HONGHUA GROUP LIMITED
宏華集團有限公司

HONGHUA GROUP LIMITED 宏華集團有限公司

ANNUAL REPORT 2009

HONGHUA GROUP LIMITED
宏華集團有限公司

(incorporated in the Cayman Islands with limited liability)
Stock Code: 196

ANNUAL REPORT 2009



CONTENTS

FINANCIAL HIGHLIGHTS

	2009 RMB'000	2008 RMB'000	Changes
Operating results			
Revenue	**1,961,517**	4,737,532	(58.6%)
(Loss)/profit from operations	**(120,736)**	736,875	(116.4%)
(Loss)/profit before taxation	**(129,211)**	655,506	(119.7%)
(Loss)/profit attributable to equity shareholders of the Company	**(127,337)**	511,974	(124.9%)
Figures per share			
(Loss)/earnings per share — Basic (RMB cents)	**(3.95)**	16.22	(124.4%)
(Loss)/earnings per share — Diluted (RMB cents)	**(3.95)**	16.22	(124.4%)
Special dividends declared and paid per share during the year	**—**	HK$0.10	(100.0%)
Final dividends proposed after the balance sheet date per share	**—**	HK$0.06	(100.0%)
Financial position			
Total non-current assets	**1,209,071**	946,480	27.7%
Total current assets	**5,379,897**	6,837,443	(21.3%)
Total assets	**6,588,968**	7,783,923	(15.4%)
Total current liabilities	**2,062,235**	3,232,425	(36.2%)
Total non-current liabilities	**262,804**	24,090	990.9%
Total liabilities	**2,325,039**	3,256,515	(28.6%)
Total equity	**4,263,929**	4,527,408	(5.8%)
Key financial ratios*			
Gross margin	**26.4%**	28.6%	(2.2%)
Net margin	**(6.5%)**	10.8%	(17.3%)
Return on average assets	**(1.8%)**	8.7%	(10.5%)
Return on average equity	**(3.0%)**	17.9%	(20.9%)
Current ratio	**2.61**	2.12	0.49
Quick ratio	**1.69**	1.49	0.20
Total debts/Total assets	**19.7%**	20.2%	(0.5%)
Total liabilities/Total assets	**35.3%**	41.8%	(6.5%)

* *Earnings exclude minority interests*
Equity excludes minority 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

Chen Guoming
Liu Xiaofeng
Qi Daqing
Tai Kwok Leung, Alexander
Wang Li
Shi Xingquan

SECRETARY OF BOARD OF DIRECTORS

Liu Gangqiang

BOARD COMMITTEE

Audit Committee

Qi Daqing *(Committee Chairman)*
Chen Guoming
Liu Xiaofeng
Tai Kwok Leung, Alexander
Wang Li
Shi Xingquan

Corporate Governance Committee

Liu Xiaofeng *(Committee Chairman)*
Chen Guoming
Qi Daqing
Tai Kwok Leung, Alexander
Wang Li
Shi Xingquan

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
Wang Li

JOINT COMPANY SECRETARIES

Liu Gangqiang
Corinna Leung

QUALIFIED ACCOUNTANT

Lu Hong *(FCCA, HKICPA, CICPA)*

LEGAL ADVISORS

as to Hong Kong law

King & Wood

as to PRC LAW

King & Wood

as to Cayman Islands law

Appleby

PRINCIPAL BANKERS

Bank of China Limited
Agricultural Bank of China
China Merchants Bank Co., Ltd
Industrial and Commercial Bank of China Limited
China Construction Bank Corporation
Hong Kong and Shanghai Banking Corporation Limited
The Export-Import Bank of China

AUDITOR

KPMG
Certified Public Accountants

COMPLIANCE ADVISOR

CCB International Capital Limited

REGISTERED OFFICE

Clifton House,
75 Fort Street, PO Box 1350
Grand Cayman, KY1-1108
Cayman Island

HEAD OFFICE

99 East Road, Information Park,
Jinniu District
Chengdu, Sichuan 610036
PRC

PLACE OF BUSINESS IN HONG KONG

Room 2508, Harcourt House
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
Shops 1712–1716,
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

Facing the drastic decline of the Group's business performance and the recording of a loss in 2009, the management has given serious reflection on the situation and proactively implemented corrective measures for improvement. Following the steady growth of oil and gas demand, Honghua is confident in implementing its growth strategies with a focus on energy industries, building on its foundation of technical expertise in equipment manufacturing to expand into the energy resource and oilfield service sectors, so as to resume its growth momentum.

ZHANGMI
CHAIRMAN

DEAR SHAREHOLDERS,

On behalf of the board of Directors, I am to announce the annual results for the year ended 31 December 2009 (the "Year").

Under the influence of the economic crisis, global industrial production experienced a sharp decline, which led to the rapid deterioration of the international land drilling rig market. As a result, the Group recorded a revenue of approximately RMB1,962 million, representing a decline of 58.6% as compared to RMB4,738 million in the same period last year. During the Year, gross profit of the Group amounted to RMB518 million, representing a decrease of 61.8% as compared to the same period last year. Loss attributable to shareholders amounted to RMB127 million, whereas a profit attributable to shareholders of RMB512 million was recorded in the same period last year. The Board does not recommend payment of a final dividend.

MARKET OVERVIEW

Since the second half of 2008, the global economic recession brought about by the financial crisis has led to a weakened demand in the oil and gas industry. In addition to the global credit crunch, most oil companies have reduced their capital expenditure, or even delayed orders or cancelled related investments.

2009 was a challenging and volatile year for the global land drilling rig market. In the first half of 2009, due to decreasing oil exploration activities as well as drilling rig dayrates, the number of active drilling rigs decreased drastically as compared to 2008. Statistics from Rigzone indicate that the U.S. and Europe experienced relatively significant drops in active drilling rig count, with declines of 56% and 45% respectively, whereas the Middle East and Central Asia experienced drops of approximately 15% on average. In the second half of 2009, due to the launch of economic stimulus packages in various countries, the global economic recession was gradually alleviated, followed by resumed oil demand and stabilized oil prices, as well as an increasing number of active rigs globally.

BUSINESS DEVELOPMENT

In the face of weakened demand for drilling rigs in 2009, the Group sold 40 units of drilling rigs and 117 units of mud pumps and a number of various related parts and components. During the Year, leveraging on its leading research and development capabilities, the Group produced numerous high-performance-to-value products to satisfy the needs of different markets, which offset the impact of the shrinking land drilling rig market to some extent. Among which, desert trailer drilling rigs were tailor-made for the Middle-Eastern market, of which 13 units were sold during the Year. Sales from the Middle-Eastern market accounted for 39.6% of total sales, representing a significant increase as compared to 8.8% in the same period last year. Furthermore, during the Year, the Group has signed sales and purchase agreements for land drilling rigs and jack-up packages with Shanghai Zhenhua Heavy Industry Co., Ltd. worth over RMB2.3 billion in total. This allows the Group to consolidate its land drilling business, and at the same time extend its business to enter the offshore segment, building an important foundation for the Group's further entry into the offshore drilling market.

Some Directors and senior management of the Company with officials in Qidong visited Honghua offshore base

Honghua Group annual meeting in 2009

During the Year, the Group actively developed new products to enhance performance and value, so as to capture future business opportunities brought by gradual economic recovery. In terms of development for drilling rigs, train-skidding arctic rigs and helicopter-mounted drilling rigs developed by the Group have successfully penetrated the European market and received positive feedback from clients for their excellent performance. Furthermore, the Group has successfully developed continuous pipe rigs to satisfy clients' needs for shallow oil and gas exploration, which further enriched the Group's product mix.

As for parts and components, during the Year, the Group increased its intensity on the research and development of high performance, valued-added parts and components for oil and gas exploration, including the leading PRC developed planetary gearbox drawworks and direct-drive mud pumps. During the Year, top drives developed by the Group have been sold to the Europe and the Central Asia and Central Asian customer. We believe, by having continuous innovation to suit market needs, developing a product mix with high performance-to-value as well as enhancing in-house production of parts and components and its efficiency, the Group will be able to enlarge its worldwide market share.

During the Year, under the "sales advancement" strategy, the Group set up offices or subsidiaries in Uzbekistan, Russia, India, Indonesia and Pakistan to enhance its international sales network and expand its client base to further extend income sources, providing a strong impetus for future business expansion.

CORPORATE GOVERNANCE

During the Year, the Group continued to enhance internal controls to effectively manage operational and financial risks. Meanwhile, with the assistance of IBM the Group has steadily propelled the ERP project to improve management and streamline operation procedures including supply, production and sales, so as to strengthen controls on key processes and further enhance the effectiveness of the Group's operation.

In addition, the Group has received numerous awards for being socially responsible such as protecting staff rights and actively participating in charity work.

PROSPECT

As the global economy gradually recovers, it is expected that the upstream oil and gas companies will increase expenditure on oil and gas exploration. In the meantime, the exploration of unconventional energy (especially for shale gas) and offshore oil and gas exploration will advance technological development and boost the demand for high performance oil drilling equipment, driving the growth of the overall oil and gas equipment industry.

The group will continue to build on its market leadership in the land drilling sector through constant innovation, increased research intensity and enhanced product designs. We will set up an office in Kazakhstan and put more efforts to develop markets in Europe and the Central Asia. As the offshore equipment manufacturing industry shifts to developing countries, the Group is endeavored to capture opportunities through accelerating the construction of its infrastructure in the offshore production base. Meanwhile, we will enhance research and development of offshore drilling modules and platforms so as to lay a solid foundation for penetrating the offshore drilling and exploration market.

Furthermore, Honghua Oil & Gas Engineering Services Limited has commenced operation. Leveraging on the Group's competitive advantages in drilling rig equipment and technological expertise, the oilfield services segment is expected to become one of the new revenue drivers in the near future.

The management of the Group has seriously reflected upon the revenue decrease and the loss during the Year. The Group will continue focus on risk control, further enhance internal control. As for business development, as a manufacturer mainly focusing on land drilling rigs and parts and components, the Group's ability to withstand risks is relatively weak when faced with an adverse economic and market environment. Therefore, in the next ten years, the Group will gradually transform into a diversified operation involving "Two Fields and Three Sectors". This indicates that based on the solid experience on land and offshore oil and gas equipment manufacturing, the Group will gradually extend its production chain to realise vertical and horizontal expansion, so as to develop into a diversified energy company with interactive development in the fields of equipment production, resource exploration and engineering services. We dedicate our best efforts to realise the Group's long-term development goals and bring maximised returns to shareholders.

ACKNOWLEDGEMENT

On behalf of the Board, I would like to express my gratitude to all Shareholders, customers and business partners for their trust and support. Furthermore, 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.

Zhang Mi
Chairman
Hong Kong, 13 April 2010

MANAGEMENT DISCUSSION AND ANALYSIS

MARKET OVERVIEW

The global financial crisis continued to adversely affect the world economy in 2009 and brought a stern challenge to the global oil drilling industry. The drop in oil demand, together with uncertain economic prospects led to a reduction in expenditure on oil exploration, lowered drilling activities and drilling rig day rates. However, due to the launch of economic stimulus packages and monetary policies in different countries, the global economic downturn began to gradually alleviate from the second half of 2009 and industrial production as well as the oil price gradually resumed. As a result, the number of existing drilling rigs gradually recovered from its low point, providing support for the steady recovery of the global oil drilling industry.

BUSINESS REVIEW

In light of the challenging market conditions, the Group has proactively strengthened its internal management, put additional emphasis on product research and development, and continued to implement a "sales advancement" strategy. While maintaining its long-term relationship with existing clients, the Group has been proactively building its global sales network and expanding its marketing and sales efforts in emerging markets. During the Year, as the Middle East and Central Asia were relatively less affected by the economic crisis compared to the U.S. and European countries, the Group strategically enhanced market penetration in these regions. Leveraging on its superior performance-to-cost products, the Group sold 13 units of land drilling rigs in the Middle Eastern market, representing an increase of 6 units as compared to the same period last year, and subsequently received positive responses from clients which boost our confidence in expanding our business in this region. Furthermore, the Group has signed sales and purchase agreements with Shanghai Zhenhua Heavy Industry Co., Ltd., the largest heavy-duty equipment manufacturer in the world, for land drilling rigs and jack-up drilling packages worth over RMB2.3 billion. It not only provides strong support for the Group's land drilling business, but also creates favorable conditions to establish research, development and manufacturing of its offshore jack-up drilling platform.

Technical support at our customers' drilling sites

mud pump sets

The Group has confirmed the site for its new offshore production base in Qidong City, Jiangsu Province, and in the second half of 2009, infrastructure construction has commenced as scheduled. According to the Group's strategy, construction, equipment installation and production will take place concurrently so as to accelerate its completion and ensure that the designed production capacity target could be reached. Meanwhile, the Group has completed the initial construction of an offshore equipment research centre and sales centre in Shanghai, and the formation of related business operations and execution departments were orderly carrying on.

During the Year, through continuous enhancement of product quality and strengthening of its research and product design, the Group has maintained its competitiveness in the international market. For product research and development, the Group has developed various superior performance-to-cost products to meet the needs of different markets, including a new high speed drilling rig, desert trailer drilling rig for the Middle-Eastern market, a train-skidding arctic rig and helicopter-mounted drilling rigs for the Russian market, as well as continuous pipe rigs for shallow oil and gas exploration. Besides, the Group continued to develop high value-added parts and components to enhance in-house production. Our land rigs configured the top drive developed by the Group have been sold to the European customers during the Year. The sales and purchase agreements with Shanghai Zhenhua Heavy Industry Co., Ltd. for land drilling rigs and jack-up drilling packages will be equipped with the nation's leading direct-driven mud pump and planetary gearbox drawworks developed by the Group. Owing to their high performance, light weight and compact size, the clients will benefit from enhanced operational efficiency and reduced maintenance costs.

Furthermore, the Group continued to expand its research and development team during the Year. At the end of 2009, the Group had a total of 368 employees in research and development department in Chengdu, Guanghan and Shanghai. Currently, the Group has successfully applied for 43 patents (12 of which are awaiting approval from the State Intellectual Property Office of the PRC), which represents an increase of 12 patents approved as compared to the same period last year.

PROSPECTS

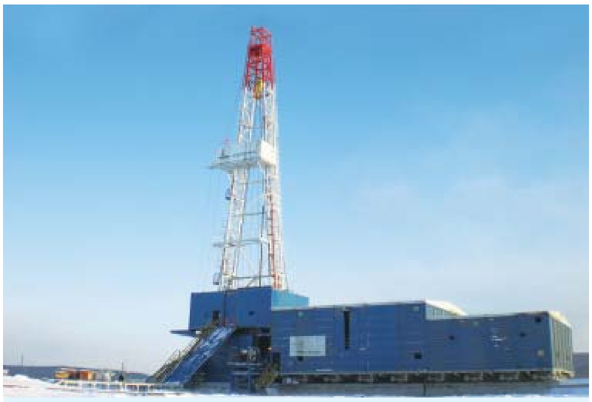
In 2010, as the global economy gradually recovers, energy consumption is expected to increase and capital expenditure on oil and gas exploration will grow accordingly. The International Energy Agency predicts that the global oil demand will increase from 85 million barrels per day in 2008 to 106 million barrels per day by 2030. A research report by Barclay's Capital also estimates that the global expenditure on oil and gas exploration and development could reach US$439 billion in 2010, representing an increase of 11% as compared to 2009. In the long-run, global oil and gas exploration and development will resume its long-term growth momentum.

The Group will continue to seize business opportunities in the drilling rig industry, strengthen its research and development capabilities, enhance product quality and enrich its product mix to satisfy different market needs for high performance drilling rigs. Furthermore, the Group will continuously expand its global sales network, especially in the markets such as the Middle-East, South America and Russia. The Group will adopt a "sales advancement" strategy to expand its client base so as to enhance the Group's competitiveness in the international market. Meanwhile, the Group will continue to push ahead with the construction of its offshore production base in Qidong City, Jiangsu Province, and improve the design, research and development of offshore drilling rigs through the establishment of an offshore equipment research centre in Shanghai. The Group will also focus on the marketing and promotion of its digitized prototype model to potential clients for achieving sales of the offshore drilling platform as soon as possible.

Facing the drastic decline of the Group's business performance and the recording of a loss in 2009, the management have given serious reflection on the situation. In the future, the Company will continue focus on risk control to improve the internal control process. Meanwhile, in order to enhance the ability to cope with risk in complex circumstances, through extending its production chain to realise vertical and horizontal expansion, the Group will gradually transform into a diversified energy company with interactive development in the fields of equipment production, resource exploration and engineering services based on the solid experience on land and offshore oil and gas equipment manufacturing. i.e "Two Fields and Three Sectors".

FINANCIAL REVIEW

During the Year, the Group's gross profit and loss attributable to shareholders amounted to approximately RMB518 million and approximately RMB127 million respectively, while the gross profit and profit attributable to shareholders amounted to approximately RMB1,356 million and approximately RMB512 million respectively in the same period last year. Gross margin and net loss margin amounted to 26.4% and 6.5% respectively. During the Year, the decrease in gross profit and increase in loss attributable to shareholders were mainly due to the adverse affects as a result of the global economic crisis, which led to a sharp reduction in revenue.



Train-skidding arctic rig developed by Honghua

Honghua 70DBS Drilling Rig successfully commenced drilling in Russia

REVENUE

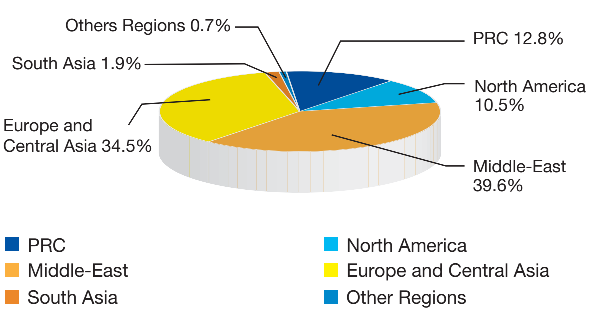
During the Year, the Group's revenue amounted to approximately RMB1,962 million, representing a decrease of approximately 58.6% as compared to approximately RMB4,738 million in the same period last year. The decrease was mainly attributable to decreased demand for land drilling rigs. The number of drilling rigs sold decreased from 94 units in 2008 to 40 units during the Year.

During the Year, revenue by geographical areas were as follows: revenue from exports amounted to approximately RMB1,711 million, representing a decrease of approximately RMB2,555 million as compared to the same period last year, accounting for approximately 87.2% of the Group's total revenue. The decrease was mainly attributable to the decrease in demand for drilling rigs in Europe and Central Asia, where the sales volume was 16 units during the Year, compared to 45 units in 2008, and a drop in the average selling price due to the variation in rig configurations. On the contrary, revenue from the Middle-Eastern market increased rapidly and recorded total sales of 13 units, compared to a total of 7 units in the same period last year. This was mainly attributable to the enhancement of sales network and improvement in the market initiatives of the Group's subsidiary in Dubai. Other markets including South Asia, North America, the PRC and other areas were all affected by the slowdown in rig demand. As a result, the sales volume in these markets were 3, 2, 6 and 0 units respectively, representing a decrease of 8, 1, 17, 5 units respectively as compared to the same period last year, leading to a decrease in revenue to different extents.

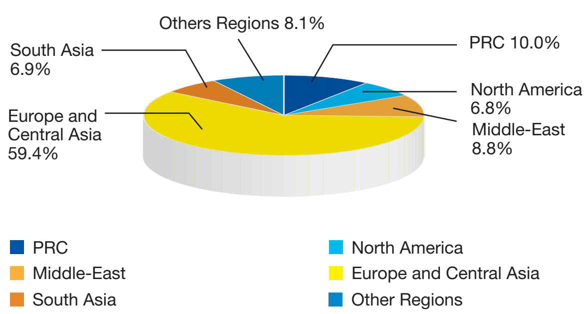
Ultrasonic detecting

SALES BY GEOGRAPHICAL AREA

Revenue in 2009



Revenue in 2008



During the Year, revenue by product categories are as follows:

By product category	For the year ended 31 December 2009 Revenue RMB'000	%	Quantity (Unit)	For the year ended 31 December 2008 Revenue RMB'000	%	Quantity (Unit)	2009 vs 2008 Change RMB'000	Change (%)
Digitally-controlled Rigs	**1,366,821**	**69.7%**	**31**	3,395,962	71.7%	57	(2,029,141)	-59.8%
Conventional Rigs	**282,832**	**14.4%**	**9**	963,958	20.3%	37	(681,126)	-70.7%
Subtotal	**1,649,653**	**84.1%**	**40**	4,359,920	92.0%	94	(2,710,267)	-62.2%
Mud Pumps	**123,403**	**6.3%**	**117**	113,732	2.4%	120	9,671	8.5%
Other Parts and Components	**188,461**	**9.6%**		263,880	5.6%		(75,419)	-28.6%
Subtotal	**311,864**	**15.9%**	**117**	377,612	8.0%	120	(65,748)	-17.4%
Total	**1,961,517**	**100.0%**		4,737,532	100.0%		(2,776,015)	-58.6%

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

During the Year, revenue from drilling rigs and parts and components were RMB1,650 million and RMB312 million respectively, representing a decrease of 62.2% and 17.4% as compared to RMB4,360 million and RMB378 million in the same period last year.

Drilling rigs comprise digitally-controlled land rigs and conventional land rigs, sales of which amounted to RMB1,367 million and RMB283 million respectively. The decrease in revenue from drilling rigs was mainly due to the decrease in sales volume of drilling rigs from 94 units in the same period last year to 40 units during the Year. During the Year, the Group recorded sales of 7 heavy 7000-meter drilling rigs, 8 medium 5000-meter drilling rigs and 8 medium 4000-meter drilling rigs, 14 light 3000-meter drilling rigs and 3 light 1000-meter drilling rigs, among which all 3000-meter drilling rigs were low-temperature drilling rigs sold to Russian clients.

The decrease in revenue from parts and components was mainly due to the decrease in demand for replacing old parts and components. However, the sale of mud pumps amounted to 117 units, which was approximately equal to that of last year (2008: 120 units). Among which, 9 high specification mud pumps were sold, driving the average selling price from RMB0.95 million last year to RMB1.05 million in the Year.

COST OF SALES

During the Year, the Group's cost of sales amounted to approximately RMB1,443 million, representing a decrease of approximately RMB1,938 million or 57.3% as compared to the same period last year. The decrease was mainly due to the decrease in the Group's revenue.

GROSS PROFIT AND GROSS MARGIN

During the Year, the Group recorded a gross profit of approximately RMB518 million, representing a decrease of 61.8% or RMB838 million as compared to the same period last year. Gross profit from drilling rigs amounted to approximately RMB431 million, representing a decrease of 65.1% as compared to the same period last year. Gross profit from digitally-controlled rigs and conventional rigs were RMB352 million and RMB79 million respectively, representing a decrease of 64.7% and 67.1% as compared to the same period last year. Gross profit from parts and components amounted to approximately RMB87 million, representing a decrease of 27.2% as compared to the same period last year.

During the Year, the Group's overall gross margin was 26.4%, representing a decrease of 2.2 percentage points as compared to that in the same period last year. The decrease was due to the fact that some of the drilling rigs were sold to trading company instead of end-users, reducing the profit margins. Meanwhile, the Group amended the raw materials imported for digitally-controlled drilling rigs in response to the change in need of clients.

The gross margin of drilling rigs was approximately 26.1%, representing a decrease of 2.2 percentage points as compared to 28.3% in the same period last year. Among which, the gross profit of digitally-controlled drilling rigs was 25.8%, representing a decrease of 3.5 percentage points compared to that in the same period last year. The gross margin of conventional drilling rigs was 27.8%, representing an increase of 3.0 percentage points compared to that in the same period last year.

Gross margin of rig parts and components was 28.0%, representing a decrease of 3.8 percentage points as compared to that in the same period last year. The decrease was mainly attributable to the decrease in exports of mud pumps, which have a higher profit margin than those sold domestically.

OTHER NET OPERATING REVENUE AND OTHER NET INCOME

During the Year, the Group's other net operating revenue amounted to approximately RMB6.28 million, as compared to other net operating expenses of approximately RMB1.60 million in the same period last year. The increase was mainly due to the increase of the maintenance service income during the Year. Other net income amounted to approximately RMB9.23 million, as compared to that of RMB13.66 million in the same period last year. The decrease was mainly attributable to realised gains on investments at fair value amounted to approximately RMB3.28 million last year while approximately RMB0.06 million during the Year.

EXPENSES IN THE YEAR

During the Year, the Group's selling expenses amounted to approximately RMB180 million, representing a decrease of RMB190 million or 51.3% as compared to RMB370 million in the same period last year, which was mainly due to the decrease in transportation costs. Transportation costs amounted to RMB85 million, representing a decrease of 67.2% as compared to RMB259 million in the same period last year. The decrease in transportation costs was mainly due to the decrease in sales volume and the sharp drop in the costs of drilling rigs delivery to Russia borne by the Group.

During the Year, the Group's general and administrative expenses amounted to approximately RMB351 million, representing an increase of RMB88 million or 33.4% as compared to RMB263 million in the same period last year. The increase was primarily based on the following: firstly, the expenses resulted from contract negotiation amounted to approximately RMB33 million during the Year, while none in the last year. Secondly, the amortisation of intangible assets arising from technological input by Nabors, which amounted to RMB37 million, compared to RMB12 million in the same period last year. The technology was put in use and began amortisation in September 2008. In addition, according to the quality control and the requirements of API application, an internationally renowned supervising company was engaged during the Year and hence the consultation fee recorded a significant growth to RMB17 million from RMB7 million in the same period last year.

During the Year, because the global economic crisis adversely affected our trade receivables, we have made a provision of approximately RMB123 million based on the payment ability of our clients.

During the Year, the Group's net finance expenses amounted to approximately RMB3.71 million, as compared to that of approximately RMB88.70 million in the same period last year. The sharp decrease was mainly due to the stable exchange rate between RMB and US dollars, as well as the 10% increase in the exchange rate of the Euro against RMB. The Group recorded a net exchange gain of approximately RMB24.43 million, compared to a net exchange loss of approximately RMB67.18 million last year.

SHARE OF LOSS/PROFIT FROM JOINTLY CONTROLLED ENTITIES

During the Year, the Group's share of loss from jointly controlled entities amounted to approximately RMB5 million, compared to a share of profit of RMB7 million in the same period last year, which was mainly attributable to the decrease in sales in Egyptian Petroleum HH Rig Manufacturing Shareholder Co.. 2 rigs were sold in the same period last year while none was sold during the Year.

LOSS/PROFIT BEFORE TAXATION

During the Year, loss before taxation of the Group amounted to approximately RMB129 million, compared to profit before taxation of approximately RMB656 million the same period last year. The decrease was mainly attributable to the decrease in gross profit.

INCOME TAX CREDIT/EXPENSES

During the Year, the Group's income tax credit amounted to approximately RMB7 million, as compared to income tax expenses of approximately RMB116 million the same period last year. The decrease was mainly attributable to the decrease in profit before taxation. In addition, the equity-settled share based payment expenses of RMB35 million (2008: RMB38 million) and amortisation expenses of intangible assets amounted to RMB37 million (2008: RMB12 million) were not deductible from income tax calculation during the Year.

LOSS/PROFIT FOR THE YEAR

During the Year, the Group's loss amounted to approximately RMB122 million, as compared to profit of approximately RMB540 million the same period last year. Among which, loss attributable to equity shareholders of the Company was approximately RMB127 million, while earnings attributable to minority interests was approximately RMB5 million. Net loss margin amounted to approximately 6.5%, as compared to net profit margin of approximately 10.8% the same period last year. This was mainly attributable to a lower gross margin and a higher proportion of general and administrative expenses as well as selling expenses as compared to the same period last year.

EBITDA AND EBITDA MARGIN

During the Year, EBITDA amounted to approximately RMB-43 million, as compared to that of approximately RMB791 million in the same period last year. The decrease was mainly due to the sharp decrease in gross profit. The EBITDA margin was -2.2%, as compared to 16.7% in the same period last year. The decrease was mainly attributable to a lower gross margin and a higher proportion of general and administrative expenses as well as selling expenses as compared to the same period last year.

DIVIDEND

During the Year, the Group has paid the final dividends of HK$0.06 per Share for the year ended 2008 which were declared on 14 April 2009, which amounted to HK$193 million in total. For the year ended 31 December 2009, the Directors do not recommend the payment of dividend.

SOURCE OF CAPITAL AND BORROWINGS

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

At 31 December 2009, the Group's bank borrowings amounted to approximately RMB1,298 million, representing a decrease of approximately RMB277 million as compared to 31 December 2008. Among which, borrowings repayable within one year amounted to approximately RMB1,046 million, representing a decrease of RMB515 million as compared to 31 December 2008.

DEPOSIT AND CASH FLOW

At 31 December 2009, the Group's cash and cash equivalents amounted to approximately RMB1,603 million, representing an increase of approximately RMB136 million as compared to that at 31 December 2008. During the Year, the Group's operating cash inflow amounted to approximately RMB468 million, which was mainly due to the receipt of receivables and a reduction in pledged bank deposits; cash inflow from investing activities amounted to approximately RMB186 million as a result of the decrease of bank deposits maturing over 3 months of RMB455 million; and cash outflow from financing activities amounted to approximately RMB519 million which was mainly used to repay bank loans and dividends.

ASSETS STRUCTURE AND CHANGES THEREOF

At 31 December 2009, the Group's total assets amounted to approximately RMB6,589 million, representing a decrease of RMB1,195 million as compared to that at 31 December 2008. The decrease was mainly due to repayment of loans and the decrease of accounts payables and receipts in advance. Among which, current assets amounted to approximately RMB5,380 million, which were mainly cash and cash equivalents, trade receivables and inventories, accounting for 81.7% of total assets; non-current assets amounted to approximately RMB1,209 million, accounting for approximately 18.3% of total assets.

LIABILITIES

At 31 December 2009, the Group's total liabilities amounted to approximately RMB2,325 million, representing a decrease of approximately RMB931 million as compared to 31 December 2008. Among which, current liabilities amounted to approximately RMB2,062 million, accounting for approximately 88.7% of total liabilities; non-current liabilities amounted to approximately RMB263 million, accounting for approximately 11.3% of total liabilities, the increase as compared to 31 December 2008 was due to newly medium term loan of approximately RMB238 million during the year. At 31 December 2009, the Group's gearing ratio is approximately 35.3%.

TOTAL EQUITY

At 31 December 2009, total equity amounted to RMB4,264 million, representing a decrease of RMB263 million as compared to 31 December 2008. Total equity attributable to equity shareholders of the Company amounted to approximately RMB4,169 million, representing a decrease of RMB265 million as compared to 31 December 2008. Minority interests amounted approximately to RMB95 million, representing an increase of RMB2 million as compared to 31 December 2008. Net asset value reached approximately RMB1.32 per Share. During the Year, the Group's loss per Share was approximately RMB3.95 cents.

CONTINGENT LIABILITIES AND PLEDGE

Details of contingent liabilities are set out in Note 36 to the financial statements of 2009 annual report.

At 31 December 2009, the Group has pledged bank deposits of approximately RMB31 million, representing a decrease of approximately RMB228 million as compared to 31 December 2008, which was mainly attributable to better borrowing terms won over from banks.

CAPITAL EXPENDITURE, MAJOR INVESTMENT AND CAPITAL COMMITMENTS

During the Year, capital expenditure of the Group on infrastructure and technical improvements amounted to approximately RMB198 million, representing an increase of approximately RMB43 million as compared to the same period last year. This was mainly due to the increase of approximately RMB88 million of interests in leasehold land held for own use under operating leases as compared to the same period last year.

At 31 December 2009, the Group had capital commitments of approximately RMB1,983 million, which will be used for the construction of offshore equipment production base at Qidong City, Jiangsu Province, and for the expansion of the Group's business as well as its production capacity.

FOREIGN CURRENCY RISK

The Group owns certain foreign currency deposits. At 31 December 2009, the Group's foreign currency deposits were equivalent to approximately RMB129 million, trade receivables and other receivables in foreign currency were equivalent to approximately RMB695 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 proceeds in 2008, and the adjusted use of proceeds are as follows: as at 31 December 2009, proceeds of HK$1,275 million to be used for offshore project, of which HK$306 million has incurred; proceeds of HK$592 million to be used for potential acquisitions, none has incurred; proceeds of HK$354 million to be used for production capacity expansion and R&D expenses, of which HK$322 million has incurred; proceeds of HK$737 million to be used and has incurred as working capital and day to day expenses.

EMPLOYEE REMUNERATION AND BENEFITS

During the Year, the average number of the Group's employees was 3,600, representing an increase of 113 persons as compared with that the same period last year. The total remuneration and benefits amounted to approximately RMB280 million, representing an increase of approximately RMB2 million as compared to the same period last year. Due to the adverse effect of the financial crisis, the Group has adjusted the floating wages accordingly; employee's individual remuneration was based on his job duties, work performance and individual capability. The Group maintains a good corporate culture and a people-oriented principle, focuses on improving team cohesion and employees' morale, and strengthens its fundamental management and building up of working procedures through steady implementation of ERP projects, so as to gradually set up a sound human resources management system which conforms to the Group's business strategy.

EXECUTIVE DIRECTORS

Mr. Zhang Mi (張弭先生), aged 53, 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
(formerly known as Asia Harbour International Limited)	chairman, and chief executive officer	Since 8 September 2009
Sichuan Honghua Petroleum Equipment Co., Ltd.	chairman, and	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, and general manager	Since 8 June 2009
Shanghai Honghua Offshore Oil and 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 Shareholder Co. Ltd	director	Since 26 April 2007
Sichuan Hongcheng Business Trading Co., Ltd.	executive director	Since 16 April 2008
Sichuan Honglian Industrial Co., Ltd. (was dissolved on 11 March 2010)	executive director	Since 28 April 2008 Until 11 March 2010

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 43, 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 engineer by Sichuan Honghua Petroleum Equipment Co., Ltd..

In the early stages of Sichuan Honghua Petroleum Equipment Co., Ltd., 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 rig, 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 (formerly known as Asia Harbour International 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
Newco (H. K.) Limited	director	Since 22 June 2008
	chairman, and general manager	Since 22 September 2009
Alpha Advance Limited	director	Since 10 July 2009
Russia Honghua Co., Ltd	director	Since 26 June 2008
Egyptian Petroleum HH Rig Manufacturing Shareholder Co.	director	Since 7 August 2009
Honghua America, LLC	director	Since 10 October 2008

Mr. Liu Zhi (劉智先生), aged 46, has been an Executive Director of the Company since 26 May 2008. He is also a Vice-president of the Company. In 2008, Mr. Liu was in charge of management of quality department, technical centre of research of drilling equipment, materials supply department and sale department of Sichuan Honghua Petroleum Equipment. Co., Ltd.. Mr. Liu graduated from Southwest Petroleum University in 2003, with a Master 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 Rigs Manufacturing Shareholder Co.	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

NON-EXECUTIVE DIRECTORS

Mr. Xiang Qingsheng (相慶生先生), aged 63, has been a Non-executive Director of the Company since 18 January 2008. He was a director of Honghua Holdings Limited (formerly known as Asia Harbour International Limited) from March 2007 to 13 April 2010. He was a director of Sichuan Honghua Petroleum Equipment Co., Ltd., from July 2007 to 13 April 2010 and was a director of Honghua Offshore Oil & Gas Equipment (Jiangsu) Co., Ltd. from 8 June 2010 to 13 April 2010. Since 14 January 2010 he has been a director of Honghua (China) Investment Co, Ltd.. He has been the president of Qingdao Pacific Oceaneering Co., Ltd. Shenzhen Branch. From 2004 to May 2008, he was a director and general manager of China Ocean Oilfields Services (Hong Kong) Ltd. (COOS). From 2004 to April 2009, Mr. Xiang was a director of China Nanshan Development (Group) Incorporation, a vice-chairman of Nanhai West Oil Oilfield Service (Shen Zhen) Co., Ltd., and a director of CNOOC Insurance Limited. Mr. Xiang graduated at Sinkiang Karamay Petroleum School majoring in Oil Exploitation Geology in September 1968 and at Guangdong South China Normal University majoring in English in 1986. He obtained a senior economist qualification from CNOOC in 1997. Mr. Xiang resigned as a Non-executive Director of the Company with effect from 14 April 2010.

Mr. Huang Dongyang (黃東陽先生), aged 49, has been appointed as a Non-executive Director of the Company with effect from 14 April 2010. He has been a director of Honghua Holdings Limited (formerly known as Asia Harbour International Limited), Sichuan Honghua Petroleum Equipment Co., Ltd., and Honghua Offshore Oil & Gas Equipment (Jiangsu) Co., Ltd. respectively since 13 April 2010. Mr. Huang has been the managing director of China Ocean Oilfields Services (H.K.) Ltd. ("COOS") since March 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 degree of science in 1982. From March 1985 to July 1986, Mr. Huang further studied English Language in College of Foreign Languages at Sun Yat-Sen University. Mr. Huang has been a senior engineer since February 1995.

Mr. He Sean Xing (何欣先生), aged 45, has been a Non-executive Director of the Company since 18 January 2008. He was a director of Sichuan Honghua Petroleum Equipment Co., Ltd. from March 2007 to 13 April 2010. He was a director of Honghua Holdings Limited (formerly known as Asia Harbour International Limited) from 6 December 2006 to 13 April 2010. He was a director of Honghua Offshore oil and gas equipment (Jiangsu) Co., Ltd. from 8 June 2009 to 13 April 2010. He has been a director of Anshine International Group (incorporated in the Cayman Islands) since 10 September 2006. He has been a director of Informax Optical Technology Corporation since May 2002. He has been a director of eBIS Co., Ltd., since 28 May 2003. Mr. He graduated from Zhejiang University in 1985, with a Bachelor's degree in structural engineering, and in 1991 he received a Master's degree in engineering from Carleton University (Canada). In 1994, he earned an MBA from the Schulich School of Business, York University (Canada). In 1997, Mr. He qualified as an American Chartered Financial Analyst (CFA). Mr. He resigned as a Non-executive Director of the Company with effect from 14 April 2010.

Mr. Siegfried Meissner, aged 57, 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 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 47, 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 16 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 46, 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 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 and Focus Technology Co., Ltd. respectively. He is also an independent director, member of the audit committee and chairman of the remuneration of committee of China Vanke Co., Ltd. He is directly involved in the formulation of accounting policies and audit processes.

Mr. Tai Kwok Leung, Alexander (戴國良先生), aged 52, 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 accountancy, corporate finance and investment experience in Hong Kong and overseas. Mr. Tai is a shareholder and an executive director of 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.

Mr. Liu Yinchun (劉銀春先生), aged 63, has been an Independent Non-executive Director of the Company since 18 January 2008. Mr Liu served as director of East China Oil Bureau from 2002 to 2007. Mr. Liu graduated from Beijing Geosciences College (now known as China University of Geosciences) in 1969. He has extensive experience in oil drilling and business management. In 1997, he served as the deputy director and Chief Engineer of East China Oil and Geology Bureau from 1996 to 2002. He was awarded Senior Engineer at professor level and has been receiving special subsidies granted by the State Council of the PRC government (政府特殊津貼) since February 1998, for his significant contribution to the development of engineering technology in China. Mr. Liu Yinchun resigned as an Independent Non-executive Director of the Company with effect from 14 April 2010.

Mr. Chen Guoming (陳國明先生), aged 47, 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 promoted to Associate Professor and then 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 promoted to 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 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. Wang Li (王礫先生), aged 39, has been an Independent Non-executive Director of the Company since 18 January 2008. 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 Lawyer Partner of Guangdong Jindi Law Firm Sichuan Office.

Mr. Shi Xingquan (史興全先生), aged 67, 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.

SENIOR MANAGEMENT

Mr. Luo Qiping (羅啓平先生), aged 46, has been a Vice-president of the Company since 18 January 2008. He has been a deputy general manager of Sichuan Honghua Petroleum Equipment Co., Ltd. since June 2007. He was a director of Honghua International Co., Ltd. from 13 January 2004 to 19 May 2008. From 1989 to 1993, he studied at the No. 2 Heavy Machinery Plant Vocational University (now "Sichuan college of Architectural Technology") majoring in machinery manufacture and design, and obtained an engineering qualification from the Personnel Bureau of Sichuan Province, in September 1997. He joined Sichuan Honghua Petroleum Equipment Co., Ltd. as an engineer in 1999. Prior to joining Sichuan Honghua Petroleum Equipment Co., Ltd., he worked as an assistant engineer and then an engineer in Dongfang Petro Chemical General Equipment Factory (東方石化通用設備總廠) from 1982 to 1999. Mr. Luo has extensive experience in production management. He passed an examination in ISO9000:2000 Quality Management System Requirements and Internal Auditing Skills in April 2001 and awarded by Det Norske Veritas ("DNV") certificate of training. Mr. Luo Qiping resigned as a Vice-president of the Company with effect from 18 Januray 2010.

Mr. Zhao Ping (趙平先生), aged 53, has been a Vice-president of the Company since 27 April 2008. He has respectively been a director and general manager of Sichuan Honghua Petroleum Equipment Co., Ltd. since 18 January 2010. 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 Youxin Company. From 1972 to 1999, Mr Zhao worked in South-Sichuan Mining Area of Sichuan Petroleum Bureau. He was the head of Quality Management Office from 1993, and director of Workshop No. 1 from 1994 to 1996, and was the deputy factory director. 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 54, 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 since 1st August 2009. 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 manager and director of Luzhou Huayou Compressed Gas Co., Ltd. from 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 (劉剛强先生), aged 40, 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 Sichuan Honghua Petroleum Equipment Co., Ltd. since March 2004. 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 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.

Ms. Lu Hong (魯紅女士), aged 40, was appointed financial controller of Sichuan Honghua Petroleum Equipment Co., Ltd. in May 2007, and has been the financial controller and the qualified accountant of the Company since June 2007. She is the chief financial officer of Honghua Holdings Limited since 8 September 2009. Before 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 43, has been a human resources officer of the Company since 18 January 2010. Mr. Chen became Human Resource department director of the Company in January 2008. In October 2003, Mr. Chen joined in Sichuan Honghua Petroleum Equipment Co., Ltd. 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 42, 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.

The Board presents this Corporate Governance Report in the Group's annual report for the year ended 31 December 2009.

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 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 set out in the CG Code throughout the year ended 31 December 2009, 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 performances. The senior management was delegated the authority and responsibilities 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 set out in their terms of reference.

All Directors have carried out their duties in good faith and 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 members comprising Independent Non-executive Directors.

The Board comprises the following Directors:

Executive Directors:

Zhang Mi	*(Chairman and President (Chief Executive Officer, "CEO"), Member of Remuneration Committee and Chairman of Strategic Investment and Risk Control 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	
Xiang Qingsheng	*(Member of Strategic Investment and Risk Control Committee) (Resigned with effect from 14 April 2010)*
He Sean Xing	*(Chairman of Remuneration Committee and Member of Strategic Investment and Risk Control Committee) (Resigned with effect from 14 April 2010)*
Huang Dongyang	*(Member of Strategic Investment and Risk Control Committee) (Appointed with effect from 14 April 2010)*

Independent Non-executive Directors:

Qi Daqing	*(Chairman of Audit Committee and member of Remuneration Committee and Corporate Governance Committee)*
Liu Xiaofeng	*(Member of Audit Committee and Chairman of Corporate Governance Committee)* *(Appointed with effect from 14 April 2010 as Chairman of Remuneration Committee)*
Chen Guoming	*(Member of Audit Committee and Corporate Governance Committee)*
Liu Yinchun	*(Member of Audit Committee and Corporate Governance Committee)* *(Resigned with effect from 14 April 2010)*
Wang Li	*(Member of Audit Committee, Corporate Governance Committee and Strategic Investment and Risk Control Committee)*
Tai Kwok Leung Alexander	*(Member of Audit Committee and Corporate Governance Committee)*
Wang Chunlin	*(Member of Audit Committee and Corporate Governance Committee)* *(Resigned with effect from 13 February 2009)*
Shi Xingquan	*(Member of Audit Committee and Corporate Governance Committee)* *(Appointed with effect from 14 April 2009)*

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

During the year ended 31 December 2009, 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 judgment 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 and Strategic Investment and Risk Control 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 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.

In accordance with the Company's Articles of Association, all Directors of the Company 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 Board reviews 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 shall 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.

Mr. Shi Xingquan, having been appointed as Independent Non-executive Director of the Company during the year, has retired and being eligible, offered himself for re-election at the annual general meeting of the Company held on 3 June 2009.

At 2010 annual general meeting, Mr. Ren Jie, Mr. Siegfried Meissner, Mr. Huang Dongyang, Mr. Liu Xiaofeng and Mr. Tai Kwok Leung, Alexander will retire by rotation and being eligible, offer themselves for re-election.

The Board recommended the re-appointment of the Directors standing for re-election at the 2010 annual general meeting of the Company.

The Company's circular for the 2010 annual general meeting shall contain detailed information of the Directors standing for re-election.

TRAINING, INDUCTION AND CONTINUING DEVELOPMENT FOR 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 regulatory 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 whenever 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.

Notices of regular Board meetings are served on 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 the 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 2009, 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 Remuneration Committee, the Audit Committee, the Corporate Governance Committee and the Strategic Investment and Risk Control Committee during the year ended 31 December 2009 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	08/08	–	01/01	–	02/02
Ren Jie	08/08	–	–	–	02/02
Liu Zhi	07/08	–	–	–	01/02
He Sean Xing	06/08	–	01/01	–	02/02
Siegfried Meissner	04/08	–	–	–	–
Xiang Qingsheng	08/08	–	–	–	02/02
Chen Guoming	08/08	02/02	–	02/02	–
Liu Xiaofeng	08/08	02/02	–	02/02	–
Liu Yinchun	07/08	02/02	–	02/02	–
Qi Daqing	07/08	02/02	01/01	01/02	–
Tai Kwok Leung, Alexander	05/08	02/02	–	0/02	–
Wang Li	08/08	02/02	–	01/02	02/02
Shi Xingquan *(appointed with effect from 14 April 2009)*	07/07	01/01	–	01/01	–
Wang Chunlin *(resigned with effect from 13 February 2009)*	01/01	0/00	–	0/00	–

MODEL CODE FOR SECURITIES TRANSACTIONS

The Company has adopted its own code of conduct regarding Directors' dealings in the Company's securities (the "Company's 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's Code throughout the year ended 31 December 2009.

The Company also has 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 incident 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 decisions 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 work tasks are periodically reviewed. Approval has to be obtained from the Board prior to any significant transactions entered into by the abovementioned officers.

The Board has established 4 committees, namely, the Remuneration Committee, the Audit Committee, the Corporate Governance Committee and the Strategic Investment and Risk Control Committee for overseeing particular aspects of the Company's affairs. Most of the 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 Chief Executive Officer and the senior management to discharge its responsibilities.

REMUNERATION OF DIRECTORS AND SENIOR MANAGEMENT

REMUNERATION COMMITTEE

The Remuneration Committee comprises 3 members, namely, Liu Xiaofeng (Chairman) (who has been appointed to replace He Sean Xing who has resigned with effect from 14 April 2010), Zhang Mi and Qi Daqing, the majority of them are Non-executive Directors.

The primary objectives of the Remuneration Committee include:

- 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 on 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 2009 and the attendance records are set out under "Directors' Attendance Records" on page 34.

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 2009.

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, Chen Guoming, Wang Li, Tai Kwok Leung, Alexander and Shi Xingquan (who has been appointed with effect from 14 April 2009 to replace Wang Chunlin who has resigned with effect from 13 February 2009), including 3 Independent Non-executive Directors who possess the appropriate professional qualifications or accounting or related financial management expertise. Liu Yinchun was also a member of the Audit Committee and has resigned with effect from 14 April 2010.

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 2009, the financial reporting and compliance procedures, the report from the management on the Company's internal control and risk management review and processes and the re-appointment of the external auditors.

The Audit Committee held two meetings during the year ended 31 December 2009 and the attendance records are set out under "Directors' Attendance Records" on page 34.

CORPORATE GOVERNANCE COMMITTEE

The Corporate Governance Committee comprises all the six Independent Non-executive Directors, namely Liu Xiaofeng (Chairman), Qi Daqing, Chen Guoming, Wang Li, Tai Kwok Leung, Alexander and Shi Xingquan (who has been appointed with effect from 14 April 2009 to replace Wang Chunlin who has resigned with effect from 13 February 2009). Liu Yinchun was a member of the Corporate Governance Committee and has resigned with effect from 14 April 2010.

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 2009 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 was formed by Zhang Mi (Chairman), Liu Zhi, Ren Jie, Huang Dongyang (appointed with effect from 14 April 2010) and Wang Li. He Sean Xing and Xiang Qingsheng were members of the Strategic Investment and Risk Control Committee and have resigned with effect from 14 April 2010.

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 two meetings during the year ended 31 December 2009 and the attendance records are set out under "Directors' Attendance Records" on page 34.

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 page 59.

During the year ended 31 December 2009, the remuneration paid to the Company's auditors, Messrs. KPMG, is set out below:

Category of Services	Fees Paid/ Payable (in HK Dollars)
Audit Services	2,400,000
Non-audit Services	
— Reviewing interim financial information	600,000
— Proceeding of continuing connected transactions	50,000
Total	3,050,000

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 and the Corporate Governance Committee or, in their absence, other members of the respective committees normally attend the annual general meetings and other relevant Shareholders' meetings to answer questions at Shareholders' meetings.

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 the 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' meetings.

The Board presents this annual report, together with the audited consolidated financial statements of the Group for the year ended 31 December 2009.

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 the offshore drilling module. Meanwhile it also provides technical support services and drilling engineering services 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 2009 are set out in the Financial Statements on pages 61 to 140 of this annual report.

The Board recommended no payment of final dividends for the year ended 31 December 2009.

SHARE CAPITAL

Changes in the share capital of the Company during the year are set out in Note 29 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 2009.

RESERVES

As of 31 December 2009, the Group has a total of approximately RMB3,869 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 subsidiaries as of 31 December 2009 are set out in Note 16 to the Financial Statements.

SIGNIFICATE 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]	(Chairman)
Mr. Ren Jie[4]	(Appointed on 18 January 2008)
Mr. Liu Zhi[4]	(Appointed on 26 May 2008)

Non-Executive Directors

Mr. He Sean Xing[2, 4]	(Appointed on 18 January 2008 and resigned with effect from 14 April 2010)
Mr. Xiang Qingsheng[4]	(Appointed on 18 January 2008 and resigned with effect from 14 April 2010)
Mr. Siegfried Meissner	(Appointed on 26 May 2008)
Mr. Huang Dongyang[4]	(Appointed with effect from 14 April 2010)

Independent Non-Executive Directors

Mr. Qi Daqing[1, 2, 3]	(Appointed on 18 January 2008)
Mr. Liu Xiaofeng[1, 2, 3, 5]	(Appointed on 18 January 2008)
Mr. Chen Guoming[1, 3]	(Appointed on 18 January 2008)
Mr. Liu Yinchun[1, 3]	(Appointed on 18 January 2008 and resigned with effect from 14 April 2010)
Mr. Wang Li[1, 3, 4]	(Appointed on 18 January 2008)
Mr. Tai Kwok Leung, Alexander[1, 3]	(Appointed on 18 January 2008)
Mr. Shi Xingquan[1, 3]	(Appointed on 14 April 2009)
Mr. Wang Chunlin[1, 3]	(Appointed on 18 January 2008 and resigned on 13 February 2009)

Notes:

1. Audit Committee Members
2. Remuneration Committee Members
3. Corporate Governance Committee Members
4. Strategic Investment and Risk Control Committee Members
5. Mr. Liu Xiaofeng has been appointed as the chairman of Remuneration Committee of the Company with effect from 14 April 2010

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. Huang Dongyang, Mr. Liu Xiaofeng and Mr. Tai Kwok Leung, Alexander 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 following "Continuing connected transactions", 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 2009, details of remuneration for the Directors and Senior Management are set out in Notes 9 and 10 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 2009, 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 for Securities Transactions by Directors of Listed Issuers (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	1,625,824,837[(1)(4)]	50.44%
Mr. Ren Jie	Long	Personal interest, corporate interest and settlor of a discretionary trust	1,625,824,837[(2)(4)]	50.44%
Mr. Liu Zhi	Long	Corporate interest and settlor of a discretionary trust	1,625,824,837[(3)(4)]	50.44%

(1) Zhang Mi individually owns 280,000 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 1,617,727,837 Shares. The Trustee of The ZYL Family Trust owns 3,000,000 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 1,000,000 Shares. The Trustee of a discretionary trust, The LZWM Family Trust, whose settlor is Liu Zhi, another member of the Concert Group, owns 1,070,000 Shares. The Trustee of a discretionary trust, The FBX Family Trust, whose settlor is Fan Bing, another member of the Concert Group, owns 693,000 Shares. The other members of the Concert Group collectively own 1,885,000 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 1,617,727,837 Shares. The Trustee of The RJDJ Victory Trust owns 1,000,000 Shares.

Zhang Mi, another member of the Concert Group and the settlor of a discretionary trust, The ZYL Family Trust, individually owns 280,000 Shares. The Trustee of The ZYL Family Trust owns 3,000,000 Shares. The Trustee of a discretionary trust, The LZWM Family Trust, whose settlor is Liu Zhi, another member of the Concert Group, owns 1,070,000 Shares. The Trustee of a discretionary trust, The FBX Family Trust, whose settlor is Fan Bing, another member of the Concert Group, owns 693,000 Shares. The other members of the Concert Group collectively own 1,885,000 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 1,617,727,837 Shares. The Trustee of The LZWM Family Trust owns 1,070,000 Shares.

Zhang Mi and Ren Jie, the other two members of the Concert Group, collectively hold 449,000 Shares. The Trustees of the two discretionary trusts, whose settlors are Zhang Mi and Ren Jie respectively, collectively own 4,000,000 Shares. The Trustee of a discretionary trust, The FBX Family Trust, whose settlor is Fan Bing, another member of the Concert Group, owns 693,000 Shares. The other members of the Concert Group collectively own 1,885,000 Shares.

(4) The Concert Group is defined is 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	1,000,000	—
Mr. Liu Xiaofeng	Long	1,000,000	—
Mr. Tai Kwok Leung, Alexander	Long	850,000	—
Mr. Chen Guoming	Long	750,000	—
Mr. Liu Yinchun	Long	750,000	—
Mr. Wang Li	Long	750,000	—
Mr. Shi Xingquan	Long	750,000	—

Saved as disclosed above, on 31 December 2009, 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 2009, 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						
Name	Long/Short Position	Personal 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
		Share option	Shares Interest					
Ally Giant Limited	Long	–	1,617,727,837	–	–	48,287,000	1,666,014,837[1]	51.69%
Ample Chance International Limited	Long	–	–	1,617,727,837	–	48,287,000	1,666,014,837[2]	51.69%
Wealth Afflux Limited	Long	–		1,617,727,837	–	48,287,000	1,666,014,837[3]	51.69%
Ally Smooth Investments Limited	Long	–	–	1,617,727,837	–	48,287,000	1,666,014,837[3]	51.69%
Equity Trustee Limited	Long	–	–	–	1,623,490,837	–	1,623,490,837 [3][5][6][9][10][14][20][22]	50.37%
Charm Moral International Limited	Long	–	–	1,617,727,837	–	48,287,000	1,666,014,837[4]	51.69%
Mowbray Worldwide Limited	Long	–	–	1,617,727,837	–	48,287,000	1,666,014,837[5]	51.69%
Ecotech Enterprises Corporation	Long	–	–	1,617,727,837	–	48,287,000	1,666,014,837[6]	51.69%
Mr. Zheng Yong	Long	2,085,000	–	1,617,727,837	–	46,202,000	1,666,014,837[7]	51.69%
Beauty Clear Holdings Limited	Long	–	–	1,617,727,837	–	48,287,000	1,666,014,837[8]	51.69%
Mr. Zuo Huixian	Long	1,734,000	–	–	1,617,727,837	46,553,000	1,666,014,837[9]	51.69%
Vast & Fast Corporation	Long	–	–	1,617,727,837	–	48,287,000	1,666,014,837[9]	51.69%
Mr. Zhang Xu	Long	1,833,000	–	–	1,617,727,837	46,454,000	1,666,014,837[10]	51.69%
Cavendish Global Corporation	Long	–	–	1,617,727,837	–	48,287,000	1,666,014,837[10]	51.69%
Elegant Scene International Limited	Long	–	–	1,617,727,837	–	48,287,000	1,666,014,837[11]	51.69%
Mr. Wang Jiangyang	Long	941,000	1,785,000	1,617,727,837	–	45,561,000	1,666,014,837[11]	51.69%
Mr. Chen Jun	Long	872,000	–	1,617,727,837	–	47,415,000	1,666,014,837[12]	51.69%
Believe Power International Limited	Long	–	–	1,617,727,837	–	48,287,000	1,666,014,837[13]	51.69%
Mr. Fan Bing	Long	1,744,000	–	–	1,618,420,837	45,850,000	1,666,014,837[14]	51.69%
Brondesbury Enterprises Limited	Long	–	–	1,617,727,837	–	48,287,000	1,666,014,837[14]	51.69%
Mr. Zhang Yanyong	Long	1,480,000	100,000	1,617,727,837	–	46,707,000	1,666,014,837[15]	51.69%
Mr. Ao Pei	Long	683,000	–	1,617,727,837	–	47,604,000	1,666,014,837[16]	51.69%
Mr. Tian Diyong	Long	550,000	–	1,617,727,837	–	47,737,000	1,666,014,837[17]	51.69%
Mr. Shen Dingjian	Long	262,000	–	1,617,727,837	–	48,025,000	1,666,014,837[18]	51.69%
Benefit Way International Limited	Long	–	–	1,617,727,837	–	48,287,000	1,666,014,837[19]	51.69%
Mr. Liu Xuetian (deceased)	Long	–	–	–	1,617,727,837	48,287,000	1,666,014,837[20]	51.69%
Dobson Global Inc.	Long	–	–	1,617,727,837	–	48,287,000	1,666,014,837[20]	51.69%
Ms. Qu Yihong	Long	–	–	1,617,727,837	–	48,287,000	1,666,014,837[21]	51.69%
Ms. Liu Ying	Long	–	–	1,617,727,837	–	48,287,000	1,666,014,837[21]	51.69%
Mr. Zhou Bing	Long	1,445,000	–	–	1,617,727,837	46,842,000	1,666,014,837[22]	51.69%
Darius Enterprises Limited	Long	–	–	1,617,727,837	–	48,287,000	1,666,014,837[22]	51.69%
Ms. Lv Lan	Long	519,000	–	1,617,727,837	–	47,768,000	1,666,014,837[23]	51.69%
Mr. Tian Yu	Long	515,000	–	1,617,727,837	–	47,772,000	1,666,014,837[24]	51.69%

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. Li Hanqiang	Long	345,000	–	1,617,727,837	–	47,942,000	1,666,014,837[25]	51.69%
Mr. Liu Yingguo	Long	242,000	–	1,617,727,837	–	48,045,000	1,666,014,837[26]	51.69%
Ms. Liu Lulu	Long	243,000	–	1,617,727,837	–	48,044,000	1,666,014,837[27]	51.69%
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%

(1) Ally Giant Limited is wholly-owned by Ample Chance International Limited and holds 1,617,727,837 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 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 Wang Jiangyang, approximately 5.10% by Chen Jun, and a total of approximately 42.74% by 3 other shareholders.

(9) Approximately 23.63% of the 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 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 Lu Lan, approximately 3.91% by Tian Yu, approximately 3.50% by Li Hanqiang, approximately 1.52% by Liu Yingguo, 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 1,617,727,837 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 the 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 the 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 the issued share capital of Ample Chance International Limited. Li Hanqiang is a member of the Concert Group.

(26) Liu Yingguo 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 the 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 the 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 98.8% by China National Offshore Oil Corporation and approximately 1.2% by Overseas Oil & Gas Corporation Limited.

(29) Nabors Drilling International II Limited holds 450,000,000 Shares. The entire issued share capital of Nabors Drilling International II Limited was owned by Nabors International Management Limited. Nabors International Management Limited is wholly owned by 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 Cayman II, L. P., which in turn is holding subsidiaries that hold 166,841,887 Shares.

Save as disclosed above, to the best of the Directors and the Chief Executives of the Company's knowledge, as at 31 December 2009, 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 2009, none of the grantees has exercised the share options granted to him under the Pre-IPO share option scheme and 671,000 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 dated of grant. As at 31 December 2009, 40% of the total number of the share options granted or 24,000,000 (if not cancelled) 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.

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 despatch a circular to Shareholders, containing identity of the participants, numbers of share options to be granted by the participant and related terms (and share options previously granted to this participant) and all other data as required by the Listing Rules. The numbers and terms of the share options to be granted to this participant (including exercise price) must be determined before approval by the Shareholder. 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 subscribed 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 the Share Option Scheme.

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 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

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 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 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 effective and enforceable under the provisions of Share Option Scheme.

On 15 April 2009, options to subscribe for 60,000,000 Shares of HK$0.10 each were granted to the eligible participants at an exercise price of HK$1.27 per Share under the Share Option Scheme adopted by resolutions in writing of all the Shareholders on 21 January 2008. 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 2019. The valid period of the Share Option Scheme is up to 14 April 2019. Particulars and movements of share options under the Share Option Scheme during the year ended 31 December 2009 were as follows:

NUMBER OF SHARE OPTIONS

Name or category of participant	Outstanding as at 1 January 2009	Granted during the year ended 31 December 2009	Exercised during the year ended 31 December 2009	Lapsed during the year ended 31 December 2009	Cancelled during the year ended 31 December 2009	Outstanding as at 31 December 2009	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
Mr. Liu Xiaofeng	–	1,000,000	–	–	–	1,000,000	15/04/2009	01/12/2009–14/04/2019	1.27	1.29
Mr. Liu Yinchun	–	750,000	–	–	–	750,000	15/04/2009	01/12/2009–14/04/2019	1.27	1.29
Mr. Qi Daqing	–	1,000,000	–	–	–	1,000,000	15/04/2009	01/12/2009–14/04/2019	1.27	1.29
Mr. Tai Kwok Leung, Alexander	–	850,000	–	–	–	850,000	15/04/2009	01/12/2009–14/04/2019	1.27	1.29
Mr. Wang Li	–	750,000	–	–	–	750,000	15/04/2009	01/12/2009–14/04/2019	1.27	1.29
Mr. Shi Xingquan	–	750,000	–	–	–	750,000	15/04/2009	01/12/2009–14/04/2019	1.27	1.29
Sub-total	–	14,747,000	–	–	–	14,747,000				
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 Di Yong	–	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										
Employees	–	39,536,000	531,100	177,600	–	38,827,300	15/04/2009	01/12/2009–14/04/2019	1.27	1.29
Sub-total	–	39,536,000	531,000	177,600	–	38,827,300				
Total	–	60,000,000	531,100	177,600	–	59,291,300				

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, waivers from strict compliance under Rule 14A.42(3) of the Listing Rules have been granted by the Stock Exchange in relation to the Existing Purchase Framework Agreement (as defined below) and 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 and its subsidiaries. Nabors Group, through Nabors International, 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 entered into a sales framework agreement dated 31 August 2008 (the "Sales Framework Agreement") with Nabors Industries with a term commencing from 31 August 2008 and ending on 31 December 2010 or when the Nabors Group and its associates ceased to be connected persons of the Company (whichever is the earlier). Pursuant to the Sales Framework Agreement, the Group shall sell to the Nabors Group certain types of drilling rigs and workover rigs from 450HP to 3,000HP and their parts and components, and similar products to be developed in line with the future market needs, and provision by the Group to the Nabors Group of the after-sales services. The approved annual caps of the Products and Services (as defined in the Sales Framework Agreement) shall not exceed US$200 million, US$250 million and US$300 million for each of the three years ending 31 December 2010 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 after-sales services amounted to approximately RMB138,566,266.

2. PURCHASES FRAMEWORK AGREEMENT ENTERED INTO WITH NABORS GROUP

In order to expand the business with the Nabors Group, the Company entered into a purchases framework agreement dated 31 August 2008 (the "Purchases Framework Agreement") with Nabors Industries with a term commencing from 31 August 2008 and ending on 31 December 2010 or when the Nabors Group and its associates ceased to be connected persons of the Company (whichever is the earlier). Pursuant to the 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 Purchases Framework Agreement) shall not exceed US$20 million, US$40 million and US$40 million for each of the three years ending 31 December 2010 respectively.

During the year, the total purchases of the Products and Services made by the Group from the Nabors Group amounted to approximately RMB662,661.

3. PURCHASE FRAMEWORK AGREEMENT ENTERED INTO WITH HONGTAI 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 dated 15 February 2008 (the "Existing Purchase Framework Agreement") with Hongtai Company for a term commencing from 1 January 2007 and ending on 31 December 2009. Pursuant to the Existing Purchase Framework Agreement, the Group shall purchase paint, tools, welding materials and worker-protection items from Hongtai Company. It is excepted that the maximum aggregate annual purchase price payable by the Group to Hongtai Company shall not exceed RMB50 million, RMB30 million and RMB30 million for each of the three years ended 31 December 2009.

During the year, the total purchases made by the Group from Hongtai Company amounted to approximately RMB14,019,110.

In view of the forthcoming expiry of the Existing Purchase Framework Agreement, Honghua Company and Hongtai Company entered into a renewal purchase framework agreement on 16 December 2009 (the "Renewal Purchase Framework Agreement") for a further term of three years commencing from 1 January 2010 and expiring on 31 December 2012. Pursuant to the Renewal Purchase Framework Agreement, Honghua Company shall purchase low value consumables, auxiliary accessories, tools, welding materials and worker-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 Purchase Framework Agreement shall not exceed RMB28 million, RMB26 million and RMB26 million for each of the three financial years ending 31 December 2012 respectively. Announcement was published on 16 December 2009 regarding the continuing connected transactions contemplated under the Renewal Purchase Framework Agreement in accordance with the Listing Rules.

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 interests of the Shareholders as a whole.

The auditor has confirmed that the above continuing connected transactions:

(1) have been approved by the Board;

(2) are in accordance with the pricing policies of the Group;

(3) are entered into in accordance with the terms of the relevant agreements governing such transactions; and

(4) have not exceeded their respective caps as set out respectively in the prospectus of the Company dated 25 February 2008 and the previous announcement.

BANK LOANS

Details of our bank loans and other borrowings are set out in Note 22 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 the economic and financial situations, and the resources price including land and steel have dropped significantly, 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 the Global Offering (the details are set out in the announcement published on 26 November 2008). Therefore, as of 31 December 2009, the intended use of the net proceeds and the usage status are as follows:

(1) Proceeds of around 43% 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 & coastlines of Shanghai or the nearby province, investment in R&D of new equipments and construction of new factory buildings. This part of fund is around HK$1,275 million, out of which HK$306 million has been utilised and HK$969 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, out of which HK$322 million has been utilised and HK$32 million is retained.

(3) Proceeds of around 20% is to be used for acquisition and setting up joint venture and strategic partnership with international companion. This part of fund of approximately HK$592 million has not been utilised.

(4) Remaining proceeds of HK$737 million is to be used for working capital and current expenditure and the whole sum of HK$737 million has been utilised.

As of 31 December 2009, we 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 7(b) & 24 to the Financial Statements.

FIXED ASSETS

Details of the changes of the fixed assets of the Group are set out in Note 13 to the Financial Statements.

MAJOR CUSTOMERS AND SUPPLIERS

1. During the Year, the Group’s five largest customers accounted for approximately 73.6% of revenue and the largest customer was Hebei Haihua Energy Development Group Co., Ltd., accounting for approximately 28.7% of revenue. The others in descending proportions were Kuwait Drilling Company, Petroleum Equipment Supplies & NV, and Burgan Co. for Well Drilling, Trading and Maint. KSCC and Nabors Drilling Int’l, Ltd, accounting for approximately 21.2%, 9.0%, 8.2% and 6.5% respectively.

2. During the Year, the Group’s five largest suppliers in total accounted for approximately 37.6% of total purchase, and the largest suppliers was National Oilwell Varco, accounting for approximately 12.7% of total purchase. The others in descending proportions were Chengdu Zhongyeda Co., Ltd., Caterpillar S.A.R.L, Singapore Branch, Grand Rig International Limited and Chongqing Iron & Steel Company Limited, accounting for approximately 9.1%, 6.4%, 6.3% and 3.1% 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 2009, 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 8 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 latest practical date before the issue 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 annual general meeting of the Company.

QUALIFIED ACCOUNTANT

The Company engages a qualified accountant who is responsible for supervising the financial reporting procedures and internal control of the Company.

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

Hong Kong, 13 April 2010

KPMG

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") set out on pages 61 to 140, which comprise the consolidated and company balance sheets as at 31 December 2009, 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 notes.

DIRECTORS' RESPONSIBILITY FOR THE FINANCIAL STATEMENTS

The directors of the company are responsible for the preparation and the true and fair presentation of these financial statements in accordance with International Financial Reporting Standards issued by the International Accounting Standards Board and the disclosure requirements of the Hong Kong Companies Ordinance. This responsibility includes designing, implementing and maintaining internal control relevant to the preparation and the true and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

AUDITOR'S RESPONSIBILITY

Our responsibility is to express an opinion on these 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 as to whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and true and fair presentation of the financial statements 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 financial statements.

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

INDEPENDENT AUDITOR'S REPORT

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 2009 and of the group's loss 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

13 April 2010

CONSOLIDATED INCOME STATEMENT

For the year ended 31 December 2009 (Expressed in Renminbi)

	Note	2009 RMB'000	2008 RMB'000
Revenue	5	**1,961,517**	4,737,532
Cost of sales		**(1,443,455)**	(3,381,730)
Gross profit		**518,062**	1,355,802
Other operating revenue	6	**7,085**	5,375
Other operating expenses		**(803)**	(6,970)
Selling expenses		**(179,980)**	(369,787)
General and administrative expenses		**(351,070)**	(263,114)
(Impairment losses recognised)/impairment losses written-back on trade receivables	19(b)	**(123,264)**	1,907
Other net income	6	**9,234**	13,662
(Loss)/profit from operations		**(120,736)**	736,875
Finance income		**61,094**	52,023
Finance expenses		**(64,803)**	(140,724)
Net finance expenses	7(a)	**(3,709)**	(88,701)
Share of (loss)/profit from jointly controlled entities	17	**(4,766)**	7,332
(Loss)/profit before taxation	7	**(129,211)**	655,506
Income tax credit/(expenses)	8(a)	**7,126**	(115,560)
(Loss)/profit for the year		**(122,085)**	539,946
Attributable to:			
Equity shareholders of the company	11	**(127,337)**	511,974
Minority interests		**5,252**	27,972
(Loss)/profit for the year		**(122,085)**	539,946
(Loss)/earnings per share — Basic and diluted (RMB cents)	12		
Basic		**(3.95)**	16.22
Diluted		**(3.95)**	16.22

The notes on pages 69 to 140 form part of these financial statements.

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

For the year ended 31 December 2009 (Expressed in Renminbi)

	2009 RMB'000	2008 RMB'000
(Loss)/profit for the year	**(122,085)**	539,946
Other comprehensive income for the year:		
Exchange differences on translation of financial statements of operations outside the PRC	**(1,318)**	(87,360)
Total comprehensive income for the year	**(123,403)**	452,586
Attributable to:		
Equity shareholders of the company	**(128,655)**	424,614
Minority interests	**5,252**	27,972
Total comprehensive income for the year	**(123,403)**	452,586

The notes on pages 69 to 140 form part of these financial statements.

CONSOLIDATED BALANCE SHEET

At 31 December 2009 (Expressed in Renminbi)

	Note	2009 RMB'000	2008 RMB'000
Non-current assets			
Fixed assets			
— Property, plant and equipment	13	414,746	375,169
— Interests in leasehold land held for own use under operating leases	13	141,829	53,461
— Freehold land	13	5,504	5,509
		562,079	434,139
Deposits paid for acquisition of leasehold land		209,308	90,108
Construction in progress	14	59,144	40,369
Intangible assets	15	318,859	356,216
Interests in jointly controlled entities	17	10,309	9,604
Deferred tax assets	26(b)	49,372	16,044
Total non-current assets		1,209,071	946,480
Current assets			
Inventories	18	1,901,168	2,033,488
Trade and other receivables	19	1,246,351	2,045,069
Amounts due from related companies	32(b)	31,096	34,018
Amount due from immediate holding company	32(b)	6	8
Amount due from ultimate holding company	32(b)	6	42
Current tax recoverable	26(a)	24,393	—
Pledged bank deposits	20	30,663	259,099
Bank deposits maturing over 3 months		542,898	998,356
Cash and cash equivalents	21	1,603,316	1,467,363
Total current assets		5,379,897	6,837,443
Total assets		6,588,968	7,783,923
Current liabilities			
Interest-bearing borrowings	22	1,046,090	1,561,000
Amounts due to related companies	32(b)	5,609	21,376
Trade and other payables	23	974,024	1,540,729
Current tax payable	26(a)	20,933	77,079
Provision for product warranties	27	15,579	32,241
Total current liabilities		2,062,235	3,232,425

CONSOLIDATED BALANCE SHEET

At 31 December 2009 (Expressed in Renminbi)

	Note	2009 RMB'000	2008 RMB'000
Net current assets		**3,317,662**	3,605,018
Total assets less current liabilities		**4,526,733**	4,551,498
Non-current liabilities			
Interest-bearing borrowings	22	**252,390**	14,401
Deferred tax liabilities	26(b)	**10,414**	9,689
Total non-current liabilities		**262,804**	24,090
Total liabilities		**2,325,039**	3,256,515
Equity			
Share capital	29(c)	**299,542**	299,495
Reserves		**3,869,363**	4,134,887
Total equity attributable to equity shareholders of the company		**4,168,905**	4,434,382
Minority interests		**95,024**	93,026
Total equity		**4,263,929**	4,527,408
Total liabilities and equity		**6,588,968**	7,783,923

Approved and authorised for issue by the board of directors on 13 April 2010.

Zhang Mi
Director

Liu Zhi
Director

The notes on pages 69 to 140 form part of these financial statements.

BALANCE SHEET

At 31 December 2009 (Expressed in Renminbi)

	Note	2009 RMB'000	2008 RMB'000
Non-current assets			
Intangible assets	15	318,859	356,216
Investments in subsidiaries	16	2,687,023	2,691,301
Total non-current assets		3,005,882	3,047,517
Current assets			
Other receivables		501	84
Amounts due from related companies		49	16
Amount due from a subsidiary	28	40,645	8,086
Cash and cash equivalents	21	47,246	50,241
Total current assets		88,441	58,427
Total assets		3,094,323	3,105,944
Current liabilities			
Other payables	23	400	7,948
Total current liabilities		400	7,948
Net current assets		88,041	50,479
Total assets less current liabilities		3,093,923	3,097,996
Total liabilities		400	7,948
Equity	29(a)		
Share capital		299,542	299,495
Reserves		2,794,381	2,798,501
Total equity		3,093,923	3,097,996
Total liabilities and equity		3,094,323	3,105,944

Approved and authorised for issue by the board of directors on 13 April 2010.

Zhang Mi	**Liu Zhi**
Director	*Director*

The notes on pages 69 to 140 form part of these financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

For the year ended 31 December 2009 (Expressed in Renminbi)

		Attributable to equity shareholders of the company									
	Note	Share capital RMB'000 (note 29(c))	Share premium RMB'000 (note 29(d)(v))	Other reserve RMB'000 (note 29(d)(iii))	Capital reserve RMB'000 (note 29(d)(iv))	Surplus reserve RMB'000 (note 29(d)(i))	Exchange reserve RMB'000 (note 29(d)(ii))	Retained profits RMB'000	Sub-total RMB'000	Minority interests RMB'000	Total equity RMB'000
At 1 January 2009		299,495	2,508,202	59,358	436,796	199,490	(76,424)	1,007,465	4,434,382	93,026	4,527,408
Dividends approved in respect of the previous financial year	29(b)	–	(32,243)	–	–	–	–	(138,128)	(170,371)	–	(170,371)
Dividends to minority shareholders		–	–	–	–	–	–	–	–	(5,104)	(5,104)
Capital injection by minority shareholders		–	–	–	–	–	–	–	–	2	2
Acquisition of minority interests		–	–	(1,848)	–	–	–	–	(1,848)	1,848	–
Equity-settled share-based transactions	25	–	–	–	34,803	–	–	–	34,803	–	34,803
Shares issued under share option schemes	25	47	746	–	(199)	–	–	–	594	–	594
Options lapsed under share option schemes		–	–	–	(215)	–	–	215	–	–	–
Total comprehensive income for the year		–	–	–	–	–	(1,318)	(127,337)	(128,655)	5,252	(123,403)
Appropriation to surplus reserve		–	–	–	–	12,061	–	(12,061)	–	–	–
At 31 December 2009		299,542	2,476,705	57,510	471,185	211,551	(77,742)	730,154	4,168,905	95,024	4,263,929
At 1 January 2008		233,155	–	60,760	–	140,662	10,936	841,990	1,287,503	68,208	1,355,711
Shares issued under placing and public offering net of issuing expenses	29(c)(i)	76,077	2,623,896	–	–	–	–	–	2,699,973	–	2,699,973
Waiver of loan from immediate holding company		–	–	–	398,710	–	–	–	398,710	–	398,710
Dividends to minority shareholders		–	–	–	–	–	–	–	–	(4,556)	(4,556)
Special dividend declared and paid	29(b)	–	–	–	–	–	–	(287,671)	(287,671)	–	(287,671)
Repurchase of own shares	29(c)(ii)	(9,737)	(115,694)	–	–	–	–	–	(125,431)	–	(125,431)
Acquisition of minority interests		–	–	(1,402)	–	–	–	–	(1,402)	1,402	–
Equity-settled share-based transactions	25	–	–	–	38,086	–	–	–	38,086	–	38,086
Total comprehensive income for the year		–	–	–	–	–	(87,360)	511,974	424,614	27,972	452,586
Appropriation to surplus reserve		–	–	–	–	58,828	–	(58,828)	–	–	–
At 31 December 2008		299,495	2,508,202	59,358	436,796	199,490	(76,424)	1,007,465	4,434,382	93,026	4,527,408

The notes on pages 69 to 140 form part of these financial statements.

CONSOLIDATED CASH FLOW STATEMENT

For the year ended 31 December 2009 (Expressed in Renminbi)

	Note	2009 RMB'000	2008 RMB'000
Operating activities			
(Loss)/profit before taxation		**(129,211)**	655,506
Adjustments for:			
— Amortisation and depreciation			
— intangible assets		**36,821**	12,423
— assets held for use under operating leases		**1,394**	1,636
— other assets		**44,163**	32,475
— Realised gains on investments at fair value through profit or loss		**(59)**	(3,280)
— Interest income		**(36,664)**	(52,023)
— Interest expense		**59,199**	66,138
— Share of loss/(profit) from jointly controlled entities		**4,766**	(7,332)
— Loss on disposals of fixed assets		**990**	287
— Equity-settled share based payment expenses		**34,803**	38,086
— Impairment losses recognised/ (impairment losses written-back) on trade receivables		**123,264**	(1,907)
— Unrealised foreign exchange gain		**(656)**	(70,306)
Operating profit before change in working capital		**138,810**	671,703
Decrease/(increase) in inventories		**132,038**	(999,984)
Decrease/(increase) in trade and other receivables		**670,340**	(424,072)
Decrease in amounts due from related companies		**2,922**	6,780
Decrease/(increase) in amount due from immediate holding company		**2**	(8)
Decrease/(increase) in amount due from ultimate holding company		**36**	(42)
Decrease in pledged bank deposits		**228,436**	2,010
(Decrease)/increase in trade and other payables		**(565,910)**	422,624
Decrease in amounts due to related companies		**(15,767)**	(25,114)
(Decrease)/increase in provision for product warranties		**(16,662)**	11,462
Cash generated from/(used in) operations		**574,245**	(334,641)
Income tax paid		**(106,004)**	(70,287)
Net cash generated from/(used in) operating activities		**468,241**	(404,928)

CONSOLIDATED CASH FLOW STATEMENT

For the year ended 31 December 2009 (Expressed in Renminbi)

	Note	2009 RMB'000	2008 RMB'000
Investing activities			
Payment for addition of fixed assets (excluding interests in leasehold land)		(51,305)	(74,544)
Proceeds from disposals of fixed assets		4,745	3,159
Payment for construction in progress		(50,780)	(80,589)
Deposits paid for acquisition of leasehold land		(208,962)	(61,595)
Payment for leasehold land		—	(267)
Capital contribution to a jointly controlled entity		(5,157)	—
Interest received		42,281	39,893
Payment for purchase of investments at fair value through profit or loss		(210,000)	(359,680)
Proceeds from sale of investments at fair value through profit or loss		210,059	362,960
Decrease/(increase) in bank deposits maturing over 3 months		455,458	(998,356)
Net cash generated from/(used in) investing activities		186,339	(1,169,019)
Financing activities			
Proceeds from issue of shares, net of issuing expenses		—	2,699,973
Proceeds from new bank loans		1,454,141	1,798,051
Repayment of bank loans		(1,731,048)	(1,093,427)
Proceeds from shares issued under share option schemes		93	—
Payment for repurchase of shares		—	(125,431)
Repayment from shareholders loans		—	(76,850)
Dividends paid to equity shareholders of the company		(170,371)	(287,671)
Dividends paid to minority interests		(5,104)	(4,556)
Interest paid		(66,338)	(64,146)
Net cash (used in)/generated from financing activities		(518,627)	2,845,943
Net increase in cash and cash equivalents		135,953	1,271,996
Cash and cash equivalents at 1 January		1,467,363	195,367
Cash and cash equivalents at 31 December	21	1,603,316	1,467,363

During the year ended 31 December 2008, the immediate holding company of the company waived the loan to Honghua Holdings Limited ("Honghua Holdings") amounting to US$57,000,000 (equivalent to RMB398,710,000). The amount is recorded in "capital reserve".

The notes on pages 69 to 140 form part of these financial statements.

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 2009 comprise the company and its subsidiaries (collectively referred to as the "group") and the group's interests in jointly controlled entities.

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

(b) Basis of preparation of the financial statements

The financial statements are presented in Renminbi ("RMB"), rounded to the nearest thousand. 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 People's Republic of China (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 investments at fair value through profit or loss are stated at their fair value as explained in the accounting policy 2(e).

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

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

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.

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 37.

(c) Subsidiaries and minority 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 unrealised gains but only to the extent that there is no evidence of impairment.

Minority interests represent the portion of the net assets of subsidiaries attributable to interests that are not owned by the company, whether directly or indirectly through subsidiaries, 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. Minority interests are presented in the consolidated balance sheet within equity, separately from equity attributable to equity shareholders of the company. Minority 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 minority interests and the equity shareholders of the company.

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

(c) Subsidiaries and minority interests (continued)

Where losses applicable to the minority exceed the minority's interest in the equity of a subsidiary, the excess, and any further losses applicable to the minority, are charged against the group's interest except to the extent that the minority has a binding obligation to, and is able to, make additional investment to cover the losses. If the subsidiary subsequently reports profits, the group's interest is allocated all such profits until the minority's share of losses previously absorbed by the group has been recovered.

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

(d) Jointly controlled entities

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 a jointly controlled entity is accounted for in the consolidated financial statements under the equity method and is initially recorded at cost and adjusted thereafter for the post acquisition change in the group's share of the jointly controlled entity's net assets and any impairment loss relating to the investment (see note 2(k)). The group's share of the post-acquisition, post-tax results of the jointly controlled entity 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 jointly controlled entity's other comprehensive income is recognised in the consolidated statement of comprehensive income.

When the group's share of losses exceeds its interest in the 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 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 jointly controlled entity.

Unrealised profits and losses resulting from transactions between the group and its jointly controlled entities are eliminated to the extent of the group's interest in the 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.

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

(e) Investments at fair value through profit or loss

Investments at fair value through profit or loss are initially stated at cost, which is their transaction price unless fair value can be more reliably estimated using valuation techniques whose variables include only the data from observable markets. Investments at fair value through profit or loss are classified as current assets. Any attributable transaction costs are recognised in profit or loss as incurred. At each balance sheet date the fair value is remeasured, with any resultant gain or loss being recognised in profit or loss.

Investments are recognised/derecognised on the date the group/the company commits to purchase/sell the investments or they expire.

(f) Fixed assets and depreciation

Fixed assets are stated in the balance sheet at cost less accumulated depreciation and impairment losses (see note 2(k)).

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(v)).

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
— 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.

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

(g) 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(k)). 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.

(h) Intangible assets

Intangible assets represent the technology licences granted by the holding company and are stated in the balance sheet at cost less accumulated amortisation (where the estimated useful life is finite) and impairment losses (see note 2(k)).

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 of 10 years. Both the period and method of amortisation are reviewed annually.

(i) Leasehold land

Leasehold land represents cost of land use rights paid to the PRC's governmental authorities. Land use rights are carried at cost less accumulated amortisation and impairment loss (see note 2(k)). Amortisation is charged to profit or loss on a straight-line basis over the respective periods of the rights.

(j) Operating lease charges

Where the group has the use of assets 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)

(k) Impairment of assets

(i) Impairment of trade and other receivables and other financial assets

Trade and other current receivables and other financial assets carried at cost or amortised cost 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; and

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

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

— For investments in jointly controlled entities recognised using the equity method (see note 2(d)), the impairment loss is measured by comparing the recoverable amount of the investment as a whole with its carrying amount in accordance with note 2(k)(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(k)(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 financial assets carried at amortised cost 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)

(k) Impairment of assets (continued)

(i) Impairment of trade and other receivables and other financial assets (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.

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 amount previously written off directly are recognised in profit or loss.

(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;

— investments in subsidiaries; and

— deposits paid for acquisition of leasehold land.

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

(k) Impairment of assets (continued)

(ii) Impairment of other assets (continued)

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 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 other 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.

— 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.

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

(l) Inventories

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

Cost is calculated using the first-in first-out 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.

(m) Trade and other receivables

Trade and other receivables are initially recognised at fair value and thereafter stated at amortised cost less allowance for impairment of doubtful debts (see note 2(k)), 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.

(n) 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.

(o) 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.

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

(p) 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.

(q) 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 scheme 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.

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).

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

(r) 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 they 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.

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.

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

(r) Income tax (continued)

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.

(s) 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)

(t) 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 repairing services

Revenue is recognised when the service has been rendered.

(u) 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.

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

(u) Translation of foreign currencies (continued)

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 recognised 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.

(v) 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.

(w) Research and development

Research and development costs comprise all costs that are directly attributable to research and development activities or that can be allocated on a reasonable basis to such activities. Because of the nature of the group's research and development activities, no costs satisfy the criteria for the recognition of such costs as an asset. Research and development costs are therefore recognised as expenses in the period in which they are incurred.

(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

For the purposes of these financial statements, a party is considered to be related to the group if:

(i) the party has the ability, directly or indirectly through one or more intermediaries, to control the group or exercise significant influence over the group in making financial and operating policy decisions, or has joint control over the group;

(ii) the group and the party are subject to common control;

(iii) the party is an associate of the group or a joint venture in which the group is a venturer;

(iv) the party is a member of key management personnel of the group or the group's parent, or a close family member of such an individual, or is an entity under the control, joint control or significant influence of such individuals;

(v) the party is a close family member of a party referred to in (i) or is an entity under the control, joint control or significant influence of such individuals; or

(vi) the party is a post-employment benefit plan which is for the benefit of employees of the group or of any entity that is a related party of the group.

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

(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 materially may be aggregated if they share a majority of these criteria.

3 CHANGES IN ACCOUNTING POLICIES

The IASB has issued one new IFRS, a number of amendments to IFRSs and new Interpretations 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:

— IFRS 8, *Operating segments*

— IAS 1 (revised 2007), *Presentation of financial statements*

— Improvements to IFRSs (2008)

— Amendments to IAS 27, *Consolidated and separate financial statements — cost of an investment in a subsidiary, jointly controlled entity or associate*

— Amendments to IFRS 7, *Financial instruments: Disclosures — improving disclosures about financial instruments*

— IAS 23 (revised 2007), *Borrowing costs*

— Amendments to IFRS 2, *Share-based payment — vesting conditions and cancellations*

The amendments to IFRS 2, IAS 27, IFRS 7 and Improvements to IFRSs (2008) have had no material impact on the group's financial statements as the amendments and interpretations were consistent with policies already adopted by the group. In addition, the amendments to IFRS do not contain any additional disclosure requirements specifically applicable to these financial statements. The impact of the remainder of these developments is as follows:

— IFRS 8 requires segment disclosure to be based on the way that the group's chief operating decision maker regards and manages the group, with the amounts reported for each reportable segment being the measures reported to the group's chief operating decision maker for the purposes of assessing segment performance and making decisions about operating matters. This contrasts with the presentation of segment information in prior years which was based on a disaggregation of the group's financial statements into segments based on related products and services and on geographical areas. The adoption of IFRS 8 has resulted in the presentation of segment information in a manner that is more consistent with internal reporting provided to the group's most senior executive management. Corresponding amounts have been provided on a basis consistent with the revised segment information.

3 CHANGES IN ACCOUNTING POLICIES (continued)

— As a result of the adoption of IAS 1 (revised 2007), details of changes in equity during the period arising from transactions with equity shareholders in their capacity as such have been presented separately from all other income and expenses in a revised consolidated statement of changes in equity. All other items of income and expenses are presented in the consolidated income statement, if they are recognised as part of profit or loss for the period, or otherwise in a new primary statement, the consolidated statement of comprehensive income. Corresponding amounts have been restated to conform to the new presentation. This change in presentation has no effect on reported profit or loss, total income and expense or net assets for any period presented.

— The IAS 23 (revised) eliminates the option in IAS 23 (2004 version) of recognising all borrowing costs immediately as an expense. Consequently the group is required to adopt a policy of capitalising borrowing costs which are directly attributable to the acquisition, construction or production of a qualifying asset as part of the cost of that asset. As a result, 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. 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. In accordance with the transitional provisions in the amendment, this new policy will be applied prospectively to any borrowing costs relating to qualifying assets for which the commencement date for capitalisation is on or after 1 January 2009.

4 SEGMENT REPORTING

The group manages its business by divisions, which are organised by both business lines (drilling rigs and parts and components) and geography. On first-time adoption of IFRS 8, *Operating segments* and 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 identified the following two reportable segments. No operating segments have been aggregated to form the following reportable segments.

Drilling rigs — This segment manufactures and sells drilling rigs. Currently the group's products in this regard are mainly sold to customers in the PRC, North America, Middle East, Europe and Central Asia and South Asia.

Parts and components — This segment manufactures and sells parts and components of drilling rigs. Currently the group's products in this regard are mainly sold to customers in the PRC, North America, Middle East, Europe and Central Asia and South Asia.

4 SEGMENT REPORTING (continued)

(a) Segment results, assets and liabilities

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

Segment assets include all tangible, intangible assets and current assets with the exception of interests in jointly controlled entities, current tax recoverable, deferred tax assets, pledged bank deposits, bank deposits maturing over 3 months, cash and cash equivalents and other corporate assets. Segment liabilities include trade creditors, accruals and bills payable attributable to the manufacturing and sales activities of the individual segments, with the exception of interest-bearing borrowings, current tax payable, deferred tax liabilities and other corporate liabilities.

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 "profit from operations", i.e. "adjusted earnings before net finance income/costs and taxes". To arrive at profit from operations, the group's earnings are further adjusted for items not specifically attributed to individual segments, such as share of profits of jointly controlled entities, directors' remuneration and other head office or corporate administration costs.

4 SEGMENT REPORTING (continued)

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

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

Information regarding the group's reportable segments as provided to the group's most senior executive management for the purposes of resource allocation and assessment of segment performance for the years ended 31 December 2009 and 2008 is set out below.

	Drilling rigs		Parts and components		Total	
	2009	2008	**2009**	2008	**2009**	2008
	RMB'000	RMB'000	**RMB'000**	RMB'000	**RMB'000**	RMB'000
Revenue from external customers	**1,649,653**	4,359,920	**311,864**	377,612	**1,961,517**	4,737,532
Inter-segment revenue	**—**	—	**689,456**	1,258,086	**689,456**	1,258,086
Reportable segment revenue	**1,649,653**	4,359,920	**1,001,320**	1,635,698	**2,650,973**	5,995,618
Reportable segment (loss)/profit	**(23,595)**	733,364	**64,664**	178,919	**41,069**	912,283
Depreciation and amortisation for the year	**66,006**	30,765	**15,255**	14,318	**81,261**	45,083
Reportable segment assets	**2,918,121**	3,698,482	**1,304,594**	1,389,674	**4,222,715**	5,088,156
Additions to non-current segment assets during the year	**51,118**	79,653	**47,264**	71,154	**98,382**	150,807
Reportable segment liabilities	**828,329**	1,335,279	**290,405**	519,086	**1,118,734**	1,854,365

4 SEGMENT REPORTING (continued)

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

	2009 RMB'000	2008 RMB'000
(Loss)/profit		
Reportable segment profit	**41,069**	912,283
Elimination of inter-segment profits	**(163,751)**	(186,024)
Reportable segment (loss)/profit derived from group's external customers	**(122,682)**	726,259
Share of (loss)/profit from jointly controlled entities	**(4,766)**	7,332
Other operating revenue, expenses and net income	**15,516**	12,067
Net finance expenses	**(3,709)**	(88,701)
Unallocated head office and corporate income/(expenses)	**(13,570)**	(1,451)
Consolidated (loss)/profit before taxation	**(129,211)**	655,506
Assets		
Reportable segment assets	**4,222,715**	5,088,156
Elimination of inter-segment receivables	**(203,810)**	(368,630)
	4,018,905	4,719,526
Interests in jointly controlled entities	**10,309**	9,604
Current tax recoverable	**24,393**	—
Deferred tax assets	**49,372**	16,044
Unallocated head office and corporate assets	**2,485,989**	3,038,749
Consolidated total assets	**6,588,968**	7,783,923
Liabilities		
Reportable segment liabilities	**1,118,734**	1,854,365
Elimination of inter-segment payables	**(203,810)**	(368,630)
	914,924	1,485,735
Current tax payable	**20,933**	77,079
Deferred tax liabilities	**10,414**	9,689
Unallocated head office and corporate liabilities	**1,378,768**	1,684,012
Consolidated total liabilities	**2,325,039**	3,256,515

4 SEGMENT REPORTING (continued)

(c) Geographic information

The following table sets out information about the geographical location of (i) the group's revenue from external customers and (ii) the group's fixed assets, deposits paid for acquisition of leasehold land, construction in progress, intangible assets and interests in jointly controlled entities ("specified non-current assets"). The geographical location of customers is based on the location of the customers. 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, the location of the operation to which they are allocated, in the case of intangible assets and interests in jointly controlled entities.

	Revenue from external customers		Specified non-current assets	
	2009	2008	**2009**	2008
	RMB'000	RMB'000	**RMB'000**	RMB'000
PRC	**250,454**	471,519	**1,111,162**	888,763
North America	**205,109**	322,021	**36,824**	31,234
Middle East	**777,590**	417,321	**1,330**	785
Europe and Central Asia	**676,323**	2,816,936	**19**	50
South Asia	**37,759**	326,914	**—**	—
Others	**14,282**	382,821	**10,364**	9,604
	1,961,517	4,737,532	**1,159,699**	930,436

5 REVENUE

The principal activities of the group are the manufacturing, sale and trading of drilling rigs and related parts and components. Revenue represents the sales value of goods supplied to customers less value-added tax, returns and trade discounts.

	2009	2008
	RMB'000	RMB'000
Sale of drilling rigs	**1,649,653**	4,359,920
Sale of parts and components	**311,864**	377,612
	1,961,517	4,737,532

5 REVENUE (continued)

For the year ended 31 December 2009, the group's customer base includes two customers with whom transactions representing 29% and 21% (2008: 35% and 15%) of the group's revenue respectively. In 2009, revenues from sales of drilling rigs and related parts and components to these customers, amounted to approximately RMB563 million and RMB416 million (2008: RMB1,643 million and RMB711 million) respectively which arose in Europe and Central Asia and Middle East regions.

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

6 OTHER OPERATING REVENUE AND OTHER NET INCOME

	2009 RMB'000	2008 RMB'000
Other operating revenue		
Rendering of repairing services	5,439	4,293
Commission	147	114
Others	1,499	968
	7,085	5,375
Other net income		
Government grants	16,727	10,648
Loss on disposals of fixed assets	(990)	(287)
Realised gains on investments at fair value through profit or loss	59	3,280
Donations	(4,743)	—
Others	(1,819)	21
	9,234	13,662

7 (LOSS)/PROFIT BEFORE TAXATION

(Loss)/profit before taxation is arrived at after charging/(crediting):

		2009 RMB'000	2008 RMB'000
(a)	Net finance expenses		
	Exchange (gain)/loss, net	**(24,430)**	67,175
	Interest income	**(36,664)**	(52,023)
	Interest on interest-bearing borrowings wholly repayable within five years	**65,543**	66,138
	Bank charges	**5,604**	7,411
		10,053	88,701
	Less: interest expense capitalised into assets under construction *	**(6,344)**	—
		3,709	88,701

* The borrowing costs have been capitalised at a rate of 2.55% – 8.25% per annum (2008: Nil).

		2009 RMB'000	2008 RMB'000
(b)	Staff costs		
	Contributions to defined contribution retirement schemes	**34,508**	29,815
	Equity-settled share based payment expenses (note 25)	**34,803**	38,086
	Salaries, wages and other benefits	**210,328**	209,745
		279,639	277,646
(c)	Other items		
	Amortisation and depreciation		
	— leasehold land held for use under operating leases	**1,394**	1,636
	— other assets	**44,163**	32,475
	— intangible assets	**36,821**	12,423
	Auditors' remuneration	**3,494**	5,130
	Operating lease charges: properties	**5,628**	3,227
	Research and development costs *	**36,094**	30,550

* The amounts included staff costs of employees in the Research and Development Department, which are included in the total staff costs as disclosed in note 7(b).

8 INCOME TAX (CREDIT)/EXPENSES

(a) Taxation in the consolidated income statement represents:

	2009 RMB'000	2008 RMB'000
Current tax — outside Hong Kong		
Provision for the year	**29,668**	119,246
Over-provision in respect of prior years	**(2,044)**	(5,531)
Tax credit	**(2,152)**	—
	25,472	113,715
Deferred tax		
Origination and reversal of temporary differences (note 26(b))	**(32,598)**	1,845
Income tax (credit)/expenses	**(7,126)**	115,560

(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 (2008: 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 2009 (2008: 25%), except for the following companies:

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

On 15 September 2006, Honghua Company changed from being a domestic enterprise to a wholly-owned foreign invested enterprise, and was entitled to tax concessions from 1 October 2006 whereby the profit for the first two financial years commencing on the profit-making year (after netting off tax losses carried forward from prior years) was exempt from national income tax in the PRC and the profit for each of the subsequent three financial years was taxed at 50% of the prevailing tax rates set by the relevant authorities.

8 INCOME TAX (CREDIT)/EXPENSES (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 principal revenue of over 70% generated from the encouraged business activities. Pursuant to the approvals obtained from the relevant PRC tax authorities, the companies are entitled to a preferential income tax rate of 15%.

(iii) 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 resident enterprises are subject to withholding tax at a rate of 10% unless reduced by tax treaties or agreements. Under the *Arrangement between the Mainland of China and Hong Kong Special Administrative Region for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with respect to Taxes on Income*, Hong Kong tax residents which hold 25% or more of a PRC enterprise are entitled to a reduced dividend withholding tax rate of 5%. Pursuant to CaiShui 2008 No. 1 *Notice on Certain Preferential Enterprise Income Tax Policies*, undistributed earnings generated prior to 1 January 2008 are exempted from such withholding tax. Accordingly, dividends receivable by Honghua Holdings Limited from its subsidiaries established in the PRC in respect of their profits earned since 1 January 2008 is subject to 5% withholding tax. 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 forseeable future.

8 INCOME TAX (CREDIT)/EXPENSES (continued)

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

	2009 RMB'000	2008 RMB'000
(Loss)/profit before taxation	**(129,211)**	655,506
Notional tax on (loss)/profit before taxation, calculated at the rates applicable to (losses)/profits in the countries concerned	**(29,659)**	160,194
Tax effect of non-deductible expenses	**17,014**	17,033
Tax effect of non-taxable income	**—**	(75)
Tax effect of temporary differences previously not recognised	**—**	(2,278)
Over-provision in respect of prior years	**(2,044)**	(5,531)
Withholding tax on profits from PRC subsidiaries	**730**	5,696
Effect on deferred tax balance resulting from an increase in tax rate at the year of expected realisation	**(3,040)**	—
Tax credit	**(2,152)**	—
Effect of preferential tax rate on loss/(income)	**12,025**	(59,479)
Actual tax (credit)/expenses	**(7,126)**	115,560

9 DIRECTORS' REMUNERATION

Details of directors' remuneration are set out below:

	2009					
	Fees RMB'000	Basic salaries, allowances and other benefits in kind RMB'000	Contributions to defined contribution retirement scheme RMB'000	Discre-tionary bonuses RMB'000	Equity-settled share based payment expenses RMB'000	Total RMB'000
Chairman and Executive Director						
Zhang Mi	–	715	15	266	4,294	5,290
Executive Directors						
Ren Jie	–	394	15	313	1,723	2,445
Liu Zhi	–	380	15	245	1,567	2,207
Non-executive Directors						
Siegfried Meissner	–	–	–	–	–	–
Xiang Qingsheng (resigned with effect from 14 April 2010)	–	–	–	–	–	–
He Sean Xing (resigned with effect from 14 April 2010)	–	–	–	–	–	–
Independent Non-executive Directors						
Qi Daqing	176	–	–	–	280	456
Liu Xiaofeng	176	–	–	–	280	456
Chen Guoming	88	–	–	–	210	298
Wang Li	88	–	–	–	210	298
Tai Kwok Leung, Alexander	132	–	–	–	238	370
Wang Chunlin (resigned on 13 February 2009)	16	–	–	–	–	16
Liu Yinchun (resigned with effect from 14 April 2010)	88	–	–	–	210	298
Shi Xingquan (appointed on 14 April 2009)	63	–	–	–	210	273
Total	827	1,489	45	824	9,222	12,407

(Expressed in Renminbi unless otherwise indicated)

9 DIRECTORS' REMUNERATION (continued)

Details of directors' remuneration are set out below: (continued)

	2008					
	Fees	Basic salaries, allowances and other benefits in kind	Contributions to defined contribution retirement scheme	Discre-tionary bonuses	Equity-settled share based payment expenses	Total
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
Chairman and Executive Director						
Zhang Mi	–	1,144	13	1,067	6,284	8,508
Executive Directors						
Ren Jie	–	385	13	771	1,968	3,137
Liu Zhi	–	719	12	434	1,777	2,942
Zhang Xu (resigned on 26 May 2008)	–	66	4	–	277	347
Non-executive Directors						
Wang Yaoxin (resigned on 26 May 2008)	–	–	–	–	–	–
Siegfried Meissner	–	–	–	–	–	–
Xiang Qingsheng	–	–	–	–	–	–
He Sean Xing	–	–	–	–	–	–
Independent Non-executive Directors						
Qi Daqing	176	–	–	–	–	176
Liu Xiaofeng	176	–	–	–	–	176
Chen Guoming	88	–	–	–	–	88
Wang Li	88	–	–	–	–	88
Tai Kwok Leung, Alexander	132	–	–	–	–	132
Wang Chunlin (resigned on 13 February 2009)	132	–	–	–	–	132
Liu Yinchun	88	–	–	–	–	88
Total	880	2,314	42	2,272	10,306	15,814

9 DIRECTORS' REMUNERATION (continued)

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 10 below as an inducement to join or upon joining the group or as compensation for loss of office. There was no arrangement under which a director waived or agreed to waive any remuneration during the year (2008: Nil).

10 INDIVIDUAL WITH HIGHEST EMOLUMENTS

The five highest paid individuals of the group include three directors during the year ended 31 December 2009 (2008: three) whose emoluments are disclosed in note 9. Details of remuneration paid to the remaining two (2008: two) highest individuals of the group are as follows:

	2009 **RMB'000**	2008 RMB'000
Basic salaries, allowances and other benefits in kind	**717**	1,000
Discretionary bonuses	**534**	861
Contributions to defined contribution retirement schemes	**2**	13
Share-based payments	**2,395**	2,412
	3,648	4,286

The emoluments of these individuals are within the following bands:

	2009	2008
HK$1,500,001 to HK$2,000,000	**1**	—
HK$2,000,001 to HK$2,500,000	**1**	2

11 PROFIT ATTRIBUTABLE TO EQUITY SHAREHOLDERS OF THE COMPANY

The consolidated profit attributable to equity shareholders of the company includes a profit of RMB135,838,000 (2008: RMB284,101,000) which has been dealt with in the financial statements of the company.

(Expressed in Renminbi unless otherwise indicated)

12 (LOSS)/EARNINGS PER SHARE

(a) Basic (loss)/earnings per share

The calculation of basic (loss)/earnings per share is based on the loss attributable to ordinary equity shareholders of the company of RMB127,337,000 (2008: a profit of RMB511,974,000) and the weighted average number of 3,222,697,730 (2008: 3,157,004,167) ordinary shares in issue during the year, calculated as follows:

Weighted average number of ordinary shares

	2009	2008
Issued ordinary shares at 1 January	**3,222,688,000**	2,500,000,000
Effect of shares issued under placing and public offering (note 29(c)(i))	**–**	683,081,967
Effect of shares repurchased (note 29(c)(ii))	**–**	(26,077,800)
Effect of share options exercised	**9,730**	–
Weighted average number of ordinary shares at 31 December	**3,222,697,730**	3,157,004,167

(b) Diluted (loss)/earnings per share

The calculation of diluted loss per share for the year ended 31 December 2009 is based on the loss attributable to ordinary equity shareholders of the company of RMB127,337,000 and the weighted average number of ordinary shares of 3,225,036,859, calculated as follows:

Weighted average number of ordinary shares (diluted)

	2009
Weighted average number of ordinary shares at 31 December	**3,222,697,730**
Effect of deemed issue of shares under the company's share option schemes	**2,339,129**
Weighted average number of ordinary shares (diluted) at 31 December	**3,225,036,859**

There were no dilutive potential ordinary shares for the year ended 31 December 2008 and, therefore, diluted earnings per share is the same as the basic earnings per share.

13 FIXED ASSETS

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 2009	5,509	57,843	210,125	120,609	93,376	35,873	523,335
Additions	–	–	8,318	10,771	27,304	4,912	51,305
Transfer from construction in progress (note 14)	–	–	35,545	506	2,298	–	38,349
Transfer from deposits paid for acquisition of leasehold land	–	89,762	–	–	–	–	89,762
Disposals	–	–	(1,159)	(61)	(6,127)	(1,536)	(8,883)
Exchange difference	(5)	–	(25)	(145)	(15)	–	(190)
At 31 December 2009	5,504	147,605	252,804	131,680	116,836	39,249	693,678
Accumulated amortisation and depreciation:							
At 1 January 2009	–	4,382	18,681	27,465	28,413	10,255	89,196
Charge for the year	–	1,394	12,939	12,688	13,748	4,788	45,557
Written back on disposals	–	–	(60)	(45)	(2,159)	(884)	(3,148)
Exchange difference	–	–	(2)	(2)	(2)	–	(6)
At 31 December 2009	–	5,776	31,558	40,106	40,000	14,159	131,599
Net book value:							
At 31 December 2009	5,504	141,829	221,246	91,574	76,836	25,090	562,079

13 FIXED ASSETS (continued)

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 2008	5,880	57,576	132,474	90,498	64,282	25,217	375,927
Additions	–	267	4,889	28,835	29,807	11,013	74,811
Transfer from construction in progress (note 14)	–	–	75,215	1,479	2,267	–	78,961
Disposals	–	–	(939)	(56)	(2,899)	(44)	(3,938)
Exchange difference	(371)	–	(1,514)	(147)	(81)	(313)	(2,426)
At 31 December 2008	5,509	57,843	210,125	120,609	93,376	35,873	523,335
Accumulated amortisation and depreciation:							
At 1 January 2008	–	2,746	12,389	17,327	16,690	6,612	55,764
Charge for the year	–	1,636	6,579	10,222	11,948	3,726	34,111
Written back on disposals	–	–	(223)	(42)	(192)	(35)	(492)
Exchange difference	–	–	(64)	(42)	(33)	(48)	(187)
At 31 December 2008	–	4,382	18,681	27,465	28,413	10,255	89,196
Net book value:							
At 31 December 2008	5,509	53,461	191,444	93,144	64,963	25,618	434,139

Interests in leasehold land held for own use under operating leases represent prepayments for land use rights in the PRC.

14 CONSTRUCTION IN PROGRESS

	The group	
	2009	2008
	RMB'000	RMB'000
Balance at 1 January	**40,369**	38,741
Additions	**57,124**	80,589
Transfer to fixed assets (note 13)	**(38,349)**	(78,961)
Balance at 31 December	**59,144**	40,369

15 INTANGIBLE ASSETS

	The group and the company	
	2009	2008
	RMB'000	RMB'000
Cost:		
At 1 January	**368,499**	389,691
Exchange difference	**(585)**	(21,192)
At 31 December	**367,914**	368,499
Accumulated amortisation:		
At 1 January	**12,283**	—
Amortisation for the year	**36,821**	12,423
Exchange difference	**(49)**	(140)
At 31 December	**49,055**	12,283
Net book value:		
At 31 December	**318,859**	356,216

Intangible assets represent the technology licences granted by a shareholder.

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

16 INVESTMENTS IN SUBSIDIARIES

	The company	
	2009	2008
	RMB'000	RMB'000
Unlisted equities, at cost	**220,125**	220,475
Long-term receivable from a subsidiary	**2,466,898**	2,470,826
	2,687,023	2,691,301

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

Details of the subsidiaries at 31 December 2009 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 (formerly known as Asia Harbour International Limited) (宏華控股有限公司) (note (i))	Hong Kong	HK$1	100%	–	Investment holding
Honghua Company (四川宏華石油設備有限公司) (notes (i), (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
Honghua America, LLC (宏華美國有限責任公司) (note (i))	United States of America	US$800,000	–	80%	Trading of drilling rigs and related parts

(Expressed in Renminbi unless otherwise indicated)

16 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	
Golden Coast Company (宏華金海岸設備有限公司) (note (i))	United Arab Emirates	AED1,000,000	—	100%	Trading of drilling rigs and related parts
Sichuan Honglian Industrial Co. Ltd. (四川宏聯實業有限公司) (notes (i), (ii), (iii))	The PRC	HK$758,000,000	—	100%	Trading of drilling rigs and related parts
Sichuan Hongcheng Business Trading Ltd. (四川宏程商貿有限公司) (notes (i), (ii), (iii))	The PRC	HK$758,000,000	—	100%	Trading of drilling rigs and related parts
Newco (H.K.) Limited (新順(香港)有限公司) (note (i))	Hong Kong	HK$1,000	—	100%	Trading of drilling rigs and related parts
Russia Honghua Co., Ltd (俄羅斯宏華有限公司) (note (i))	Russia	RUR10,000	—	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 (i), (ii), (iii))	The PRC	US$29,980,000	—	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
Honghua Oil & Gas Engineering Services Limited (宏華油氣工程服務有限公司) (note (i))	Hong Kong	HK$1	—	100%	Investment holding
Alpha Advance Limited (首進有限公司) (note (i))	Hong Kong	HK$10,000	—	75%	Investment holding

16 INVESTMENTS IN SUBSIDIARIES (continued)

Notes:

(i) These entities are domestic limited liability companies.

(ii) These entities are wholly-owned foreign invested enterprises.

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

17 INTERESTS IN JOINTLY CONTROLLED ENTITIES

	The group	
	2009	2008
	RMB'000	RMB'000
Share of net assets	**5,188**	9,604
Amount due from a jointly controlled entity	**5,121**	—
	10,309	9,604

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

Name of company	Place of establishment	Issued and paid up capital	Group's effective interest held by a subsidiary	Principal activities
Egyptian Petroleum HH Rig Manufacturing Shareholder Co. ("HH Egyptian Company")	Egypt	US$12,000,000	50%	Manufacturing and sale of drilling rigs, parts and components
Honghua — Ukraine Limited	Ukraine	Ukraine Hryvnia 51,500	50%	Trading of drilling rigs, parts and components

17 INTERESTS IN JOINTLY CONTROLLED ENTITIES (continued)

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

	The group	
	2009	2008
	RMB'000	RMB'000
Non-current assets	**57,227**	53,250
Current assets	**56,725**	39,957
Current liabilities	**(24,176)**	(14,766)
Non-current liabilities	**(84,588)**	(68,837)
	5,188	9,604
Income	**319**	78,924
Expenses	**(5,085)**	(71,592)
(Loss)/profit for the year	**(4,766)**	7,332

18 INVENTORIES

(a) Inventories in the balance sheet comprise:

	The group	
	2009	2008
	RMB'000	RMB'000
Raw materials	**832,164**	917,372
Work in progress	**536,600**	506,352
Finished goods	**528,554**	566,557
Goods in transit	**3,850**	43,207
	1,901,168	2,033,488

18 INVENTORIES (continued)

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

	The group	
	2009	2008
	RMB'000	RMB'000
Carrying amount of inventories sold	**1,388,090**	3,353,267
Write-down of inventories	**45,128**	24,422
Reversal of write-down of inventories	**–**	(28,200)
	1,433,218	3,349,489

19 TRADE AND OTHER RECEIVABLES

	The group	
	2009	2008
	RMB'000	RMB'000
Trade receivables	**901,707**	1,551,659
Bills receivable	**2,200**	4,706
Less: allowance for doubtful debts (note 19(b))	**(124,669)**	(1,405)
Sub-total	**779,238**	1,554,960
Value-added tax recoverable	**191,450**	257,430
Prepayments	**154,884**	182,457
Other receivables	**120,779**	50,222
	1,246,351	2,045,069

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	
	2009	2008
	RMB'000	RMB'000
Current	**276,849**	1,074,915
Less than 1 month past due	**24,970**	290,721
More than1 month but less than 3 months past due	**60,121**	130,739
More than 3 months but less than 12 months past due	**136,445**	24,852
More than 1 year past due	**280,853**	33,733
	779,238	1,554,960

The group normally grants an average credit period of 30 to 90 days to its trade customers. Further details on the group's credit policy are set out in note 30(a).

(b) Impairment of trade receivables and bills receivable

Impairment loss in respect of trade receivables and bills receivable is 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(k)).

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

	The group	
	2009	2008
	RMB'000	RMB'000
At 1 January	**1,405**	3,312
Provision for impairment losses	**123,264**	247
Written back of impairment losses	**–**	(2,154)
At 31 December	**124,669**	1,405

The individually impaired receivables relate to customers that are in financial difficulties and management assesses the recoverability is remote. Consequently, specific allowances for doubtful debts were recognised. The group does not hold any collateral over these balances.

19 TRADE AND OTHER RECEIVABLES (continued)

(c) Trade receivables that are not impaired

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 (as shown in the table in note 19(a)) 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 PLEDGED BANK DEPOSITS

The deposits are pledged to banks as security against certain banking facilities granted to the group (see note 23).

21 CASH AND CASH EQUIVALENTS

	The group		The company	
	2009	2008	**2009**	2008
	RMB'000	RMB'000	**RMB'000**	RMB'000
Cash at bank and in hand	**1,603,316**	1,467,363	**47,246**	50,241

As at 31 December 2009, deposits that were placed with banks in the PRC and included in the cash and cash equivalents above amounted to RMB1,366,037,710 (2008: RMB1,196,876,702). Remittance of funds out of the PRC is subject to the exchange restrictions imposed by the PRC government.

22 INTEREST-BEARING BORROWINGS

The interest-bearing borrowings were secured as follows:

	The group	
	2009	2008
	RMB'000	RMB'000
Secured	**14,339**	804,401
Unsecured	**1,284,141**	771,000
Total	**1,298,480**	1,575,401

The interest-bearing borrowings were repayable as follows:

	The group	
	2009	2008
	RMB'000	RMB'000
Within 1 year	**1,046,090**	1,561,000
After 1 year but within 2 years	**250,000**	11,961
After 2 years but within 5 years	**2,390**	2,440
	252,390	14,401
Total	**1,298,480**	1,575,401

The interest-bearing borrowings as at 31 December 2009 amounted to RMB14,339,000 (2008: RMB804,401,000) are secured by the equipment and inventories with an aggregate carrying value of RMB214,451,000 (2008: RMB156,602,000) and the leasehold land with an aggregate carrying value of RMB Nil (2008: RMB82,863,000).

The interest-bearing borrowings at 31 December 2009 bear interest at 2.55% to 6.50% per annum (2008: 4.86% to 8.25% per annum).

Certain banking facilities of the group are subject to the fulfilment of covenants relating to certain of the group's profitability and financial positions. 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 30(b). As at 31 December 2009 and 2008, none of the covenants relating to drawn down facilities had been breached.

23 TRADE AND OTHER PAYABLES

	The group		The company	
	2009	2008	**2009**	2008
	RMB'000	RMB'000	**RMB'000**	RMB'000
Trade payables	**413,060**	702,194	**–**	–
Bills payable	**104,442**	176,371	**–**	–
Receipts in advance	**316,444**	522,505	**–**	–
Other payables	**140,078**	139,659	**400**	7,948
	974,024	1,540,729	**400**	7,948

Bills payable as at 31 December 2008 and 2009 were secured by pledged bank deposits as disclosed in note 20. All of the trade and other payables are expected to be settled or recognised as income within one year or are repayable on demand.

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

	The group	
	2009	2008
	RMB'000	RMB'000
Within 3 months	**235,754**	645,852
3 months to 6 months	**98,020**	117,862
6 months to 1 year	**51,061**	79,895
Over 1 year	**132,667**	34,956
	517,502	878,565

24 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% (2008: 20%) of the standard wages determined by the relevant authorities in the PRC during the year ended 31 December 2009. The local government authority is responsible for the entire pension obligations payable to retired employees.

24 EMPLOYEE RETIREMENT BENEFITS (continued)

Defined contribution schemes (continued)

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 HK$20,000. Contributions to the scheme vest immediately.

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

25 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) 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)
Options granted to directors:	
— on 21 January 2008	14,191
Options granted to employees:	
— on 21 January 2008	45,809
Total share options granted	60,000

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.

25 EQUITY-SETTLED SHARE BASED PAYMENTS (continued)

(a) Pre-IPO Share Option Scheme (continued)

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

	2009 Exercise price	**2009** Number of options ('000 shares)	2008 Exercise price	2008 Number of options ('000 shares)
Outstanding at the beginning of the year	**HK$3.83**	**60,000**	–	–
Granted during the year	**–**	**–**	HK$3.83	60,000
Forfeited during the year	**HK$3.83**	**(468)**	–	–
Lapsed during the year	**HK$3.83**	**(203)**	–	–
Outstanding at the end of the year	**HK$3.83**	**59,329**	HK$3.83	60,000
Exercisable at the end of the year	**HK$3.83**	**23,740**	HK$3.83	12,000

The options outstanding at 31 December 2009 had a weighted average remaining contractual life of 8.08 years (2008: 9.08 years).

25 EQUITY-SETTLED SHARE BASED PAYMENTS (continued)

(b) Share Option Scheme

(i) The company has 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 to directors:			
— on 15 April 2009	8,897	(i) 30% on 1 December 2009	10 years
		(ii) 30% on 14 April 2010	
		(iii) 40% on 15 April 2011	
Options granted to employees:			
— on 15 April 2009	51,103	(i) 30% on 1 December 2009	10 years
		(ii) 30% on 14 April 2010	
		(iii) 40% on 15 April 2011	
Total share options	60,000		

25 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:

	2009 Exercise price	2009 Number of options ('000 shares)
Outstanding at the beginning of the year	–	–
Granted during the year	HK$1.27	60,000
Exercised during the year	HK$1.27	(531)
Forfeited during the year	HK$1.27	(178)
Outstanding at the end of the year	HK$1.27	59,291
Exercisable at the end of the year	HK$1.27	17,426

The weighted average share price at the date of exercise for share options exercised during the year was HK$1.59 (2008: not applicable).

The options outstanding at 31 December 2009 had a weighted average remaining contractual life of 9.29 years.

(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.

25 EQUITY-SETTLED SHARE BASED PAYMENTS (continued)

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

Fair value of share options and assumptions

	Pre-IPO Share Option Scheme	Share Option Scheme
Fair value at measurement date	HK$1.40	HK$0.46
Share price	HK$3.83	HK$1.27
Exercise price	HK$3.83	HK$1.27
Expected volatility (expressed as weighted average volatility used in the modelling under Binomial Lattice Model)	44.9%	56.9%
Option life (expressed as weighted average life used in the modelling under Binomial Option Pricing Model)	10 years	10 years
Expected dividends	20%	33%
Risk-free interest rate	2.647%	2.016%

26 INCOME TAX IN THE BALANCE SHEET

(a) Current taxation in the balance sheet represents:

	The group 2009 RMB'000	2008 RMB'000
Income tax		
— Provision for income tax	**27,516**	119,120
— Income tax paid	**(43,776)**	(40,788)
	(16,260)	78,332
Balance of income tax payable/ (recoverable) in respect of prior years	**12,800**	(1,253)
	(3,460)	77,079
Represented:		
Current tax recoverable	**(24,393)**	—
Current tax payable	**20,933**	77,079
	(3,460)	77,079

26 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 of 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	Total RMB'000
Deferred tax arising from:								
At 1 January 2009	4,052	4,030	(4,083)	7,962	–	(5,606)	–	6,355
(Charged)/credited to the income statement (note 8(a))	6,387	(2,083)	–	5,036	18,240	(730)	5,748	32,598
Exchange difference	–	–	5	–	–	–	–	5
At 31 December 2009	10,439	1,947	(4,078)	12,998	18,240	(6,336)	5,748	38,958
At 1 January 2008	8,096	3,741	(3,983)	–	–	–	–	7,854
(Charged)/credited to the income statement (note 8(a))	(4,044)	289	(356)	7,962	–	(5,696)	–	(1,845)
Exchange difference	–	–	256	–	–	90	–	346
At 31 December 2008	4,052	4,030	(4,083)	7,962	–	(5,606)	–	6,355

	The group	
	2009 RMB'000	2008 RMB'000
Deferred tax assets recognised on the balance sheet	49,372	16,044
Deferred tax liabilities recognised on the balance sheet	(10,414)	(9,689)
	38,958	6,355

27 PROVISION FOR PRODUCT WARRANTIES

	The group RMB'000
At 1 January 2009	32,241
Additional provision made	15,579
Written back during the year	(5,342)
Utilised during the year	(26,899)
At 31 December 2009	15,579

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.

28 AMOUNT DUE FROM A SUBSIDIARY

The amount due from a subsidiary is unsecured, interest-free and has no fixed repayment terms.

29 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 29(c))	Share premium RMB'000 (note 29(d)(v))	Other reserve RMB'000 (note 29(d)(iii))	Capital reserve RMB'000 (note 29(d)(iv))	Exchange reserve RMB'000 (note 29(d)(ii))	Accumulated losses RMB'000	Total RMB'000
At 1 January 2009		299,495	2,508,202	389,691	38,086	(131,437)	(6,041)	3,097,996
Dividends approved in respect of the previous financial year	29(b)	–	(32,243)	–	–	–	(138,128)	(170,371)
Equity-settled share-based transactions	25	–	–	–	34,803	–	–	34,803
Shares issued under share option schemes	25	47	746	–	(199)	–	–	594
Options lapsed under share option schemes		–	–	–	(215)	–	215	–
Total comprehensive income for the year		–	–	–	–	(4,937)	135,838	130,901
At 31 December 2009		299,542	2,476,705	389,691	72,475	(136,374)	(8,116)	3,093,923
At 1 January 2008		233,155	–	389,691	–	–	(2,471)	620,375
Shares issued under placing and public offering, net issuing expenses	29(c)(i)	76,077	2,623,896	–	–	–	–	2,699,973
Special dividends declared and paid	29(b)	–	–	–	–	–	(287,671)	(287,671)
Repurchase of own shares	29(c)(ii)	(9,737)	(115,694)	–	–	–	–	(125,431)
Equity-settled share-based transactions	25	–	–	–	38,086	–	–	38,086
Total comprehensive income for the year		–	–	–	–	(131,437)	284,101	152,664
At 31 December 2008		299,495	2,508,202	389,691	38,086	(131,437)	(6,041)	3,097,996

29 CAPITAL, RESERVES AND DIVIDENDS (continued)

(b) Dividends

(i) Dividends payable to equity shareholders of the company attributable to the year:

	2009 RMB'000	2008 RMB'000
Special dividends declared and paid of Hong Kong dollars ("HK$") Nil per share (2008: HK$0.10 per share)	–	287,671
Final dividend proposed after the balance sheet date of HK$Nil per share (2008: HK$0.06 per share)	–	170,371
	–	458,042

Special dividends represent non-recurring dividends declared by a board resolution on 16 September 2008.

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

(ii) Dividends payable to equity shareholders of the company attributable to the previous financial year, approved and paid during the year:

	2009 RMB'000	2008 RMB'000
Final dividend in respect of the previous financial year, approved and paid during the year, of HK$0.06 per share (2008: HK$Nil)	170,371	–

The final dividend has been distributed from both the retained profits and the share premium of the company.

29 CAPITAL, RESERVES AND DIVIDENDS (continued)

(c) Share capital

Authorised and issued share capital

	2009 Number of shares	2009 '000	2008 Number of shares	2008 '000
Authorised:				
Ordinary shares of HK$0.1 each	10,000,000,000	HK$1,000,000	10,000,000,000	HK$1,000,000
Equivalent to:		RMB968,739		RMB968,739
Ordinary shares, issued and fully paid:				
		RMB'000		RMB'000
At 1 January	3,222,688,000	299,495	2,500,000,000	233,155
Issue of shares under public offering (note (i))	–	–	833,360,000	76,077
Purchase of own shares (note (ii))	–	–	(110,672,000)	(9,737)
Shares issued under share option schemes (note 25(b)(ii))	531,100	47	–	–
At 31 December	3,223,219,100	299,542	3,222,688,000	299,495

29 CAPITAL, RESERVES AND DIVIDENDS (continued)

(c) Share capital (continued)

Authorised and issued share capital (continued)

(i) Issue of shares under public offering

On 7 March 2008, the company issued 833,360,000 shares with a par value of HK$0.10 each, at a price of HK$3.83 per share by way of an initial public offering to Hong Kong and overseas investors. Net proceeds from such issue amounted to RMB2,699,973,000 (after offsetting listing expenses of RMB213,791,000), out of which RMB76,077,000 and RMB2,623,896,000 were recorded in share capital and share premium respectively).

(ii) Purchase of own shares

During the year ended 31 December 2008, the company repurchased its own shares on the Stock Exchange as follows:

Month/year	Number of shares repurchased	Highest price paid per share HK$	Lowest price paid per share HK$	Aggregate consideration paid HK$'000
September 2008	53,304,000	1.45	1.06	70,312
October 2008	51,200,000	1.56	1.07	64,766
November 2008	6,168,000	1.30	1.15	7,491
	110,672,000			142,569

The repurchased shares were cancelled and, accordingly, the issued share capital of the company was reduced by the nominal value of these shares. The premium paid on the repurchase of the shares of HK$131,502,000 (equivalent to RMB115,694,000) was charged to the share premium account.

29 CAPITAL, RESERVES AND DIVIDENDS (continued)

(d) Nature and purpose of reserves

(i) 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.

(ii) 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(u).

(iii) Other reserve

The other reserve of the group 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 minority interests and entities under common control over the consideration given and the contribution of technology licenses by shareholder.

(iv) 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 25 and waiver of debts by the immediate holding company.

(v) 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.

(e) Distributability of reserves

At 31 December 2009, the aggregate amount of reserves available for distribution to equity shareholders of the company was RMB2,930,755,000 (2008: RMB2,929,938,000).

29 CAPITAL, RESERVES AND DIVIDENDS (continued)

(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 2009, the group's strategy, which was unchanged from 2008, 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 2009 and 2008 are 0.55 and 0.71 respectively.

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

30 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 polices 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. Trade receivables are due within 30 to 90 days from the date of billing. The group meets with those debtors with overdue balances to agree a repayment schedule and continuously 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. Normally, the group does not collect collateral from customers.

30 FINANCIAL RISK MANAGEMENT AND FAIR VALUE (continued)

(a) Credit risk (continued)

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 concentrations of credit risk primarily arise when the group has significant exposure to individual customers. At the balance sheet date, 12% (2008: 18%) and 37% (2008: 50%) of the total trade and bills receivables was due from the group's largest debtor and the five largest debtors respectively.

The maximum exposure to credit risk without taking account of any collateral held is represented by the carrying amount of each financial asset in the balance sheet after deducting any impairment allowance.

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.

(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 longer term.

30 FINANCIAL RISK MANAGEMENT AND FAIR VALUE (continued)

(b) Liquidity risk (continued)

The following table shows the remaining contractual maturities at the balance sheet date of the group's and the company's financial liabilities which are based on contractual undiscounted cash flows (including interest payments computed using contractual rates or, if floating, based on rates current at the balance sheet date) and earliest date the group and the company can be required to pay:

The group

	2009					2008				
	Contractual undiscounted cash outflow					Contractual undiscounted cash outflow				
	Within 1 year or on demand RMB'000	More than 1 year but less than 2 years RMB'000	More than 2 years but less than 5 years RMB'000	Total RMB'000	Balance sheet carrying amount RMB'000	Within 1 year or on demand RMB'000	More than 1 year but less than 2 years RMB'000	More than 2 years but less than 5 years RMB'000	Total RMB'000	Balance sheet carrying amount RMB'000
Trade and other payables	(974,024)	–	–	(974,024)	974,024	(1,540,729)	–	–	(1,540,729)	1,540,729
Interest-bearing borrowings	(1,092,865)	(257,742)	(2,546)	(1,353,153)	1,298,480	(1,663,324)	(12,585)	(2,760)	(1,678,669)	1,575,401
Amounts due to related companies	(5,609)	–	–	(5,609)	5,609	(21,376)	–	–	(21,376)	21,376
Provision for product warranties	(15,579)	–	–	(15,579)	15,579	(32,241)	–	–	(32,241)	32,241
	(2,088,077)	(257,742)	(2,546)	(2,348,365)	2,293,692	(3,257,670)	(12,585)	(2,760)	(3,273,015)	3,169,747

The company

	2009					2008				
	Contractual undiscounted cash outflow					Contractual undiscounted cash outflow				
	Within 1 year or on demand RMB'000	More than 1 year but less than 2 years RMB'000	More than 2 years but less than 5 years RMB'000	Total RMB'000	Balance sheet carrying amount RMB'000	Within 1 year or on demand RMB'000	More than 1 year but less than 2 years RMB'000	More than 2 years but less than 5 years RMB'000	Total RMB'000	Balance sheet carrying amount RMB'000
Other payables	(400)	–	–	(400)	400	(7,948)	–	–	(7,948)	7,948

30 FINANCIAL RISK MANAGEMENT AND FAIR VALUE (continued)

(c) Interest rate risk

The interest rates and maturity information of the group's interest-bearing borrowings are disclosed in note 22. 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.

The group has interest-bearing assets carrying at floating rate as set out in the table below. All of the interest-bearing borrowings of the group are fixed rate instruments and are insensitive to any change in market interest rates. The net exposure subject to the interest rate risk is not material and management does not expect the increase in interest rates at the balance sheet date would significantly affect 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			
	2009		2008	
	Effective interest rate %	**RMB'000**	Effective interest rate %	RMB'000
Fixed rate borrowings:				
Interest-bearing borrowings	**6.50%**	**2,390**	6.50%–8.25%	14,401
Variable rate borrowings:				
Interest-bearing borrowings	**2.55%–6.50%**	**1,296,090**	4.86%–7.47%	1,561,000
Interest-bearing assets:				
Pledged bank deposits	**1.98%–2.88%**	**30,663**	1.00%–3.24%	259,099
Bank deposits maturing over 3 months	**0.18%–4.14%**	**542,898**	1.10%–4.14%	998,356
Cash and cash equivalents	**0.00%–1.60%**	**1,603,316**	0.00%–2.50%	1,467,363

30 FINANCIAL RISK MANAGEMENT AND FAIR VALUE (continued)

(c) Interest rate risk (continued)

(i) Interest rate profile (continued)

	The company			
	2009		2008	
	Effective interest rate		Effective interest rate	
	%	**RMB'000**	%	RMB'000
Interest-bearing assets:				
Cash and cash equivalents	**0.01%**	**47,246**	0.01%	50,241

(ii) Sensitivity analysis

At 31 December 2009, it is estimated that a general increase/decrease of 50 basis points in interest rates, with all other variables held constant, would decrease/increase the group's loss after tax by approximately RMB4,400,000 (2008: increase/decrease the group's profit after tax by approximately RMB5,222,000).

Management assumed that certain loans maturing during the next reporting period will be rolled over upon the maturity for daily operation purpose.

The sensitivity analysis above indicates the instantaneous change in the group's (loss)/profit after tax (and retained profits) and other components of consolidated equity 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 (loss)/profit after tax (and retained profits) and other components of consolidated equity 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 2008.

30 FINANCIAL RISK MANAGEMENT AND FAIR VALUE (continued)

(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 resulting from fluctuation of USD.

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 authorised to buy and sell foreign currencies. The exchange rate adopted for the foreign exchange transactions are the rates of exchange quoted by the People's Bank of China that are determined largely by supply and demand.

In addition, 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.

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.

The group

	Exposure to foreign currencies (expressed in RMB'000) 2009		
	USD	**EUR**	**HKD**
Cash and cash equivalents	**109,716**	**17,292**	**2,280**
Trade and other receivables	**460,166**	**234,445**	**–**
Interest-bearing borrowings	**(34,141)**	**–**	**–**
Trade and other payables	**(144,635)**	**(4,242)**	**(1,849)**
Overall net exposure	**391,106**	**247,495**	**431**

30 FINANCIAL RISK MANAGEMENT AND FAIR VALUE (continued)

(d) Currency risk (continued)

The group (continued)

	Exposure to foreign currencies (expressed in RMB'000) 2008		
	USD	EUR	HKD
Cash and cash equivalents	179,408	251	4,594
Trade and other receivables	990,190	293,131	—
Trade and other payables	(145,338)	(4,182)	—
Overall net exposure	1,024,260	289,200	4,594

Sensitivity analysis

The following table indicates the instantaneous change in the group's (loss)/profit after tax (and retained profits) and other components of consolidated equity 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				
	2009			2008	
	Increase/ (decrease) in foreign exchange rates	**Effect on loss after tax RMB'000**	**Effect on retained profits RMB'000**	Increase/ (decrease) in foreign exchange rates	Effect on loss after tax and retained profits RMB'000
USD	**5%**	**(15,341)**	**15,341**	5%	41,386
	(5%)	**15,341**	**(15,341)**	(5%)	(41,386)
EUR	**5%**	**(9,550)**	**9,550**	5%	11,031
	(5%)	**9,550**	**(9,550)**	(5%)	(11,031)
HKD	**5%**	**(21)**	**21**	5%	183
	(5%)	**21**	**(21)**	(5%)	(183)

Results of the analysis as presented in the above table represent an aggregation of the instantaneous effects on each of the group entities' (loss)/profit 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.

30 FINANCIAL RISK MANAGEMENT AND FAIR VALUE (continued)

(d) Currency risk (continued)

Sensitivity analysis (continued)

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 2008.

(e) Fair values

The carrying amounts of significant financial assets and liabilities approximate their respective fair values as at 31 December 2009.

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

30 FINANCIAL RISK MANAGEMENT AND FAIR VALUE (continued)

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

31 COMMITMENTS

(a) Capital commitments

Capital commitments outstanding at 31 December 2009 not provided for in the financial statements were as follows:

	The group	
	2009	2008
	RMB'000	RMB'000
Contracted for	**108,507**	16,558
Authorised but not contracted for	**1,874,335**	786,065
	1,982,842	802,623

31 COMMITMENTS (continued)

(b) Operating lease commitments

At 31 December 2009, the total future minimum lease payments under non-cancellable operating leases are payable as follows:

	The group	
	2009	2008
	RMB'000	RMB'000
Within 1 year	**2,749**	1,666
After 1 year but within 5 years	**4,908**	765
After 5 years	**10,580**	—
	18,237	2,431

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.

32 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, LLC 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 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 subsidiary have equity interest.
HH Egyptian Company	HH Egyptian Company is 50% owned by Honghua Holdings.
Honghua — Ukraine Limited	Honghua — Ukraine Limited is 50% owned by Honghua Holdings.

32 MATERIAL RELATED PARTY TRANSACTIONS (continued)

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

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

	The group	
	2009 RMB'000	2008 RMB'000
Purchases of parts and components		
— Hongtai Company	14,278	26,113
— Chengdu Juzhong Company	398	761
— Luzhou Jianming Company	—	767
— Guanghan Huite Company	773	786
	15,449	28,427
Decoration service received		
— Luzhou Jianming Company	237	—
Sale of drilling rigs, parts and components		
— HH Egyptian Company	13,492	139,279
Payments on behalf of immediate holding company	—	3,554

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.

32 MATERIAL RELATED PARTY TRANSACTIONS (continued)

(b) Balances with related parties

The balances with related parties are unsecured, interest free and have no fixed repayment terms. There was no provision made against these amounts at 31 December 2009 (2008: RMB Nil).

(c) Key management personnel remuneration

Remuneration for the company's directors is disclosed in note 9. Remuneration for other key management personnel of the group is as follows:

	The group	
	2009	2008
	RMB'000	RMB'000
Basic salaries, allowances and other benefits in kind	**1,665**	2,109
Contributions to defined contribution retirement scheme	**47**	39
Discretionary bonus	**1,201**	2,320
Share-based payments	**5,528**	5,713
	8,441	10,181

Total remuneration is included in "staff costs" (see note 7(b)).

33 COMPARATIVE FIGURES

As a result of the application of IAS 1 (revised 2007), *Presentation of financial statements*, and IFRS 8, *Operating segments*, certain comparative figures have been adjusted to conform to current year's presentation and to provide comparative amounts in respect of items disclosed for the first time in 2009. Further details of these developments are disclosed in note 3.

34 IMMEDIATE AND ULTIMATE HOLDING COMPANY

The directors consider the immediate holding company and the ultimate holding company as at 31 December 2009 are Ally Giant Limited ("Ally Giant") and Ample Chance International Limited ("Ample Chance") respectively, which are incorporated in the British Virgin Islands. These entities do not produce financial statements available for public use.

35 SIGNIFICANT ACCOUNTING ESTIMATES AND JUDGEMENTS

Key sources of estimation uncertainty

Note 25 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.

(ii) Impairment of intangible assets and fixed assets

If circumstances indicate that the carrying value of intangible assets and fixed assets 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.

35 SIGNIFICANT ACCOUNTING ESTIMATES AND JUDGEMENTS (continued)

Key sources of estimation uncertainty (continued)

(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 2009, 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.

(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.

36 CONTINGENT LIABILITIES

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 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. 664 of the 728 original investors have agreed to the buy-out arrangement and had accepted payment from Honghua Company. The remaining 64 investors, who, collectively, invested RMB651,385, claimed that they were still shareholders and refused to accept the buy-out arrangement and payment from Honghua Company.

On 11 December 2007, 57 out of the 64 initiated legal proceedings at the Intermediate Peoples' Court of Chengdu City, Sichuan Province (Action No: (2008) Cheng Min Chu Zi No. 53)). The 57 individuals jointed as plaintiffs to the legal proceedings against Honghua Company as the 1st defendant, Honghua Holdings as the 2nd defendant and 14 individuals including Shi Shuming (3rd defendant); Huang Dequan (4th defendant), Li Yan (5th defendant), Wang Yaoxin (6th defendant), Zhou Tao (7th defendant), Wang Wei (8th defendant), Chen Zhenghua (9th defendant), Yang Xuefeng (10th defendant), Yang Yuanchun (11th defendant), Ni Xiurong (12th defendant), Yu Zhenghua (13th defendant), Xing Manrong (14th defendant), Zhi Rongmu (15th defendant) and Liu Chuanjun (16th defendant) as the 3rd to 16th defendants. There are a total of 16 defendants.

The relief sought by the 57 plaintiffs include:

(1) An adjudication by the court that the 592,250 shares held by the 3rd to 16th defendants were actually owned by the 57 plaintiffs, and all the benefits and rights in such equity interests be restored to the 57 plaintiffs and the names of the 57 plaintiffs be entered into the register of members of Honghua Company;

(2) An adjudication by the court that Honghua Company be ordered to pay to the 57 plaintiffs a total sum of RMB296,125, being the 2003 dividends;

(3) An adjudication that the repurchase of the 592,250 shares of Honghua Company be declared null and void;

(4) An adjudication that Honghua Holdings be jointly and severally liable for the above members sought by the 57 plaintiffs and the consequential liabilities thereof, and that Honghua Holdings with Honghua Company be ordered to apply to the relevant Administration of Commerce to register the 57 plaintiffs as shareholders of Honghua Company; and

36 CONTINGENT LIABILITIES (continued)

Dispute with natural persons (continued)

(5) An adjudication that all the defendants be jointly liable for the legal costs arising from proceedings.

On 13 March 2008, Honghua Company received the Supplemental Statement on Amending, Adding and Waiving the Statement of Claims (the "Supplemental Statement") submitted by the 57 plaintiffs. The plaintiffs added the following new claims:

(a) An adjudication that the 1st defendant, 3rd to 16th defendants be jointly liable for the damages of shareholders' right and interests, calculated until the date when the judgment is executed in full, including shareholders' rights for 3,760,379 bonus shares calculated until 30 September 2007, pre-emptive rights, and dividend from 2004 to 2006 in a total amount of RMB1,510,237.50;

(b) An adjudication that the 1st defendant, 3rd to 16th defendants be jointly liable for the damages and costs of RMB228,000 incurred by the plaintiffs arising from these legal proceedings; and

(c) An adjudication that the merger and acquisition of Honghua Company by Honghua Holdings be declared null and void and that Honghua Holdings be jointly liable for all the claims against Honghua Company and other defendants.

Ally Giant, Ample Chance, Wealth Afflux Limited, Mowbray Worldwide Limited, Ecotech Enterprises Corporation, Otama Company Limited, Vast & Fast Corporation, Cavendish Global Corporation, Airtech Investments Limited, Ally Smooth Investments Limited, Charm Moral International Limited, Beauty Clear Holding Limited, Brondesbury Enterprises Limited, Oriental Starz Limited, Tech Express Enterprises Inc, Dobson Global Inc, Darius Enterprises Limited, Believe Power International Limited, Benefit Way International Limited, Birdview Limited and the existing shareholders of the company have executed a deed of indemnity in respect of dispute and risk dated 15 February 2008 in favour of the group under which they agree to jointly and severally indemnify any members of the group for any potential damages that the company may suffer as a result of the legal proceedings initiated by the 57 plaintiffs.

On 17 July 2008, another 2 individuals, Wu Chuan and Gong Yumei refused to accept the buy-out arrangement and payment from Honghua Company. The relief sought is the same as the 57 plaintiffs as mentioned above.

The legal proceedings have been completed on 19 June 2009 and the verdict is yet to be announced up to the date of these financial statements.

The directors, 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, and the directors consider that sufficient provision in legal costs in respect of the dispute has been made as at 31 December 2009.

On 29 March 2010, one of the 64 investors accepted the buy-out arrangement and payment from Honghua Company, who is not a plaintiff to the legal proceedings against Honghua Company.

(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 2009

Up to the date of issue of these financial statements, the IASB has issued the following amendments, new standards and interpretations which are not yet effective for the year ended 31 December 2009 and which have not been adopted in these financial statements.

	Effective for accounting periods beginning on or after
IFRS 3 (revised), *Business combinations*	1 July 2009
Amendments to IAS 27, *Consolidated and separate financial statements*	1 July 2009
Amendments to IAS 39, *Financial instruments: Recognition and measurement — Eligible hedged items*	1 July 2009
IFRIC 17, *Distributions of non-cash assets to owners*	1 July 2009
Improvements to IFRSs 2009	1 July 2009 or 1 January 2010

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

	2009 RMB'000	2008 RMB'000	2007 RMB'000	2006 RMB'000	2005 RMB'000
Consolidated Income Statement					
Revenue	1,961,517	4,737,532	3,164,022	2,335,948	501,570
Cost of sales	(1,443,455)	(3,381,730)	(2,083,888)	(1,558,121)	(392,993)
Gross profit	518,062	1,355,802	1,080,134	777,827	108,577
Other operating revenue	7,085	5,375	22,999	4,620	3,187
Other operating expenses	(803)	(6,970)	(768)	(917)	(648)
Selling expenses	(179,980)	(369,787)	(210,319)	(84,176)	(22,971)
General and administrative expenses	(351,070)	(263,114)	(186,785)	(108,548)	(42,042)
(Impairment losses recognised)/impairment losses written-back on trade receivables	(123,264)	1,907	239	(1,637)	(394)
Other net income	9,234	13,662	22,475	3,085	1,427
(Loss)/profit from operations	(120,736)	736,875	727,975	590,254	47,136
Net finance expenses	(3,709)	(88,701)	(49,927)	(23,141)	(4,132)
Share of (loss)/profit from jointly controlled entities	(4,766)	7,332	6,468	—	—
(Loss)/profit before taxation	(129,211)	655,506	684,516	567,113	43,004
Income tax credit/(expenses)	7,126	(115,560)	(67,511)	(103,203)	(10,749)
(Loss)/profit for the year	(122,085)	539,946	617,005	463,910	32,255
Attributable to:					
Equity shareholders of the Company	(127,337)	511,974	583,235	412,814	18,454
Minority interests	5,252	27,972	33,770	51,096	13,801
Figures per share					
(Loss)/earnings per share (RMB cents)					
— Basic	(4.0)	16.2	23.3	16.5	0.7
— Diluted	(3.9)	16.2	23.3	16.5	0.7
Dividend					
Dividends declared and paid	—	287,671	—	19,533	1,638
Dividends declared and paid per share	—	HK$0.10	—	N/A	N/A
Dividend proposed after balance sheet date	—	170,371	—	—	—
Dividend proposed after balance sheet date per share	—	HK$0.06	—	—	—

FIVE-YEAR FINANCIAL HIGHLIGHTS

	2009 RMB'000	2008 RMB'000	2007 RMB'000	2006 RMB'000	2005 RMB'000
Consolidated Balance Sheet					
Total non-current assets	**1,209,071**	946,480	794,951	286,659	146,634
Total current assets	**5,379,897**	6,837,443	3,136,002	1,895,735	1,022,722
Total assets	**6,588,968**	7,783,923	3,930,953	2,182,394	1,169,356
Total current liabilities	**2,062,235**	3,232,425	2,555,556	1,818,785	1,024,510
Total non-current liabilities	**262,804**	24,090	19,686	25,558	—
Total liabilities	**2,325,039**	3,256,515	2,575,242	1,844,343	1,024,510
Total equity	**4,263,929**	4,527,408	1,355,711	338,051	144,846

	2009 RMB'000	2008 RMB'000	2007 RMB'000	2006 RMB'000	2005 RMB'000
Profitability					
Gross margin	**26.4%**	28.6%	34.1%	33.3%	21.6%
EBITDA margin	**(2.2%)**	16.7%	24.0%	25.9%	11.1%
Net margin	**(6.5%)**	10.8%	18.4%	17.7%	3.7%
Return					
Return on average equity	**(3.0%)**	17.9%	73.3%	203.9%	19.9%
Return on average assets	**(1.8%)**	8.7%	19.1%	24.6%	2.4%
Liquidity					
Current ratio	**2.61**	2.12	1.23	1.04	1.00
Quick ratio	**1.69**	1.49	0.82	0.66	0.71
Turnover					
Turnover of average trade and bills receivable	**217**	105	101	59	117
Turnover of average trade and bills payable	**178**	88	107	81	154
Turnover of average inventory	**498**	166	151	116	176
Gearing					
Total debts/Total assets	**19.7%**	20.2%	22.2%	16.8%	2.7%
Total liabilities/Total assets	**35.3%**	41.8%	65.5%	84.5%	87.6%
EBIT/Interest expenses	**(1.9)**	11.3	18.7	64.6	21.3

Note:

Profitability

Gross margin	=	Gross profit/Revenue
EBITDA	=	(Loss)/profit from operations + Share of (loss)/profit from jointly controlled entities + Depreciation + Amortisation
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 capitalised into assets under construction)

DEFINITIONS

"Ally Smooth"	Ally Smooth Investments Limited (聯順投資有限公司), a company incorporated in BVI with limited liability on 5 July 2006
"Ample Chance"	Ample Chance International Limited (宏機國際有限公司), a company incorporated in BVI with limited liability on 13 July 2006
"Articles of Association"	the Articles of Association of the Company, approved at extraordinary shareholders' meetings of the Company on 21 January 2008, revised and approved at annual general meeting of the Company on 3 June 2009
"Beauty Clear"	Beauty Clear Holdings Limited (俊朗控股有限公司), a company incorporated in BVI with limited liability on 21 July 2006
"Believe Power"	Believe Power International Limited (信力國際有限公司), a company incorporated in BVI with limited liability on 21 July 2006
"Benefit Way"	Benefit Way International Limited (益通國際有限公司), a company incorporated in BVI with limited liability on 7 July 2006
"Board of Directors" or "Board"	the Board of Directors of the Company
"BVI"	the British Virgin Islands
"Cayman Companies Law"	the Companies Law (2009 Revision) of the Cayman Islands
"Charm Moral"	Charm Moral International Limited (德美國際有限公司), a company incorporated in BVI with limited liability on 18 July 2006
"CNOOC"	China National Offshore Oil Corporation (中國海洋石油總公司), a state-owned enterprise established in the PRC on 15 February 1982
"CNOOC Group"	CNOOC and its subsidiaries
"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 17 February 2006
"Controlling Shareholder(s)"	has the meaning ascribed thereto under the Listing Rules being, for the time being, Ally Giant, Ample Chance, Ally Smooth, Beauty Clear, Charm Moral, Believe Power, Benefit Way, 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
"COOS"	China Ocean Oilfields Services (Hong Kong) Limited (中國近海石油服務（香港）有限公司), a company incorporated in Hong Kong with limited liability on 2 April 1982
"Director(s)"	member(s) of the Board of Directors of the Company

"Golden Coast Company"	Honghua Golden Coast Equipment FZE (宏華金海岸設備有限公司), formerly known as Golden Coast Equipment FZE (金海岸設備公司), a company incorporated in the United Arab Emirates with limited liability on 28 November 2006 and a wholly-owned subsidiary of Honghua Holdings
"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
"HH Egyptian Company"	Egyptian Petroleum HH Rig Manufacturing Shareholder Co., a company incorporated in Egypt with limited liability on 24 April 2007 and is held by Honghua Holdings, Petroleum Projects and Technical Consultation Company, Engineering for the Petroleum and Process Industries Company and Tharwa Petroleum Company as to 50%, 25%, 10% and 15% respectively
"HK$" or "HK dollars"	Hong Kong dollars, the lawful currency of Hong Kong
"Honghua America"	Honghua America, LLC, formerly known as New Continental Equipment Co., LLC and as New Continental Equipment Co., Ltd, a limited partnership formed in the State of Texas on 11 October 2004, and converted into a limited liability company on 19 December 2006, and a 80%-owned subsidiary of Honghua Company
"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
"Honghua Holdings"	Honghua Holdings Limited (宏華控股有限公司), formerly known as Asia Harbour International Limited (宏海國際有限公司), a company incorporated in Hong Kong with limited liability on 8 July 2006 and a wholly-owned subsidiary of the Company
"Honghua International"	Honghua International Co., Ltd. (四川宏華國際科貿有限公司), formerly known as Sichuan Honghua Trading Co., Ltd. (四川宏華貿易有限公司), a limited liability company established in the PRC on 13 January 2004, and an 85%-owned subsidiary of Honghua Company
"Hong Kong" or "HK"	the Hong Kong Special Administrative Region of the PRC

"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 21 June 2002
"Hongtian Company"	Chengdu Hongtian Electronic Drive Engineering Co., Ltd. (成都宏天電傳工程有限公司), a limited liability company established in the PRC on 6 June 2001, and an 80%-owned subsidiary of Honghua Company
"Listing Rules"	the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (as amended from time to time)
"Nabors Global"	Nabors Global Holdings Limited, an exempted company organized under the laws of Bermuda on 25 February 2005
"Nabors Group"	Nabors Industries and its subsidiaries
"Nabors Industries"	Nabors Industries Ltd., an exempted company organized under the laws of Bermuda on 11 December 2001, whose shares are listed on the New York Stock Exchange
"Nabors International"	Nabors Drilling International II Limited, an exempted company organized under the laws of Bermuda on 12 March 2003
"Nabors Management"	Nabors International Management Limited, an exempted company organized under the laws of Bermuda on 23 December 2004
"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$0.10 each
"Shareholder(s)"	holder(s) of the Share(s)
"sq.m."	square meters
"Stock Exchange"	The Stock Exchange of Hong Kong Limited
"Substantial Shareholder(s)"	has the meaning ascribed to it under the Listing Rules
"UAE"	the United Arab Emirates
"United States", "USA" or "U.S."	the United States of America, including its territories and possessions
"US$" or "U.S. dollars" or "USD"	United States dollars, the lawful currency of the United States
"Youxin Company"	Sichuan Honghua Youxin Petroleum Machinery Co., Ltd. (四川宏華友信石油機械有限公司), formerly known as Guanghan Youxin Co., Ltd. (廣漢市友信有限責任公司), a limited liability company established in the PRC on 7 August 1998, and an 80%-owned subsidiary of Honghua Company