company	**2,042**	299
Honghua-Ukraine Limited	**666**	428
Amount due from immediate/ultimate holding company (see note 33(e))	**29**	12
	4,904	2,752
	64,854	25,761

The amounts due from related parties are unsecured, interest free and have no fixed repayment terms. No provision was made against the amounts due from related parties at 31 December 2011 (2010: RMB Nil).

33 MATERIAL RELATED PARTY TRANSACTIONS (continued)

(d) Amounts due to related parties

	The group	
	2011	2010
	RMB'000	RMB'000
Trade		
HH Egyptian Company	**6,674**	26,070
Hongtai Company	**5,955**	5,006
Luzhou Jianming Company	**55**	871
Guanghan Huite Company	**1,212**	1,152
Chengdu Juzhong Company	**12**	—
	13,908	33,099
Non-trade		
HH Egyptian Company	**14,177**	14,901
NCE Management	**205**	206
	14,382	15,107
	28,290	48,206

The amounts due to related parties are unsecured, interest free and have no fixed repayment terms.

(e) Amounts due from immediate/ultimate holding company

The amounts due from immediate/ultimate holding company are unsecured, interest free and have no fixed repayment terms. No provision was made against the amounts due from immediate/ultimate holding company at 31 December 2011 (2010: RMB Nil).

33 MATERIAL RELATED PARTY TRANSACTIONS (continued)

(f) Key management personnel remuneration

Remuneration for key management personnel of the group, including amounts paid to the company's directors as disclosed in note 8 and certain of the key management personnel as disclosed in note 9, is as follows:

	The group	
	2011	2010
	RMB'000	RMB'000
Basic salaries, allowances and other benefits in kind	**4,920**	1,846
Contributions to defined contribution retirement schemes	**175**	66
Discretionary bonus	**6,506**	952
Share-based payments	**2,802**	2,307
	14,403	5,171

Total remuneration is included in "staff costs" (see note 6(b)).

34 NON-ADJUSTING POST BALANCE SHEET EVENTS

Subsequent to the balance sheet date, Honghua Company entered into an equity transfer agreement to purchase 20% non-controlling interests of Youxin Company at a consideration of RMB28,961,700. Upon completion of the acquisition, Honghua Company will hold 100% equity interest of Youxin Company. In order to optimise the group resources, Honghua Company planned to dissolve Youxin Company afterwards. All assets and liabilities of Youxin Company will be assumed by Honghua Company.

35 IMMEDIATE AND ULTIMATE HOLDING COMPANY

The directors consider the immediate holding company and the ultimate holding company as at 31 December 2011 are Ally Giant Limited and Ample Chance International Limited respectively, which are incorporated in the British Virgin Islands. These entities do not produce financial statements available for public use.

36 CONTINGENT LIABILITIES

(a) Contingent liabilities in respect of legal claim

(i) Dispute with natural persons

As of 31 December 2005, 728 employees of Oil Drilling Plant (the "original investors"), through 11 representatives, held collectively, 33.63% of Honghua Company's share capital. These 11 representatives were registered as shareholders of Honghua Company with the competent PRC government authority. On 7 January 2006, Honghua Company passed a shareholders' resolution to reduce its registered capital and buy-out the equity interests from these 11 registered shareholders.

Honghua Company entered into a share purchase agreement with the 11 registered shareholders on 12 January 2006, under which, with the written consent of the 11 registered shareholders, it agreed to pay the share purchase price directly to the 728 original investors. The capital reduction process with the competent PRC government authority was completed on 26 April 2006. 64 of the 728 original investors, who collectively invested RMB651,385, refused to accept the payment from Honghua Company and claimed that they were still shareholders.

On 11 December 2007, 57 out of the 64 original investors initiated legal proceedings at the Intermediate Peoples' Court of Chengdu City, Sichuan Province. On 17 July 2008, another 2 individuals refused to accept the buy-out arrangement and payment from Honghua Company and sought the same relief as the 57 plaintiffs mentioned above.

On 23 June 2011, the 57 plaintiffs applied to amend and add claims including one against Honghua Company for damages of RMB341,949,961.58, including shares and dividend. The Court held a hearing for these amended claims on 30 September 2011 and the verdict is yet to be announced up to the date of these financial statements.

2 of the 64 investors accepted payment from Honghua Company on 29 March 2010 and 18 April 2011 respectively, who are not plaintiffs to the legal proceedings against Honghua Company.

The management, based on the PRC legal advisor's opinion, considered that these 64 original investors had never been properly registered as shareholders of Honghua Company with the competent PRC government authority. There is no legal basis under the PRC law for them to be regarded as shareholders of Honghua Company. Accordingly, the management determined that it is not probable that the outcome of the disputes will be unfavourable to the Group. No provision was made for the potential claims under this dispute.

36 CONTINGENT LIABILITIES (continued)

(a) Contingent liabilities in respect of legal claim (continued)

(ii) Lawsuits with former sales agencies

Three former sales agencies filed lawsuits against Honghua America, NCE Management, and Honghua Company on 22 September 2011. In their Second Amended Petition filed on 3 February 2012, these former agencies alleged that they are owed commissions in excess of USD83,600,000 in relation to Honghua Company's sales.

Based on the Group's US legal advisor's opinion, the management considered the relevant agreements have all expired by their terms when the Group entered into the sales transactions with the customers, and the Group has no obligation to pay commissions to these former agencies. Accordingly, the management determined that it is not probable that the outcome of the lawsuits will be unfavourable to the Group. No provision was made for the potential claims under this lawsuit.

(iii) Lawsuits with contractors and a former employee of Honghua America

Certain individual contractors and a former employee of Honghua America filed lawsuits against Honghua America in 2011, seeking compensation arising out of overtime and termination of employment. In their petitions and demand letters, the plaintiffs alleged damages, costs and fees in excess of USD3,173,297.

The management considered, based on the Group's US legal advisor's opinion, Honghua America has complied with the relevant US laws and acted appropriately to its contractors and former employee. Accordingly, the management determined that it is not probable that the outcome of the lawsuits will be unfavourable to the Group. No provision was made for the potential claims under this lawsuit.

(b) Financial guarantees issued

As at 31 December 2011, Honghua Holdings has issued a single guarantee to Chengdu Investment Holding Group, which is a shareholder of Chengdu Jinkong and provided financial guarantee in respect of a banking facility granted to Chengdu Jinkong that expires on 2 June 2012.

As at 31 December 2011, the management do not consider it probable that a claim will be made against Honghua Holdings under the single guarantee. 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).

(Expressed in Renminbi unless otherwise indicated)

37 POSSIBLE IMPACT OF AMENDMENTS, NEW STANDARDS AND INTERPRETATIONS ISSUED BUT NOT YET EFFECTIVE FOR THE YEAR ENDED 31 DECEMBER 2011

Up to the date of issue of these financial statements, the IASB has issued a number of amendments and interpretations and one new standard which are not yet effective for the year ended 31 December 2011 and which have not been adopted in these financial statements. These include the following which may be relevant to the group:

	Effective for accounting periods beginning on or after
Amendments to IAS 1, *Presentation of financial statements — Presentation of items of other comprehensive income*	1 July 2012
IFRS 10, *Consolidated financial statements*	1 January 2013
IFRS 11, *Joint arrangements*	1 January 2013
IFRS 12, *Disclosure of interests in other entities*	1 January 2013
IFRS 13, *Fair value measurement*	1 January 2013
IAS 27, *Separate financial statements (2011)*	1 January 2013
IAS 28, *Investments in associates and joint ventures*	1 January 2013
Revised IAS 19, *Employee benefits*	1 January 2013
Amendments to IFRS 7, *Financial instruments: Disclosures — Offsetting financial assets and financial liabilities*	1 January 2013
Amendments to IAS 32, *Financial instruments: Presentation — Offsetting financial assets and financial liabilities*	1 January 2014
IFRS 9, *Financial instruments (2009)*	1 January 2015
IFRS 9, *Financial instruments (2010)*	1 January 2015
Amendments to IFRS 9, *Financial instruments and IFRS 7 Financial instruments: Disclosures — Mandatory effective date and transition disclosures*	1 January 2015

The group is in the process of making an assessment of what the impact of these amendments is expected to be in the period of initial application. So far it has concluded that the adoption of them is unlikely to have a significant impact on the company's results of operations and financial position.

FIVE-YEAR FINANCIAL HIGHLIGHTS

	2011	2010	2009	2008	2007
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
			(restated)	(restated)	
Consolidated Income Statement					
Turnover	**3,485,046**	1,877,931	1,961,517	4,737,532	3,164,022
Cost of sales	**(2,514,942)**	(1,497,453)	(1,444,081)	(3,385,626)	(2,083,888)
Gross profit	**970,104**	380,478	517,436	1,351,906	1,080,134
Other revenue	**27,444**	29,900	7,085	5,375	22,999
Other net income/(loss)	**60,012**	(5,274)	9,234	13,662	22,475
Selling expenses	**(385,532)**	(180,642)	(179,980)	(369,787)	(210,319)
General and administrative expenses	**(408,877)**	(340,360)	(474,334)	(261,207)	(186,546)
Other operating expenses	**(19,295)**	(3,905)	(803)	(6,970)	(768)
Profit/(loss) from operations	**243,856**	(119,803)	(121,362)	732,979	727,975
Net finance expenses	**(50,335)**	(59,441)	(3,709)	(88,701)	(49,927)
Share of Profit/(loss) from jointly controlled entities	**293**	2,801	(4,766)	7,332	6,468
Share of profit from an associate	**5,398**	—	—	—	—
Profit/(loss) before taxation	**199,212**	(176,443)	(129,837)	651,610	684,516
Income tax (expenses)/credit	**(27,769)**	4,372	7,126	(115,560)	(67,511)
Profit/(loss) for the year	**171,443**	(172,071)	(122,711)	536,050	617,005
Attributable to:					
Equity shareholders of the Company	**167,984**	(184,165)	(127,963)	508,078	583,235
Non-controlling interests	**3,459**	12,094	5,252	27,972	33,770
Figures per share					
Earnings/(loss) per share (RMB cents)					
— Basic	**5.21**	(5.71)	(3.97)	16.1	23.3
— Diluted	**5.21**	(5.71)	(3.97)	16.1	23.3
Dividend					
Dividends declared and paid	**—**	—	—	287,671	—
Dividends declared and paid per share	**—**	—	—	HK$0.10	—
Dividend proposed after balance sheet date	**104,700**	—	—	170,371	—
Dividend proposed after balance sheet date per share	**HK$0.04**			HK$0.06	

FIVE-YEAR FINANCIAL HIGHLIGHTS

	2011 RMB'000	2010 RMB'000	2009 RMB'000 (restated)	2008 RMB'000 (restated)	2007 RMB'000
Consolidated Balance Sheet					
Total non-current assets	**1,882,332**	1,354,893	1,209,071	946,480	794,951
Total current assets	**4,810,368**	4,639,753	5,375,375	6,833,547	3,136,002
Total assets	**6,692,700**	5,994,646	6,584,446	7,780,027	3,930,953
Total current liabilities	**2,119,137**	1,729,051	2,062,235	3,232,425	2,555,556
Total non-current liabilities	**398,705**	194,804	262,804	24,090	19,686
Total liabilities	**2,517,842**	1,923,855	2,325,039	3,256,515	2,575,242
Total equity	**4,174,858**	4,070,791	4,259,407	4,523,512	1,355,711

Key financial ratios	**2011 RMB'000**	2010 RMB'000	2009 RMB'000 (restated)	2008 RMB'000 (restated)	2007 RMB'000
Profitability					
Gross margin	**27.8%**	20.3%	26.4%	28.5%	34.1%
EBITDA margin	**10.2%**	(1.5%)	(2.2%)	16.6%	24.0%
Net margin	**4.8%**	(9.8%)	(6.5%)	10.7%	18.4%
Return					
Return on average equity	**4.2%**	(4.5%)	(3.0%)	17.8%	73.3%
Return on average assets	**2.6%**	(2.9%)	(1.8%)	8.7%	19.1%
Liquidity					
Current ratio	**2.27**	2.68	2.61	2.11	1.23
Quick ratio	**1.54**	1.61	1.69	1.49	0.82
Turnover					
Turnover of average trade and bills receivable	**104**	163	217	105	101
Turnover of average trade and bills payable	**113**	145	177	87	107
Turnover of average inventory	**247**	458	497	165	151
Gearing					
Total debts/Total assets	**13.1%**	10.4%	19.7%	20.2%	22.2%
Total liabilities/Total assets	**37.6%**	32.1%	35.3%	41.9%	65.5%
EBIT/Interest expenses	**4.6**	(2.5)	(1.9)	11.2	18.7

Note:

Profitability

Gross margin	=	Gross profit/Revenue
EBITDA	=	(Loss)/profit from operations + Share of (loss)/profit from jointly controlled entities + Depreciation + Amortization
EBITDA margin	=	EBITDA/Revenue
Net margin	=	(Loss)/profit attributable to equity shareholders of the Company/Revenue

Return

Return on average assets	=	(Loss)/profit attributable to equity shareholders of the Company/Average assets
Return on average equity	=	(Loss)/profit attributable to equity shareholders of the Company/Average equity attributable to equity shareholders of the Company

Liquidity

Current ratio	=	Current assets/Current liabilities
Quick ratio	=	(Current assets-Inventory)/Current liabilities

Turnover

Turnover of average trade and bills receivable	=	365.25*Average trade and bills receivable/Revenue
Turnover of average trade and bills payable	=	365.25*Average trade and bills payable/Cost of sales
Turnover of average inventory	=	365.25*Average inventory/Cost of sales

Gearing

Total debts/Total assets	=	(Long term interest-bearing borrowings + Short term interest-bearing borrowings)/Total assets
Total liabilities/Total assets	=	Total liabilities/Total assets
EBIT/Interest expenses	=	((Loss)/profit from operations + Share of (loss)/profit from jointly controlled entities)/Interest expenses (including the interest expense capitalized into assets under construction)

DEFINITIONS

"Articles of Association"	the Articles of Association of the Company, approved at extraordinary shareholders' meetings of the Company on 21January 2008, revised and approved at annual general meeting of the Company on 3 June 2009
"Board of Directors" or "Board"	the Board of Directors of the Company
"Companies Ordinance"	the Companies Ordinance (Chapter 32 of the Laws of Hong Kong)
"Company" or "our Company"	Honghua Group Limited, (宏華集團有限公司) an exempted company incorporated in the Cayman Islands with limited liability on 15 June 2007
"Concert Group"	several shareholders of Honghua Company forming a concert group as set out in the "Company History and Reorganisation-Ownership Continuity and Control" section of the prospectus of the Company dated 25 February, 2008, namely, Zhang Mi (張弭), Ren Jie (任杰), Liu Zhi (劉智), Zheng Yong (鄭勇), Zuo Huixian (左輝先), Zhang Xu (張旭), Wang Jiangyang (王江陽), Chen Jun (陳俊), Fan Bing (范兵), Zhang Yanyong (張彥永), Ao Pei (敖沛), Tian Diyong (田弟勇), Shen Dingjian (沈定建), Liu Xuetian (劉學田) (deceased), Zhou Bing (周兵), Lv Lan (呂蘭), Tian Yu (田雨), Li Hanqiang (李漢強), Liu Yingguo (劉映國), Liu Lulu (劉露璐), He Guangfu (何光福), Zhang Zongyou (張宗友) and Chen Zongliang (陳宗良), out of which He Guangfu (何光福), Zhang Zongyou (張宗友) and Chen Zongliang (陳宗良) transferred an aggregate of approximately 9.1325% equity interests in Honghua Company to the other members of the Concert Group. The transfers were completed on February 17, 2006
"Controlling Shareholder(s)"	has the meaning ascribed thereto under the Listing Rules being, for the time being, Ally Giant Limited, Ample Chance International Limited, Ally Smooth Investments Limited, Charm Moral International Limited, Beauty Clear Holdings Limited, Believe Power International Limited, Benefit Way International Limited, Wealth Afflux Limited, Mowbray Worldwide Limited, Ecotech Enterprises Corporation, Vast & Fast Corporation, Cavendish Global Corporation, Brondesbury Enterprises Limited, Dobson Global Inc, Darius Enterprises Limited, Zhang Mi (張弭), Ren Jie (任杰), Liu Zhi (劉智), Zheng Yong (鄭勇), Zuo Huixian (左輝先), Zhang Xu (張旭), Wang Jiangyang (王江陽), Chen Jun (陳俊), Fan Bing (范兵), Zhang Yanyong (張彥永), Ao Pei (敖沛), Tian Diyong (田弟勇), Shen Dingjian (沈定建), Liu Xuetian (劉學田) (deceased), Zhou Bing (周兵), Lv Lan (呂蘭), Tian Yu (田雨), Li Hanqiang (李漢強), Liu Yingguo (劉映國) and Liu Lulu (劉露璐). Contracts executed by the Controlling Shareholders after Liu Xuetian's death were executed by his legal successors

"Director(s)"	member(s) of the Board of Directors of the Company
"During the Year"	for the year ended 31 December 2011
"Group" or "we" or "us"	the Company and its subsidiaries, and, for the period before the Company became the holding company for such subsidiaries, the entities which carried on the business of the Group
"HK$" or "HK dollars"	Hong Kong dollars, the lawful currency of Hong Kong
"Hong Kong" or "HK"	the Hong Kong Special Administrative Region of the PRC
"Honghua Company"	Sichuan Honghua Petroleum Equipment Co., Ltd. (四川宏華石油設備有限公司), formerly known as Chuanyou Guanghan Honghua Co., Ltd. (川油廣漢宏華有限公司), a limited liability company established in the PRC on 31 December 1997, and a wholly-owned subsidiary of Honghua Holdings Limited
"Hongtai Company"	Guanghan Hongtai Business Trading Co., Ltd (廣漢市宏泰商貿有限公司), a limited liability company established in the PRC on June 21, 2002
"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)
"PRC" or "China"	the People's Republic of China and, except where the context requires and only for the purpose of this Annual Report, references in this Annual Report to the PRC or China do not apply to Taiwan or Hong Kong and Macau Special Administrative Regions
"RMB" or "Renminbi"	Renminbi, the lawful currency of the PRC
"Russia"	The Russian Federation

"Securities and Futures Commission" or "SFC"	the Securities and Futures Commission of Hong Kong
"SFO"	the Securities and Futures Ordinance (Chapter 571 of the Laws of Hong Kong)
"Share(s)"	ordinary shares issued by the Company, with a nominal value of HK$0.10 each
"Shareholder(s)"	holder(s) of our Share(s)
"Stock Exchange" or "HKSE"	The Stock Exchange of Hong Kong Limited
"Substantial Shareholder(s)"	has the meaning ascribed to it under the Listing Rules
"SZSE"	Shenzhen Stock Exchange
"UAE"	the United Arab Emirates
"United States", "USA" or "U.S."	the United States of America, including its territories and possessions
"US$" or "U.S. dollars" or "USD"	United States dollars, the lawful currency of the United States

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