HONGHUA GROUP LIMITED

宏华集团有限公司

2013 Annual Report

(incorporated in the Cayman Islands with limited liability)

Stock Code: 196

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CONTENTS

CORPORATE INFORMATION

BOARD OF DIRECTORS

EXECUTIVE DIRECTORS

Zhang Mi *(Chairman)*
Ren Jie
Liu Zhi

NON-EXECUTIVE DIRECTORS

Siegfried Meissner
Popin Su
(The alternate director to Siegfried Meissner)
Huang Dongyang
(Resigned with effect from 19 March 2013)

INDEPENDENT NON-EXECUTIVE DIRECTORS

Liu Xiaofeng
Qi Daqing
Tai Kwok Leung, Alexander
(Resigned with effect from 19 March 2014)
Chen Guoming
Shi Xingquan
Guo Yanjun

SECRETARY OF BOARD OF DIRECTORS

Liu Gangqiang
(Resigned with effect from 27 December 2013)
He Bin
(Appointed with effect from 27 December 2013)

BOARD COMMITTEES

AUDIT COMMITTEE

Qi Daqing *(Committee Chairman)*
Liu Xiaofeng
Tai Kwok Leung, Alexander
(Resigned with effect from 19 March 2014)
Chen Guoming
Shi Xingquan
Guo Yanjun

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 Dongyuang
(Resigned with effect from 19 March 2013)
Shi Xingquan
Liu Xiaofeng
(Appointed with effect from 19 March 2013)

CORPORATE GOVERNANCE COMMITTEE (DISMISSED WITH EFFECT FROM 19 MARCH 2013)

Liu Xiaofeng *(Committee Chairman)*
Qi Daqing
Tai Kwok Leung, Alexander
(Resigned with effect from 19 March 2014)
Chen Guoming
Shi Xingquan
Guo Yanjun

NOMINATION COMMITTEE (DISMISSED WITH EFFECT FROM 19 MARCH 2013)

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

JOINT COMPANY SECRETARIES

Liu Gangqiang
(Resigned with effect from 27 December 2013)
He Bin
(Appointed with effect from 27 December 2013)
Corinna Leung

LEGAL ADVISOR

AS TO HONG KONG LAW

King & Wood Mallesons

CORPORATE INFORMATION

PRINCIPAL BANKERS

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

AUDITOR

KPMG
Certified Public Accountants

REGISTERED OFFICE

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

HEAD OFFICE

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

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

CORPORATE PROFILE

1. GROUP PROFILE

WHO WE ARE

The Group is headquartered in Chengdu, Sichuan Province. Its land and offshore equipment production bases are located in Guanghan, Sichuan Province and Qidong, Jiangsu Province, respectively. The Group has set up subsidiaries or joint ventures in the United States, Russia, Egypt, Dubai and also set up a number of sales offices and after-service centers in major oil & gas producing areas such as the Middle East, Central Asia and South America.

Honghua Group is a large-scale equipment manufacturing and drilling engineering service enterprise specialized in the research, design, manufacture and general assembly of oil drilling rigs, offshore engineering and petroleum exploration & development equipment. It is China's largest and the world's second largest land oil drilling rigs and parts and components manufacturer.

In recent years, the Group has annually sold nearly 100 sets of drilling rigs in China and around the world, of which nearly 80% were sold to overseas markets. By the end of 2013, more than 800 sets of drilling rigs produced by the Group had been in use worldwide, including nearly 550 sets used in overseas countries. The Group has comprehensively promoted the upgrade of global land drilling rigs.

The Group boasts of China's largest land drilling rig production base with an annual production capacity of 150 sets of various drilling rigs, 600 drilling pumps and 80 sets of top drives. Meanwhile, the Group is building China's largest offshore equipment production base. Upon completion of the first phase of the project, it will have an annual production capacity of 10 sets of jack-up platforms.

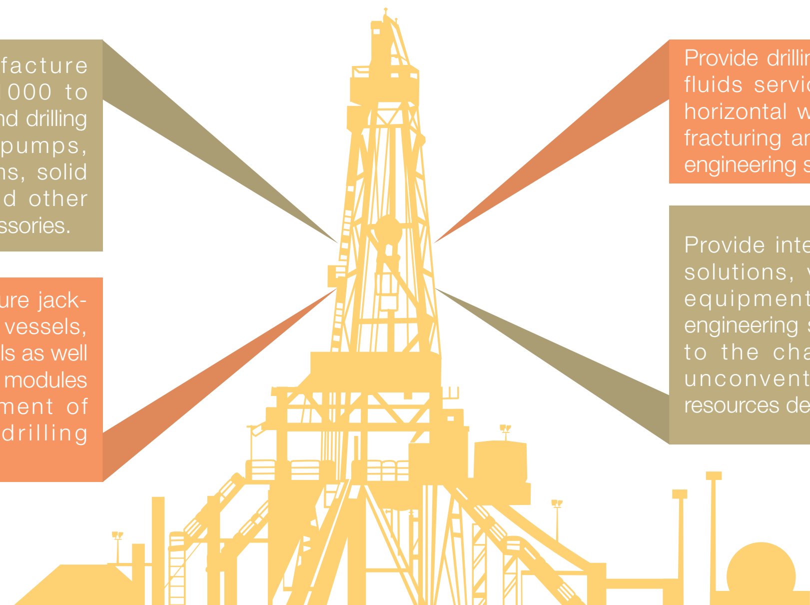
By the end of 2013, the Group had a total of 7724 employees.

The Group has a high-quality research and development ("R&D") team comprising of about 600 professionals. Till now, it has possessed a number of products with proprietary intellectual property rights.

WHAT WE DO

Design and manufacture various types of 1000 to 12000-meter-depth land drilling rigs and ancillary pumps, electric drive systems, solid control systems and other components and accessories.

Design and manufacture jack-up platforms, drilling vessels, offshore support vessels as well as the offshore drilling modules and related equipment of various offshore drilling platforms.

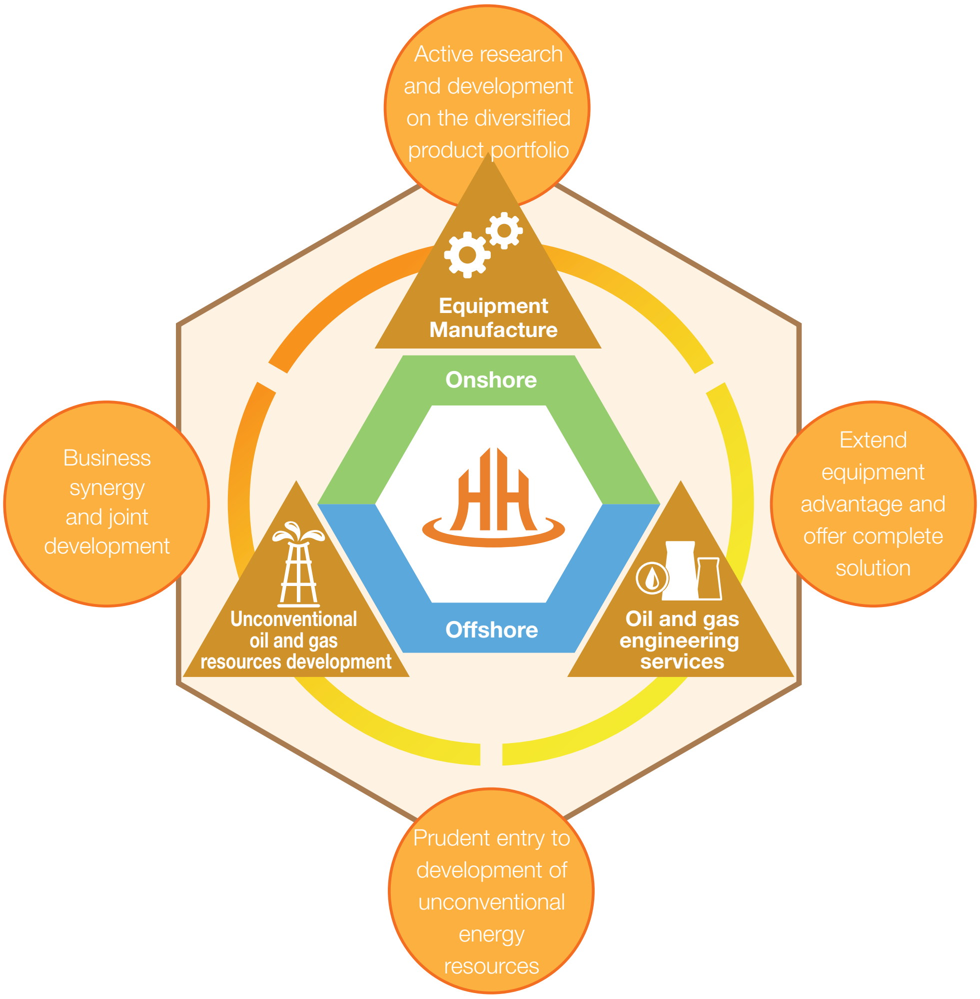


Provide drilling services, drilling fluids services, vertical and horizontal well services, acid fracturing and other oil & gas engineering services.

Provide integrated complete solutions, various featured equipment and oil & gas engineering services according to the characteristics of unconventional oil & gas resources development.

CORPORATE PROFILE

2. STRATEGIC MODEL: A "THREE SECTORS, TWO FIELDS" SYNERGY STRATEGIC MODEL



After 15 years of development, Honghua Group has gradually realized that the land drilling equipment business has been mature. In order to maintain its booming development, the Group must keep developing new businesses and exploring new markets within the oil & gas industry. After careful consideration, the Group's management team is convinced that offshore oil & gas resources and unconventional oil & gas resources will become the new growth drivers of oil & gas resources in China in the future. Meanwhile, the demand for private oil & gas engineering services in China will also keep growing as the marketization process advances. Therefore, since the Company was listed in the stock market in 2008, its management team has placed its emphasis on the above three emerging strategic sectors. In 2013, through the tough efforts of the Group's management team, the Group has basically completed a diversified development strategic layout which features three sectors — "equipment, services, unconventional oil & gas resources development" — and two fields — "onshore and offshore". The offshore sector will make use of abundant experience in producing drilling modules to produce its self-made offshore drilling platforms and to provide integrated turnkey services to customers. By relying on the self-made high-end drilling equipment of Honghua, the oil & gas engineering service sector provides customers with high-efficiency, high-quality integrated drilling engineering services; meanwhile, the sector also bears the responsibility to test new land drilling products and offer new concepts and ideas for developing land drilling equipment. Relying on its advantages in land drilling equipment and oil & gas engineering services, Honghua can provide customers with integrated solutions for unconventional oil & gas development. Meanwhile, the promotion of its solutions can also boost the sales of the Group's land equipment and oil & gas engineering service.

CORPORATE PROFILE

3. CORPORATE CULTURAL CONCEPT: "INNOVATION, ORIGINALITY, LARGENESS, WISDOM, MANUFACTURE"

Honghua's corporate cultural of "innovation, creation, harmony and progress" contributes a lot to the rapid development of the Group in the past 15 years. As Honghua enters a refreshing decade of development, shall we continue to challenge ourselves and create another miracle or shall we maintain current status and become complacent. Ambitious Honghua people choose the former. According to the long-term strategic plan of Honghua, strategic business sectors like offshore engineering, oil & gas engineering services and unconventional oil & gas resources will provide the Group a vast arena over the next five to ten years. The larger the stage, the more critical the corporate cultural concept for guiding the Group's development is. To this end, on the base of Honghua's development goals in the next decade, the Group's management team puts forward a new corporate cultural concept of "innovation, originality, largeness, wisdom, manufacture". Seemingly simple, the five words contain profound meanings.

Innovation means that in the next decade, the Group will not only keep making innovations in products and technology but also focus on innovations in its business model and business philosophy.

Originality refers to creative ideas, imaginations and concepts. The Group will not only emphasize the sophistication of its products but pursuit of the conceptual design and originality of products.

Wisdom refers to intelligence, mainly referring to enhancing the intelligent level of products. Wisdom needs arenas, frequent application, initiative, broadness and motivation.

Manufacture means that the industry needs manufacturing, which is the source of Honghua's profits and the carrier of the above four concepts. Products manufactured by Honghua should be labeled with "excellent process" and "quality guaranteed".

Largeness has a profound meaning. "Largeness" refers to the large volume and powerful performance or functionality of Honghua products. "Largeness" also refers to the broad scope of ideas, vision and ideals. It determines the width and depth of Honghua's future development. "Largeness" also refers to its inclusiveness, including its inclusiveness to competitors and the integration and fusion of advanced technologies of various industries. "Largeness" can also refer to magnifying the industry through the enlargement of thinking.

The new corporate cultural concept of "innovation, originality, largeness, wisdom, manufacture" is the source for all business sectors to achieve another leap in the future and is the driving force for Honghua to achieve take-off in the next decade. It is also the cornerstone for Honghua to improve its global competitiveness, enhance its brand image and become a pioneer in "Chinese intelligent manufacturing".

4. THE 2013 ANNUAL REPORT — 5-MINUTE REVIEW OF THE ANNUAL REPORT

The land sector:

- The "Localization" and "forward sales strategy" have proved significant effects. As of the end of December 2013, the accumulative newly signed land drilling rig orders totaled 75 units, worth about US$890 million.
- The sale of mud pumps alone reached 109 units.
- As of the end of December 2013, the accumulated new trading orders of the parts and components valued approximately US$425 million.
- Invested about RMB128 million in aggressive production capacity expansion.

The offshore sector:

- Base construction: Dock basin project has passed the inspection acceptance, and the main girder assembly work of No.1 machine of "Honghai Crane" has been successfully completed. The target completion date of the overall elevation of No.1 machine will be completed in May 2014, the overall elevation of No.2 machine will target to be completed in the end of 2014 and the delivery of the whole machine is scheduled to be completed in early 2015.
- On the production side, about 80% of the first set of the Tiger project has been completed, and about 40% of the second set has been completed. As for the PSV vessel project, the production of coating and inner member axles was almost completed. The main hull of vessel was formed, and it is expected that the vessel will be launched into water in May 2014 and delivered in September.

Oil & gas engineering service sector:

- As of the end of December 2013, the sector had 23 drilling services teams, about 30 drilling fluids service teams and 10 directional drilling services teams, and a total of about 1,300 oil & gas engineering service staff.
- After entering Xinjiang, Northeast China and Iraq in 2012, the sector successfully expanded domestic markets in Yumen, Yan'an and Yibin as well as Iraq's West Qurna in 2013.
- As of the end of December 2013, the number of wells drilled by the sector had reached up to 69, including 2 horizontal wells and 22 directional wells, and their total drilling footage had reached 213,000 meters.

Shale gas sector:

- A total of 25 units of flexible water tanks have been sold out.
- The sector has finished the joint commissioning of the 6000HP fracturing pump in the factory and is now planning an on-site industrial test in the United States.
- The sector has completed the trial manufacture of its self-developed electric frequency-conversion blender truck.

Total revenue
8.047
billion RMB

Gross profit
1.905
billion RMB

Earnings attributable to equity shareholders of the Company
538
million RMB

Dividend per share
6
HK cents

Total assets
14.23
billion RMB

Cash and cash equivalents (As at 31 December 2013)
1.275
billion RMB

FINANCIAL HIGHLIGHTS

	2013 RMB'000	2012 RMB'000	Changes
Operating results			
Turnover	8,047,108	5,068,447	58.8%
Profit from operations	848,366	672,693	26.1%
Profit before taxation	701,000	709,458	(1.2%)
Profit attributable to equity shareholders of the Company	537,617	529,458	1.5%
Figures per Share			
Earnings per Share-Basic (RMB cents)	16.99	16.58	2.5%
Earnings per Share-Diluted (RMB cents)	16.77	16.54	1.4%
Financial position			
Total non-current assets	4,548,371	3,227,901	40.9%
Total current assets	9,680,684	6,617,975	46.3%
Total assets	14,229,055	9,845,876	44.5%
Total current liabilities	7,761,845	4,517,478	71.8%
Total non-current liabilities	1,508,564	739,671	104.0%
Total liabilities	9,270,409	5,257,149	76.3%
Total equity	4,958,646	4,588,727	8.1%
Key financial ratios*			
Gross Margin	23.7%	34.5%	(10.8%)
Net Margin	6.7%	10.4%	(3.7%)
Return on average assets	4.5%	6.4%	(1.9%)
Return on average equity	11.7%	12.4%	(0.7%)
Current Ratio	1.25	1.46	(0.21)
Quick ratio	0.89	0.86	0.03
Total debt/Total assets	33.3%	20.1%	13.2%
Total liabilities/Total assets	65.2%	53.4%	11.8%

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

CHAIRMAN'S STATEMENT

CHAIRMAN'S STATEMENT

DEAR SHAREHOLDERS,

In the 2012 Annual Report, I have stated that based on on-hand sales orders and market trend, our 2013 business target was to achieve sales revenue of RMB10 billion. However, as affected by the postponement of some projects and uncommitted offshore agreement, though our revenue recorded a strong growth in 2013 and yet it did not achieve the target that we made at the beginning of the Year.

FINANCIAL HIGHLIGHTS

During the Year, the Group's revenue amounted to approximately RMB8.047 billion, representing a significant increase of 58.8% as compared to Last Year; the gross profit amounted to approximately RMB1.905 billion, representing an increase of 9.1% as compared to Last Year. Profit attributable to equity shareholders amounted to RMB538 million, an increase of 1.5% compared to Last Year.

DIVIDEND

The Board proposed to pay a final dividend of HK6 cents per Share, subject to approval of the shareholders of the Company at the forthcoming annual general meeting of the Company. The final dividend is payable on or around 18 June 2014 to shareholders of the Company whose names appear on the register of members of the Company as on 4 June 2014.

BUSINESS REVIEW

The year 2013 was a challenging one for the Group. While we will describe detailed performance of the business sectors in the section of Management Discussion and Analysis, I would like to represent 2013 highlights and future prospects in the Chairman's Statement.

- ***Opportunities and Challenges for NDC Project*** — At the end of 2011, we entered into a large-scale sales agreement of 7 sets of 9,000 meters cluster land drilling rigs which worths approximately US$300 million with National Drilling Company ("NDC"). It's our first time to tap into the high-end market in the Middle East. We were cheered but also faced with great challenges. The project's drilling rigs are huge amongst the existing land drilling rigs, with the well site area covering two standard wells and the construction period last for two years. They are drilling rigs with the largest numbers of imported components, the largest scale of debugging and the highest quality standards ever for the Group. The beginning was difficult since it was the first time for the Group to build such high-end drilling rigs. We faced obstacles in every step from foreign equipment's installment and debugging to delivery and inspection. In the construction process, we made continuous efforts and obtained experience

CHAIRMAN'S STATEMENT

gradually. We took 60 days debugging for the seventh drilling rig, while it took 217 days to debug the first one. We achieved significant improvements in working efficiencies such as having high-efficient organization and communications, as well as optimization of construction debugging procedure. In addition, we carried on the continuous shift work in 2013 to speed up the delivery and reduce the occupation of production capacity. Through our hard work, we successfully delivered five drilling rigs and completed final assembly of the remaining two by the end of 2013. Despite the delay, we are pleased that the clients were very satisfied with the quality of the first batch of drilling rigs. They purchased additional two sets of the same type drilling rigs and offered us a higher price as well as better payment terms. Through this project, we not only optimized the construction procedure system of high-end drilling rigs, but also achieved our strategic target of building our reputation in the Middle East market.

- ***Unconventional Gas drilling services project in Sichuan Province*** — In 2013, the Group's oil and gas engineering services team successfully developed unconventional oil and gas engineering services market. In 2013, Honghua Oil & Gas Engineering Services Co., Ltd completed drilling services and drilling fluids services for the first unconventional gas well in Sichuan Province. The Group succeeded in overcoming obstacles including possible incline, leakage on the target layer, and hydration, peeling off and collapse problems of long displacement, by applying rotary steering, oil-based drilling fluids system, geosteering -while-drilling, bits optimization and selection as well as other advanced techniques and methods. Meanwhile, the Group has significantly improved its well productivity and completed well path control on accretion and horizontal layers within only 22 days, hitting a new record for the exploration of unconventional gas in China. The Group completed the whole project in 90 days including simultaneously drilling, measuring and casing with well cementation and path qualified. Upon completion, the well has been drilled to a depth of 4,115 meters, the horizontal shift in the bottom is 1,728 meters and the length of horizontal segment is 1,350 meters. Based on the successful completion of the project, the Group made an in-depth summary and started to optimize the techniques for subsequent wells drilling and laid solid foundation for developing unconventional oil and gas drilling market.

- ***Honghua Offshore*** — In 2013, Honghua Offshore was yet to make strategic breakthroughs. Although the construction of Honghai Crane and Shipping Basin as well as other on-hand projects were progressing smoothly, we still have not reached the order agreement regarding the first offshore drilling platform due to certain factors. The project is currently under negotiations with customers. Nevertheless, we feel confident to step forward in this direction in 2014, backed by the positive industry market, the offshore strategies in China, as well as our years of preparation and the strict standards for selecting orders.

CHAIRMAN'S STATEMENT

- ***The shale gas industry is prospective with strong sales of shale gas feature equipment*** — The Group's worldwide initiative flexible water tanks provide four times the volume of water of a traditional tank but occupy only a quarter of area. The flexible water tanks can be foldable for removal and transportation. The volume of six sets of flexible water tanks can meet the water demand of 30 conventional tanks under the conventional fracturing work. The patented product won the "Outstanding Innovation Award" at the Portland Oil and Gas Exhibition and Technology Seminar in 2012, and was highly appreciated by the customers during the well-site tests organized by Shell. After continuous promotion for one year, the product achieved total sales of 25 sets in the second half of 2013.

  In addition, we are encouraged to see a positive development trend in China's shale gas industry. From the issue of the Policies for Shale Gas Industry by the National Energy Administration in 2013 to the National Energy Working Conference held in the beginning of 2014, the central and local governments are vigorously promoting the progress of the exploration of shale gas. On one hand, the government encourages private companies and local enterprises located in shale gas areas to involve in the exploration and development of shale gas; encourages provincial enterprises, local companies and private companies to establish joint ventures with China National Petroleum Corporation ("CNPC") and Sinopec. On the other hand, the government supports the setting-up of shale gas equipment system which is applicable to Chinese market, and encourages enterprises to carry out the integrated application of shale gas exploration technologies, explore factory operation model, reduce the occupied area in the process of drilling and fracturing, improve the recycling of drilling fluid and water resource, utilize the nearest shale gas and access to pipelines network. The policies are all favorable to the Group's future development and some of the models fit well with our integrated solutions guided by "Prioritizing distribution network, exploiting gas by using gas while simultaneously producing gas and electricity in an industrialized, assembly line operation format". In addition, CNPC and Sinopec recorded good exploration performance in Sichuan Basin which has the most abundant shale gas in China, at a lower exploration cost of a single well compared with the initial exploration cost of shale gas. All of these have signified that Chinese companies have advanced shale gas exploration technology and matured experience and are expected to step forward to the large-scale development phase.

OUTLOOK FOR 2014

Given that Last Year's business target was not achieved, my management team and I have been thinking about how to adjust Honghua's development strategy and business plan for 2014, in order to ensure the steady development of the Group and create highest value for the Shareholders and investors.

CHAIRMAN'S STATEMENT

Since 2010, the Group has put forward a strategic model of the synergized and mutually complementary development of its onshore and offshore fields, with equipment, services and unconventional oil and gas resources as three core sectors. Looking backward, the onshore sector still keeps industrial leading advantages and in 2014 we will secure market share with innovative and quality products and keep seeking breakthroughs in new markets, new products and new business models. The performance of the service sector has exceeded our expectation — in 2014 we will increase the operational proportions in unconventional gas and oil service business and overseas market while maintaining the rapid development path of drilling, fluids, directional, horizontal business. As for the unconventional oil and gas business particularly in shale gas, the Group continued to invest in the R&D of new equipment and services, and was highly recognized by a large number of leading enterprises in the industry. In 2014, when the doors of shale gas industry is seriously opened to private companies, we believe that Honghua will be one of the enterprises best preparing for it. As for the offshore sector, we had adequate preparations over the past few years and accomplished things that most people in this industry never dare to try or imagine and to this end, we also suffered many difficulties. For this year, achieving strategic breakthroughs of offshore sector will be of our first priority.

ACKNOWLEDGEMENT

I would like to thank and express my deepest gratitude to our Shareholders, investors, customers and friends from all walks for their long-term support to Honghua and to all the Directors and staff for their devotion and contribution to the Group's long term steady development. We will strive to create better results in 2014 and bring greater returns to our Shareholders.

Zhang Mi
Chairman
19 March 2014, Hong Kong

MANAGEMENT DISCUSSION AND ANALYSIS

MANAGEMENT DISCUSSION AND ANALYSIS

HONGHUA'S LONG-TERM STRATEGY

For initial period of fifteen years, Honghua has grown out of nothing and developed from a single business to a diversified business under the guidance of "Innovation, Creation, Harmony and Aggressiveness". In the next ten years, Honghua will aim to achieve synergized and mutually complementary development of its onshore and offshore fields, with equipment, services and unconventional oil and gas resources as three core sectors. Through continuously improving its production techniques and manufacturing technology in line with the principle of "Creative Manufacturing", the Group strives to be the global leading "Chinese creative manufacturer" in the industry.

EQUIPMENT BUSINESS

As for the onshore equipment business, the Group will continue to satisfy the needs of customers and diversify its product range in order to secure its domestic and overseas markets and win more high-end customers and expand its global market share. Through creative manufacturing, the Group will make continuous effort in advancing technological innovation and industrial upgrade of land drilling rigs and the components and parts, and striving the development of onshore equipment towards more intelligent, lightweight, portable and environment-friendly. Meanwhile, the Group also actively explores various business models and innovative business ideas to seek development opportunities for the onshore equipment business. As for offshore equipment business, the Group will keep track of market trends and provide a variety of high-quality offshore oil and gas equipment to domestic and overseas customers based on the innovative concept of "onshore manufacturing of offshore platform", within shorter construction period and lower cost.

OIL AND GAS ENGINEERING SERVICES BUSINESS

As for oil and gas engineering services business, the Group will rely on its self-innovated equipment in its drilling and drilling fluids services, and expand to other services areas such as well cementation and well completion business to provide integrated service solutions for customers. In addition, through having an interactive development of onshore equipment business and oil and gas engineering services business, the Group continues to strengthen its leading position in research and development of equipment and expand its competitive edge in oil and gas engineering services business.

UNCONVENTIONAL OIL AND GAS RESOURCES BUSINESS

As for unconventional oil and gas resources business, the Group will continue to popularize a complete set of solutions guided by "Prioritizing distribution network, exploiting gas by using gas while simultaneously producing gas and electricity in an industrialized, assembly line operation format", and seize development opportunities for unconventional oil and gas from the three core pillars of equipment, services and resources.

MANAGEMENT DISCUSSION AND ANALYSIS

KEY CUSTOMERS

Regular Customers	New Customers
Eurasia Drilling Company, NDC, Kuwait Drilling Company, PDVSA Servicios Petroleros S.A etc.	Weatherford, NDSC, ABRAJ, GEOTHERMAL DEVELOPMENT COMPANY etc.

2013 BUSINESS REVIEW

ONSHORE EQUIPMENT BUSINESS

In 2013, the Group strengthened the publicity and promotion of Honghua new products, initiatives, concepts and branding in line with the principle of "Creative Manufacturing". In regard of the overseas market, the Group continued to adopt its localization strategy and rely on overseas subsidiaries to explore new markets and clients while securing the customers in the existing markets and achieved outstanding results. As for the domestic market, the Group adopted "Forward-sales" strategy, actively collected market information, visited clients and achieved satisfactory sales.

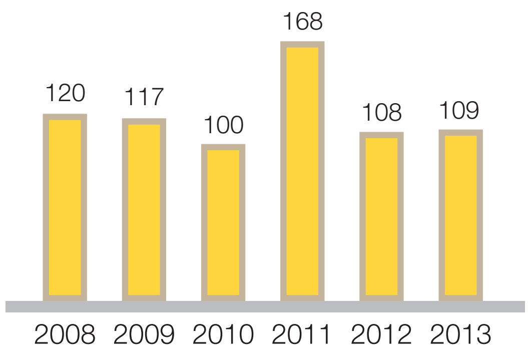
In terms of land drilling rigs sales business, in the European and Asian markets, the Group successfully entered into a renewed sales agreement of 14 sets of drilling rig which worths US$218 million with Eurasia Drilling Company, and a sales agreement of 4 sets of drilling rig which worths US$20 million with Weatherford. In the Middle East, the Group entered into a sales agreement of 2 sets of 9000-meter cluster land drilling rigs which worths US$135 million with NDC and a sales agreement of 3 drilling rigs which worths US$40 million with Kuwait Drilling Company. The Group also successfully penetrated into the Oman market and entered into a sales agreement of 6 drilling rigs which worths US$90 million with NDSC and ABRAJ drilling company as well as another sales agreement of 1 1000HP land drilling rig with ABRAJ drilling company in early 2014. In the American market, the Group entered into a renewed sales agreement of 3 training drilling rigs and a sales agreement of 4 150HP tractor hoists with PDVSA Servicios Petroleros S.A., and besides that, the Group also penetrated the Colombian market by entering into a sales agreement of 1 350HP training drilling rigs with Ecopetrol, equipped with a self-developed top-drive. In the African market, the Group established robust sales channels through three-year sales distributions and finally squeezed into the Kenyan market by signing a sales agreement of 3 drilling rigs which worths US$64 million with Geothermal Development Company. In the domestic market, the Group focused on the needs of private enterprises and also made effort to expand its business into national oil and gas market, for example, by obtaining a sales agreement of 7 drilling rigs which worths US$60 million from CCDC. By the end of December 2013, the Group had obtained new sales agreements of 75 sets, amounting to approximately US$890 million throughout the year.

MANAGEMENT DISCUSSION AND ANALYSIS

In terms of parts and components sales, the Group recorded individual sales of 109 sets of mud pump throughout the year of 2013. In addition, the Group's self-innovated new energy-saving quintuple mud pump also successfully achieved sales and obtained a sales agreement of 3 sets from Trinidad Company. The Group also recorded sales of mud pump in the Mexican market. As for trading business of parts and components, from 2013 onwards the Group actively made full use of its global procurement network and customer resources to provide integrated procurement services for its clients. In 2013, the Group entered into directional drilling equipment trading sales agreement which worths US$187 million with PDVSA Servicios Petroleros, S.A. and a renewed sales agreement of maintenance machinery for directional drilling equipment which worths US$12 million in December. In early 2014, the Group signed a renewed sales agreement of 64 sets of transportation and hoisting equipment which worths US$17 million with PDVSA Servicios Petroleros, S.A.. As at 31 December 2013, the Group's accumulated new trading orders of the parts and components valued approximately US$425 million throughout the year.

The year of 2013 was a tough year for Honghua despite of a good sales performance. In the beginning of 2013, the Group had plenty of orders, including projects from National Drilling Company that utilised a lot of production capacity. In order to deliver the products on time with quality and quantity guaranteed, our staff worked on two or three shifts and worked overtime to complete the production tasks. The Group's subsidiaries including Honghua Offshore Oil & Gas Equipment (Jiangsu) Co., Ltd. and Gansu Hongteng Oil & Gas Equipment Manufacturing Co., Ltd. also allocated some of their capacities to assist in manufacturing certain components and parts of land drilling rigs. Besides that, the Group started to streamline its production and further improve its production processes such as procurement, manufacturing, assembling, testing and logistic processes. The Group also invested RMB128 million in the expansion of production capacity.

HISTORICAL SALES OF MUD PUMPS



MANAGEMENT DISCUSSION AND ANALYSIS

OFFSHORE EQUIPMENT BUSINESS

2013 was a year with tough tasks for Honghua offshore equipment business. In terms of offshore base construction, the 150-meter-long and 110-meter-wide dock basin project was inspected and accepted by the Port Engineering Quality Supervision Station, Water Affairs Department and Fire Department of Nantong City on 10 January 2014. Meanwhile, the foundation of 400 tons gantry crane rail, the delivery and assembly site with an area of around 40,000 square meters, the revetment and flood protection system engineering as well as pipe trench, dynamic electricity and water supply and drainage system in the related areas were all completed. The construction process of Honghai Crane, the core equipment enshrining the innovative concept of "onshore manufacturing of offshore equipment", is progressing as planned, with main girder of the first crane closed. It is expected that the overall lifting of the equipment will be completed in May 2014. The installation work of 1,200 tons cantilever crane was 80% completed. The cantilever crane is expected to be welded with the main girder in the beginning of April 2014. The installation of the second crane will be commenced after the completion of the first crane, with an expectation that the overall lifting will be completed by the end of 2014 and the equipment will be delivered in early 2015.

"HONGHAI CRANE" AND DOCK BASIN

In terms of production, the Tiger project of offshore drilling package was processed as scheduled. The main parts of the first set were delivered to Shanghai shipyard; the installation was commenced and completed about 80%. The production of second crane and the member axles were completed and most axles were installed for delivery. As for the project of PSV vessel, the production of coating and inner member axles was almost completed. The hoisting and installation of warehouse segment of PSV vessel was completed, the pipe system and electric outfitting operation was in progress. The main hull of vessel was formed and expected to be launched in May 2014 and delivered in September 2014.

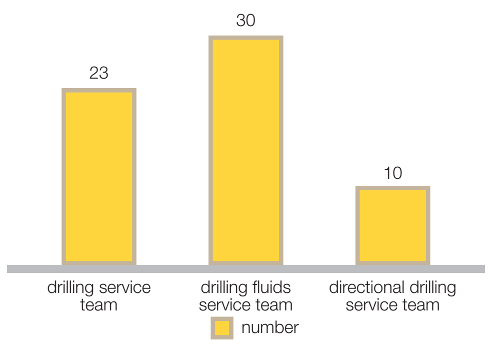
MANAGEMENT DISCUSSION AND ANALYSIS

As for marketing development, the Group actively promoted the innovative construction model of "onshore manufacturing of offshore platform" via attending international exhibitions such as the Offshore Technology Conference ("OTC"). Meanwhile, the Group proactively participated in a variety of tenders for offshore platform and accessory equipment projects in the domestic and overseas markets. During the Year, the Group communicated with prospective customers for a long time, while the first order agreement of offshore drilling platform was still not reached due to many factors. Nevertheless, the Group has gained customers' confidence in its creative manufacturing model and product quality.

OIL AND GAS ENGINEERING SERVICES BUSINESS

In 2013, Honghua's oil & gas engineering service business achieved rapid growth. In terms of service teams building, the Group expanded the scale of drilling service teams, established directional service teams and developed business lines in accordance with the domestic and overseas market trends and specific project status. In the first half of 2013, the Group successfully introduced drilling and fluids services into Honghua's domestic oil services projects in all regions to achieve the business collaboration through acquisition of Bazhou Honghua Petroleum Applied Chemistry Co., Ltd.. As at the end of December 2013, the Group had 23 drilling service teams, 30 drilling fluid service teams and 10 directional services teams. The staff of Honghua's oil & gas engineering services reached around 1,300.

TEAM SCALE



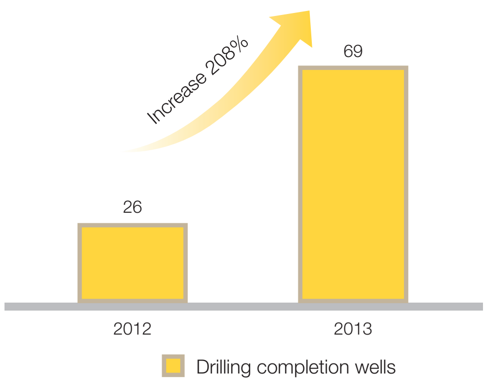
(By the end of 2013, the staff of Honghua Oil and Gas Engineering Services reached around 1,300.)

In terms of market expansion, after entering into Xinjiang, the northeastern China and Iraq in 2012, the Group successfully developed domestic markets in Yumen and Yan'an as well as West Qurna market in Iraq. In terms of business expansion, the Group started the first expansion step from conventional service to unconventional service. In 2013, Honghua's oil & gas engineering services finished the drilling services and drilling fluids services for the first unconventional gas wells in Sichuan province in the PRC. Before drilling, the Group studied geological structure carefully and developed strategies by segments. For possibly inclining top layer, motor and measurement-while-drilling systems were utilized to better control the well deviation. For the problem of carbonate formation leakage in the upper layer of the Permian system and frequent leakage in many locations, the Group adopted the method of "controlling leakage while drilling" and saved a lot of time on stopping the leakage. The Group overcame obstacles including hydration, peeling off and collapse problems of long displacement

MANAGEMENT DISCUSSION AND ANALYSIS

through applying oil-based drilling fluids system and introducing rotary steerable drilling technology which not only helped solving the problems arising from the big drag pressure of conventional motor drilling but also performed good well trajectory. After 90 days of hard work, the Group finally completed the well drilling. Upon completion, the well was drilled to a depth of 4,115 meters. The horizontal shift at the bottom is 1,728 meters and the length of horizontal segment is 1,350 meters. The success of this project laid a sound foundation for Honghua to further tap into the shale gas services market.

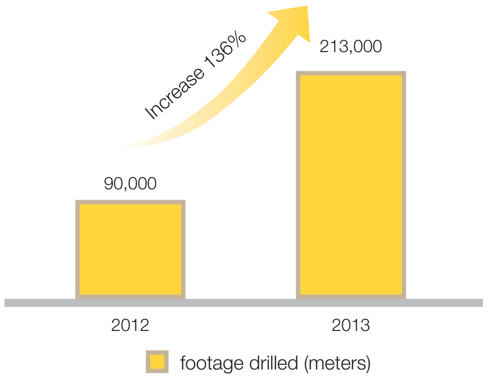
HISTORICAL NUMBER OF DRILLING COMPLETION WELLS



As for operation efficiency, with the accumulation of experience and ongoing technology innovation, the operation efficiency for oil and gas engineering were steadily improved continuously. For example, No. 1 drilling service team in Turpantte area completed 21 wells and reached a depth of 32,000 meters. It is the third drilling service team that drilled the depth of more than 30,000 meters followed the Western drilling team and the Bohai drilling team in Yudong area; it is also the only private drilling service team that achieved the depth of more than 30,000 meters in Turpan oilfield. Another example is the No. 15 drilling service team in Yumen area. Despite of the complex topography of contracted Ya well K1-29 (possible inclining, grinding, breaking, bouncing and changes), No. 15 drilling service team completed the entire drilling tasks within 45.5 days, achieving an advanced level of quick drilling in Ya Area K and setting a new record of quick drilling in this area. As at the end of December 2013, the Group completed a total of 69 wells, including 2 horizontal wells and 22 directional wells, and achieved 213,000 meters of footage drilled.

UNCONVENTIONAL OIL AND GAS RESOURCES BUSINESS

HISTORICAL FOOTAGE DRILLED



In 2013, on the basis of the successful completion of the first shale gas drilling service project, the Group also achieved sales of 25 sets of self-innovated flexible water tanks. In addition, the Group's 6000HP fracturing pump completed the single-machine commissioning test witnessed by Baker Hughes' experts; it is currently in the process of planning for an on-site industrial test at a shale gas fracturing site in America. The completion of the test laid a solid foundation for product sales both in the domestic and overseas markets. Meanwhile, the Group completed the trail production of prototype and started on-site test for the self-innovated electric fracturing blender trucks during the Year.

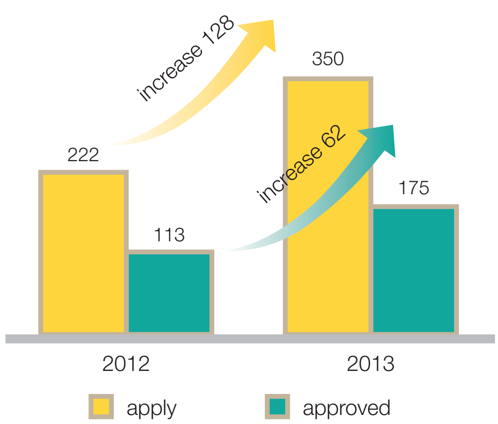
MANAGEMENT DISCUSSION AND ANALYSIS

QUALITY DEVELOPMENT AND RESEARCH & DEVELOPMENT

In 2013, the Group enhanced the building of quality management system and strengthened application for various types of qualifications. As for the land business sector, Sichuan Honghua Petroleum Equipment Co., Ltd, the Group's main production base, successfully passed the triennial recertification review of the American Petroleum Institute (API). In addition, Honghua Golden Coast Equipment FZE, the Group's overseas subsidiary, also obtained in its own API certificate and other certificates such as ISO 9001:2008, ISO/TS 29001, etc., which laid an important foundation for sales to the high-end customers in the Middle East. Gansu Hongteng Oil & Gas Equipment Manufacturing Co., Ltd. received certificates of API and prepared for developing the product series of fracturing truck into international markets. As for the oil and gas engineering services, during the Year, the Group obtained many qualifications such as the certificate from Sinopec Northeast Petroleum Administration Bureau and access certificate for western drilling market. As for the offshore engineering equipment services, the Group successfully obtained certificates of OHSAS18001:2007, ISO9001:2008 and ISO14001:2004 issued by ABS QE and built a scientific and perfect QHSE Management System.

As for the product research & development, the Group continuously optimized and improved the series of top drive, quintuple mud pump and other products during the Year. Meanwhile, with the highly mechanized and automated "next-generation drilling rigs" as the mainstay, the Group continued to integrate new technology on new equipment (e.g. drilling rig of "Honghua America I" and rack and pinion drilling rigs) and drove the R&D of automatic machines. In 2013, the Group invested RMB91 million in R&D and achieved remarkable result. As at 31 December 2013, the Group has applied for 350 patents, of which 175 were approved.

PATENTS APPLY AND APPROVED

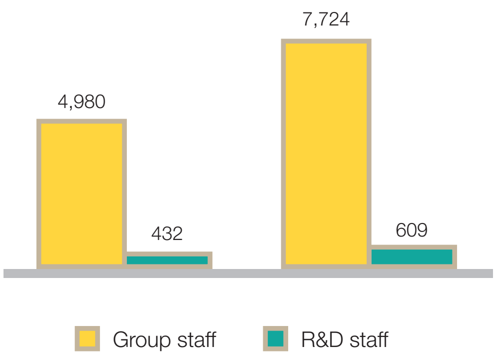


MANAGEMENT DISCUSSION AND ANALYSIS

HUMAN RESOURCES MANAGEMENT

According to Honghua's long-term development plan, Honghua's human resources function has always been considering how to raise and realize the professional value of human resources and provide effective supports to the strategic development of all its subsidiaries. During the Year, the Group's strategy of driving human resources ahead moderately reserved various types of talents of different levels. The Group recruited 3,251 staff and 345 of them are fresh graduates from renowned universities. Apart from new staff recruitment, the Group puts focus on the trainings for current employees. In 2013, the Group arranged 942 training programs including trainings for specialized competence of each system module, with an aim to enhance employees' specialized knowledge and technical skills as well as to improve efficiency. As at end of 2013, the Group had 7,724 employees, among which 609 are research personnel.

NUMBER OF STAFF



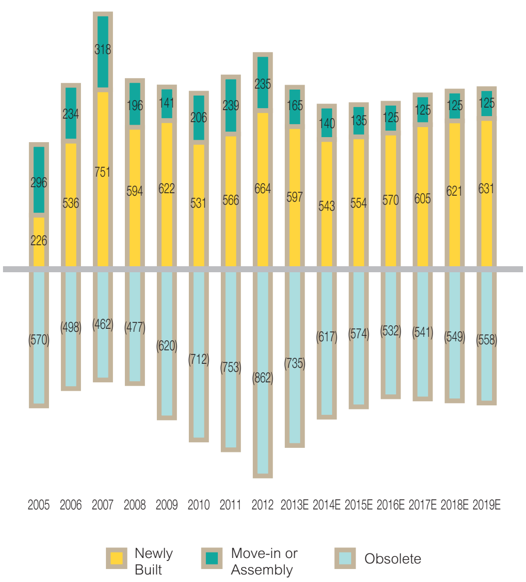
OUTLOOK FOR 2014

According to the forecast of the securities firms, in the coming years, the oil price will remain at a high level at US$90 per barrel. The high oil price will cause the capital expenditure on exploration of the major oil and gas companies to grow continuously, increasing the demand for oil and gas drilling equipment and services.

ONSHORE EQUIPMENT BUSINESS

According to latest report of Spears & Associates, in the coming years, the global annual demand for complete set of land drilling rigs will remain in the range of 500-600 units. The demand will mainly come from the new additions of drilling wells, the replacement of old drilling rigs, and the upgrade of drilling rig technology. Meanwhile, the service life of the parts and components of land drilling rigs is much shorter than that of the drilling rig main engines, and the subsequent demand for replacement is increasingly strong. In addition, due to the increasing depth and difficulty of the drilling wells, a growing number of drilling rigs require higher-end parts and components, such as more advanced top drives. Therefore, the overall demand for parts and components is also showing a steady upward trend.

EXPECTED GLOBAL MARKET FOR LAND DRILLING EQUIPMENT (UNITS OF LAND DRILLING RIGS FROM 2005 TO 2019)



Source: Spears and Associates.

MANAGEMENT DISCUSSION AND ANALYSIS

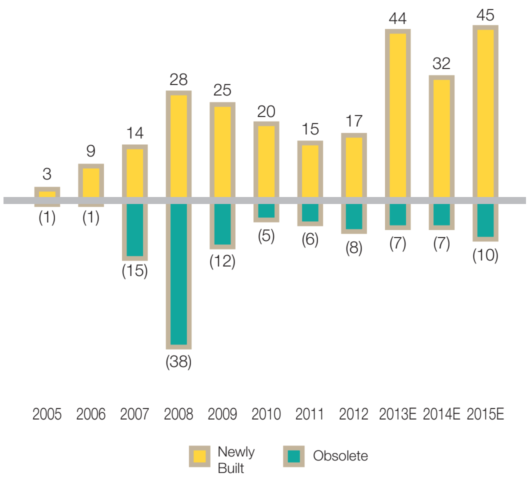
In 2014, the Group will continue to implement its "Localization" and "Forward sales" strategies, and procure sustained and steady business growth by targeting the needs of customers from different markets and adopting different sales tactics. Meanwhile, the Group will further enhance the global sales network by establishing sales offices and after-sale service centres in territories such as Mexico, Argentina and Poland. In regard to the sales of land drilling rigs, the Group will, with its innovative, efficient and quality products, secure the markets in territories such as America, Russia, the Middle East, Eurasia and China, and at the same time further explore the demand in some emerging markets such as Africa. Regarding the sales of parts and components, the Group will continue to pay attention to the demand for replacement of parts and components, further strengthen the promotion of new higher-end products such as top drive and new quintuple mud pump, and at the same time expand the parts and components trading business with the potential customers by utilizing the global procurement network. Meanwhile, the Group will continue to be in line with the principle of "Creative Manufacturing", and strive to attain objectives of "new technology", "new equipment" and "new manufacturing process", continue to advance the innovation and research and development of "new-generation smart" drilling rigs, and parts and components, and hence reflecting the Group's endeavor to relentlessly sharpen its competitive edge for continuous development in the next decade of growth. As of the end of February 2014, the Group's on-hand sales orders of complete set of land drilling rigs reached approximately 63 sets, worthing approximately RMB4,957 million, and the land drilling rigs are expected to be delivered in separate phases between 2014 and 2015.

OFFSHORE EQUIPMENT BUSINESS

The demand in the offshore equipment market is relatively steady in the recent two years. According to the forecast of Spears & Associates, the annual demand for jack-up platforms will remain in the range of 30-40 units in the next three years, which mainly comes from the replacement of the existing old platforms. According to the statistics of the securities firms, in 2012 nearly 70% of the jack-up platforms in the world will be aged 30 years or above. The gradual withdrawal of old vessels from the market is the future trend. With the rise of Chinese offshore equipment manufacturing enterprises, a growing number of sales orders of jack-up platforms was obtained by the Chinese enterprises. In 2012, the market share of jack-up platforms of Chinese offshore engineering enterprises reached 42%, which was basically catch up with that of Singaporean enterprises.

In 2014, apart from continuing to finish the construction of Honghai Crane, the Group will also complete the Tiger and PSV Vessel projects on time with the quality and quantity guaranteed. Furthermore, while further expanding the offshore equipment market and making much effort to take the sales orders of drilling modules and PSV vessels, the Group will also strive to take the first order of offshore drilling platform in 2014. The Group believes that with Honghua's offshore construction capacity being gradually proved, advantages of the innovative construction mode "onshore manufacturing of offshore platform" such as design, cost, manufacturing cycle will gradually become prominent, and Honghua's offshore equipment manufacturing business will develop in a good direction. As at the end of February 2014, the Group's on-hand sales orders of offshore parts and components value approximately RMB168 million.

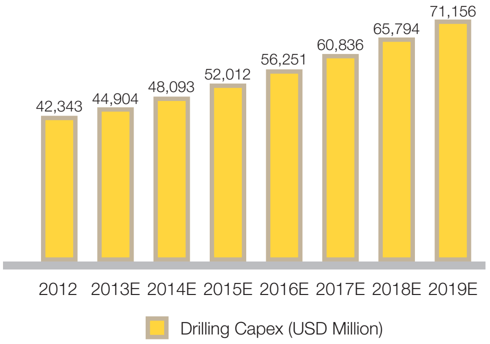
PROSPECTS FOR GLOBAL STRONG OFFSHORE JACK-UP DRILLING RIGS MARKET



Source: Spears and Associates.

MANAGEMENT DISCUSSION AND ANALYSIS

CAPEX OF DRILLING AND COMPLETION OPERATIONS CONTINUES TO INCREASE



Source: Spears and Associates.

OIL AND GAS ENGINEERING SERVICES BUSINESS

As for the oil and gas engineering services in China, according to the forecast of Spears & Associates, the capital expenditure on well completion business in China will remain at a compound growth rate of 6.7%. The rise of capital expenditure will lead to the increase in new drilling wells. Furthermore, due to the increasing depth and difficulty of exploring old oil fields, the demand for well completion service shows a steadily upward trend in the entire Chinese market. In addition, in early 2014, Sinopec proposed the downstream mixed ownership reform which will sell up to 30% of its equity to the social and private capitals. This is an indicator that the domestic oil and gas industry will hopefully be further opened in the future. The constantly deepening marketization in various major oil and gas production zones is also conducive to the flourishing development of domestic oil and gas engineering services.

In 2014, the Group will continue to rely on self-production of equipment, adhere to the drilling well and drilling fluids services as the core business, emphasize directional and horizontal drilling services, treat fracturing services as an opportunity, in order to provide customers with integrated drilling well services and gradually expand the business from conventional area to unconventional oil and gas services and from the domestic market to overseas markets. Regarding team building, the Group will maintain the existing scale of the directional drilling service team and drilling fluids service teams, and timely input equipment and expand the scale of the drilling well team based on the specific condition of potential projects. The Group will swift its focus from the rapid expansion of teams and business to efficiency enhancement, thereby raising the overall profit margin of oil and gas engineering services projects. As of the end of February 2014, the Group's on-hand sales orders of oil and gas engineering services worth approximately RMB444 million.

MANAGEMENT DISCUSSION AND ANALYSIS

UNCONVENTIONAL OIL AND GAS RESOURCES BUSINESS

In early 2014, Sinopec released a new shale gas exploration scheme, and it is expected to drill 50-70 shale gas wells during the Year. Meanwhile, PetroChina Southwest Oil & Gas Field Co. also announced that it will deploy more than 20 work platforms and drill more than 110 new wells. According to the latest plans of Sinopec and PetroChina, in 2014 shale gas exploration is expected to enter into large-scale development phase in China, with its work reaching about three to four times of that in 2013. Based on the situation, the shale gas exploration of Sinopec and PetroChina is expected to reach 10 billion m^3 in 2015, which exceeds the originally planned national output of 6.5 billion m^3. Furthermore, with the inclusion of shale gas production by CNOOC, Shaanxi Yanchang Petroleum Group, China Huadian Group, China United Coalbed Ltd. Co and some private enterprises, the national shale gas production in 2015 is expected to reach 12 billion m^3 to 13 billion m^3. With the large-scale exploration of shale gas, huge demand for exploration-related equipment such as drilling rigs, fracturing tracks and also oil and gas engineering services will be resulted.

In terms of special equipment, in 2014 the Group will continue to improve design of the flexible water tanks series and work on market promotion, in order to secure more sales orders. Meanwhile, the Group will focus on completing the on-site tests of 6000HP fracturing pump both in China and abroad, in order to realize sales in 2014. With regard to the oil and gas engineering services, the Group will, with the foundation laid in 2013, continue to look for more opportunities for unconventional oil and gas projects such as shale gas and tight gas. Concerning resources, the Group will also persistently focus on the domestic policies on shale gas and the trend in the industry, in order to seek opportunities and participate as a minority stakeholder in upstream resources exploration.

The year of 2014 is a crucial year for Honghua, as each strategic segment has basically formed and is ready for implementation. While maintaining the steady and sustainable development of the land drilling business, the Group will strive to grasp development opportunities from segments of offshore engineering, oil and gas engineering services as well as unconventional oil and gas resources in order to lay a solid foundation of Honghua's transitional development in the next decade, and create higher returns for the Shareholders.

MANAGEMENT DISCUSSION AND ANALYSIS

FINANCIAL REVIEW

During the Year, the Group's gross profit and profit attributable to shareholders of the Company amounted to RMB1,905 million and RMB538 million respectively, gross margin and net margin amounted to approximately 23.7% and 6.7% respectively. While gross profit and profit attributable to shareholders of the Company in the Last Year amounted to approximately RMB1,747 million and RMB529 million respectively, gross margin and net margin in the Last Year amounted to approximately 34.5% and 10.4% respectively. During the Year, the increase in the Group's gross profit and profit attributable to shareholders of the Company was mainly attributable to the rapid increase in sales revenue due to the Group's effort in proactive market development.

TURNOVER

During the Year, the Group's turnover amounted to approximately RMB8,047 million, while it was approximately RMB5,068 million during the Last Year, representing an increase of 58.8%. The increase was mainly attributable to the global growth in demand of oil drilling equipment, the Group's effort in proactive market development, growth of the oil and gas engineering services and offshore drilling rig parts and components. During the Year, as there was growth in demand of the Group's higher end product, the average selling price increased by 13.8%. The number of drilling rig sold during the Year increased to 74 units from 56 units of the Last Year.

(1) REVENUE BY GEOGRAPHICAL AREAS

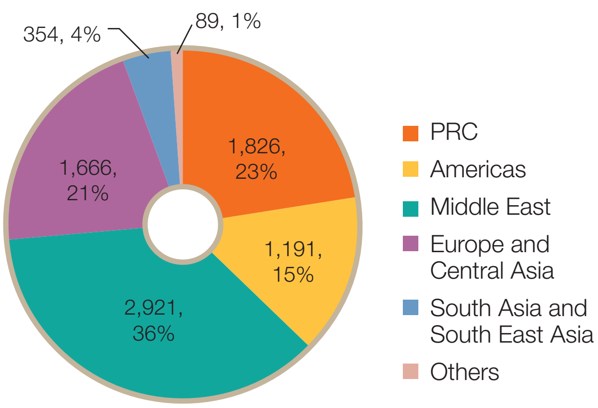
The Group's revenue by geographical segment areas during the Year was as follows: (1) the revenue from export amounted to approximately RMB6,221 million, accounting for approximately 77.3% of the total revenue, representing an increase of approximately RMB2,185 million or 54.1% as compared to those of the Last Year. Among which, the revenue from Middle East amounted to approximately RMB2,921 million, representing an increase of RMB2,874 million or 6,114.9%. The revenue from Europe and Central Asia amounted to approximately RMB1,666 million, representing an increase of approximately RMB902 million or 118.1%. The revenue from South Asia and Southeast Asia market amounted to approximately RMB354 million, representing an increase of RMB135 million or 61.6%. The revenue from American market amounted to approximately RMB1,191 million, representing a decrease of approximately RMB1,601 million or 57.3%; (2) the revenue from the PRC market amounted to approximately RMB1,826 million, accounting for approximately 22.7% of the total revenue, representing an increase of RMB794 million or 76.9% as compared to those in the Last Year.

The Group's sales revenues from different regions are affected by the local oil and gas exploration activities. The Group actively explores markets in different regions to develop new customers, to get new orders, in order to ensure sustained growth in sales revenue.

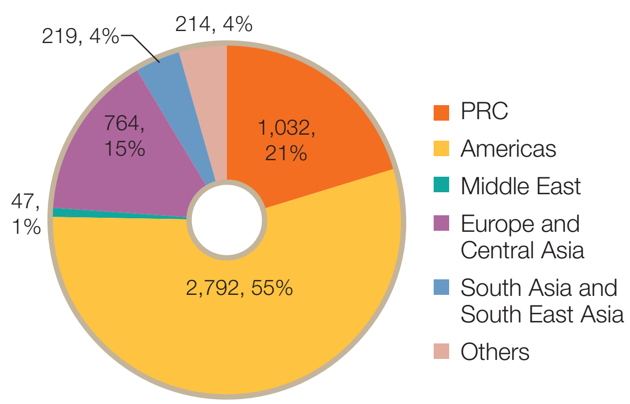
MANAGEMENT DISCUSSION AND ANALYSIS

Revenue by geographical areas in 2013 and 2012 were as follows (in RMB million).

2013 revenue by Geographical Areas



2012 revenue by Geographical Area



(2) REVENUE BY BUSINESS CATEGORIES

The Group's business are divided into land drilling rigs, land drilling rig parts and components, offshore drilling rigs and parts, oil and gas engineering services.

During the Year, revenue from land drilling rigs were amounted to approximately RMB5,665 million while it was approximately RMB3,751 million during the Last Year, representing an increase of RMB1,914 million or 51.0% as compared to the Last Year. The growth in land drilling rig sales revenue was mainly attributable to the increase in the number of sales volume from 56 units to 74 units, as well as due to the added value of the drilling rigs sold and the selling price increased during the Year.

During the Year, sales revenue from the land drilling rig parts and components amounted to approximately RMB1,777 million, while it was approximately RMB989 million during the Last Year, representing an increase of RMB788 million or 79.7% as compared to the Last Year. The revenue growth is mainly attributable to the Group's effort in proactive market development and breakthrough in sales of new products. Drilling rig transformation and parts processing generating revenue amounted to approximately RMB33 million; 109 mud pumps were sold, generating revenue amounted to approximately RMB124 million; 4 electric drive systems were sold, generating revenue amounted to approximately RMB18 million; 6 fracturing trucks were sold, generating revenues amounted approximately RMB28 million.

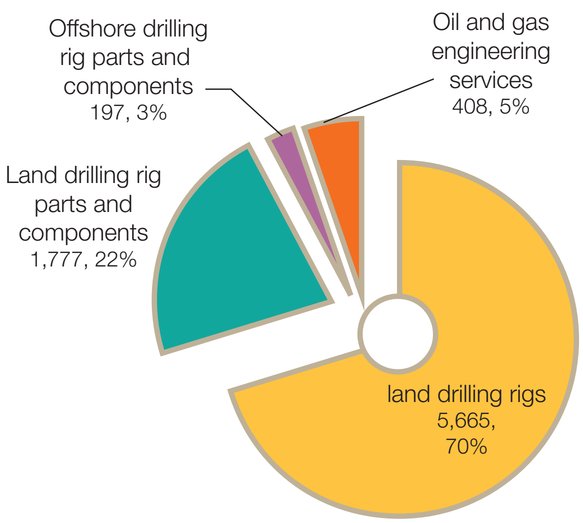
During the Year, revenue from offshore drilling rig parts and components amounted to approximately RMB197 million, while it was approximately RMB157 million in the Last Year.

During the Year, revenue from oil and gas engineering services amounted to approximately RMB408 million, mainly attributable to the Group's proactive development of oil and gas drilling service market, providing oil and gas engineering services to 23 well fields mainly located in Xinjiang and northeast China and Iraq.

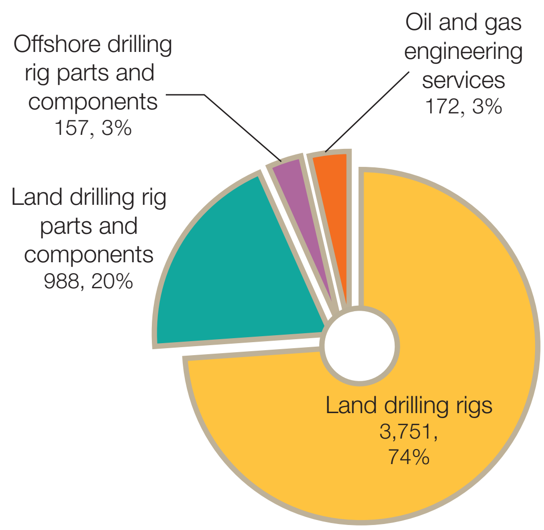
MANAGEMENT DISCUSSION AND ANALYSIS

Revenue by business categories was as follows:

2013 Revenue by business categories



2012 Revenue by business categories



COST OF SALES

During the Year, the Group's cost of sales amounted to approximately RMB6,142 million, while it was approximately RMB3,321 million in the Last Year, representing an increase of approximately 84.9% as compared to the Last Year, mainly due to substantial growth in sales revenue.

GROSS PROFIT AND GROSS MARGIN

During the Year, the Group's gross profit amounted to approximately RMB1,905 million, representing an increase of RMB158 million or 9.1% as compared to that of Last Year.

During the Year, the Group's overall gross profit margin was 23.7%, representing a decrease of 10.8 percentage points as compared to that of Last Year. This was mainly due to the Group's in proactive market development and taking the initiative to benefit customers in some markets.

EXPENSES IN THE YEAR

During the Year, the Group's selling expenses amounted to approximately RMB524 million, representing a decrease of RMB30 million or 5.4% as compared to RMB554 million in the Last Year. This was mainly attributable to the decrease of sale service expenses during the Year.

During the Year, the Group's general & administration expense amounted to approximately RMB596 million, representing an increase of RMB69 million or 13.1% as compared to RMB527 million in the Last Year. Mainly due to the growth of the business and expanding of the Group, resulting in increase in labor costs, depreciation and amortization and other administration expenses.

During the Year, the Group's net finance expenses amounted to approximately RMB139 million, representing an increase of RMB168 million as compared to net financing income of RMB29 million in the Last Year. The increase in net finance expense was mainly attributable to that the Group recorded an increase of interest expenses of RMB117 million during the Year and there was a net exchange loss of RMB27 million during the Year and there was a net exchange gain of RMB20 million in the Last Year.

PROFIT BEFORE TAXATION

During the Year, profit before taxation of the Group amounted to approximately RMB701 million, representing a decrease of RMB8 million or 1.1% as compared to RMB709 million in the Last Year, mainly attributable to the decrease in gross margin and increase in finance expense.

INCOME TAX EXPENSES

During the Year, the Group's income tax expense amounted to approximately RMB126 million as compared to RMB168 million in the Last Year. The decrease was mainly attributable to the tax incentives of withholding tax of the undistribution profits of the Company's subsidiaries in the PRC, the rate of withholding tax decrease from 10% to 5%.

PROFIT FOR THE YEAR

During the Year, the Group's profit amounted to approximately RMB575 million, representing an increase of RMB33 million or 6.1% as compared to RMB542 million in the Last Year. Among which, profit attributable to equity shareholders of the Company amounted to approximately RMB538 million, representing an increase of RMB8 million or 1.5% as compared to that in the Last Year, while earnings attributable to non-controlling interests was approximately RMB37 million. During the Year, net margin was 6.7%, representing a decrease of 3.7 percentage points as compared to 10.4% in the Last Year, which was mainly attributable to the decrease in gross profit margin.

EARNINGS BEFORE INTEREST, TAXES, DEPRECIATION AND AMORTIZATION ("EBITDA") AND EBITDA MARGIN

During the Year, EBITDA amounted to RMB1,082 million, as compared to approximately RMB828 million in the Last Year, which was mainly attributable to the marked increase in operating profit brought by the significant increase in revenue. The EBITDA margin was 13.4%, representing a decrease of 2.9 percentage points as compared to 16.3% in the Last Year, which was mainly attributable to the decrease of gross margin.

DIVIDEND

For the year ended at 31 December 2013, the Directors recommend a final dividend of HK6 cents per Share, which is subject to the approval of the shareholders of the Company at the forthcoming annual general meeting. The final dividend will be payable on or around 18 June 2014 to the shareholders of the Company whose names appear in the register of members of the Company as on 4 June 2014.

SOURCE OF CAPITAL AND BORROWINGS

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

As at 31 December 2013, the Group's bank borrowings amounted to approximately RMB4,731 million, representing an increase of approximately RMB2,748 million as compared to that at 31 December 2012. Among which, borrowings repayable within one year amounted to approximately RMB3,274 million, representing an increase of RMB2,028 million as compared to 31 December 2012. The Group's bank borrowings amounted to RMB1,252 million and RMB3,479 million were in fixed and variable rates respectively as at 31 December 2013. The increase in banking borrowings was mainly attributable to the rapid growth of the Group's operating scale, leading to increased demand for capital investment and operating cash.

MANAGEMENT DISCUSSION AND ANALYSIS

DEPOSIT AND CASH FLOW

As at 31 December 2013, the Group's cash and cash equivalents amounted to approximately RMB1,275 million, representing an increase of approximately RMB290 million as compared to that at 31 December 2012. During the Year, net operating cash outflow amounted to approximately RMB324 million, mainly because the Group had increased the procurement of raw materials to ensure timely delivery of orders in 2013; net cash outflow from investing activities amounted to approximately RMB1,690 million, which was mainly due to investment of fixed assets and construction in progress for offshore manufacturing base project and oil and gas engineering services, the cash flow of investment to other finance asset amounted to approximately RMB484 million; net cash inflow from financing activities amounted to approximately RMB2,313 million, which was due to increase of bank borrowings.

ASSETS STRUCTURE AND CHANGES THEREOF

As at 31 December 2013, the Group's total assets amounted to approximately RMB14,229 million, representing an increase of approximately RMB4,383 million or 44.5% as compared to 31 December 2012. Among which, current assets amounted to approximately RMB9,681 million, accounting for approximately 68.0% of the total assets, representing an increase of approximately RMB3,063 million as compared to that at 31 December 2012, mainly due to an increase of cash and cash equivalents, trade receivables and other financial assets; non-current assets amounted to approximately RMB4,548 million, accounting for approximately 32.0% of the total assets, representing an increase of approximately RMB1,320 million as compared to that at 31 December 2012, which were mainly due to an increase of fixed assets and long-term receivables.

LIABILITIES

As at 31 December 2013, the Group's total liabilities amounted to approximately RMB9,270 million, representing an increase of approximately RMB4,013 million as compared to that at 31 December 2012. Among which, current liabilities amounted to approximately RMB7,762 million, accounting for approximately 83.7% of the total liabilities, representing an increase of approximately RMB3,244 million as compared to that at 31 December 2012; non-current liabilities amounted to approximately RMB1,508 million, accounting for approximately 16.3% of the total liabilities, representing an increase of approximately RMB769 million as compared to that at 31 December 2012. As at 31 December 2013, the Group's gearing ratio was approximately 65.2%.

EQUITY

As at 31 December 2013, total equity amounted to RMB4,959 million, representing an increase of RMB370 million as compared to that at 31 December 2012. Total equity attributable to equity shareholders of the Company amounted to approximately RMB4,763 million, representing an increase of RMB307 million as compared to 31 December 2012. Non-controlling interests totaled to approximately RMB195 million, representing an increase of RMB63 million as compared to that at 31 December 2012. Net asset value reached approximately RMB1.47 per Share. During the Year, the Group's basic earnings per Share was approximately RMB16.99 cents, and diluted earnings per Share was approximately RMB16.77 cents.

CONTINGENT LIABILITIES AND PLEDGE

(A) CONTINGENT LIABILITIES

Contingent liabilities in respect of legal claim

Lawsuits with a sales agency

A sales agency filed lawsuit against a subsidiary of the Company, alleged that it was owed commissions in excess of USD18,000,000 in relation to its services to the Group.

On 24 April 2013, the United Arab Emirates ("UAE") Federal Court of First Instance ordered the termination of agency agreement and dismissed all claims from the sales agency. The sales agency filed an appeal to the UAE Federal Court of Appeal on the court's decision and hearing is yet to be made as at 31 December 2013. Having consulted the Group's legal advisors, management considered that the Group had legal and factual merit to defend in the lawsuits. Accordingly, management determined that it was not probable that the outcome of the lawsuits will be unfavourable to the Group. No provision was made for the potential claims under these lawsuits.

(B) PLEDGE

As at 31 December 2013, the Group has pledged bank deposits, land use rights, fixed assets and trade and other receivables of approximately RMB1,468 million, representing an increase of approximately RMB556 million as compared to that at 31 December 2012.

CAPITAL EXPENDITURE, MAJOR INVESTMENT AND CAPITAL COMMITMENTS

During the Year, capital expenditure of the Group on infrastructure and technical improvements amounted to approximately RMB1,267 million. This was mainly attributable to the input in the infrastructure construction of offshore projects and expansion of production capacity of land drilling rigs.

As at 31 December 2013, the Group had capital commitments of approximately RMB1,378 million, which will be used for the construction of Jiangsu Qidong offshore manufacturing base and expansion of the Group's business as well as the production capacity.

FOREIGN CURRENCY RISK

The Group has certain foreign currency deposits. As at 31 December 2013, the Group's foreign currency deposits were equivalent to approximately RMB258 million, trade and other receivables denominated in foreign currency were equivalent to approximately RMB2,144 million. Exports and foreign currencies settled business exposed the Group to exchange risk. The Group has managed to mitigate the exchange risk through entering into forward foreign exchange contracts and price adjustment during contract negotiation in consideration of future exchange rate circumstances. Also, the Group mitigates the exchange risk by having foreign currency bank loans and trade payables.

MANAGEMENT DISCUSSION AND ANALYSIS

LIQUIDITY RISK

The objective of liquidity risk management is to ensure that the Group always has sufficient cash to meet its liabilities and working capital requirements.

The Group liquidity management procedures involve regularly projecting cash flows in major currencies and considering the level of liquid assets and new financings necessary to meet these cash flow requirements. Every month, cash flow projections are reviewed and revised by business segments and financing actions are taken accordingly.

The Group actively seeks to diversify its funding sources so as not to be reliant on any one market. The Group's policy is to diversify the sources of funding as much as possible through the increasing use of the capital market to supplement bank borrowings and to maintain a mix of staggered maturities to minimise refinancing risk.

As at 31 December 2013, the Group had foreign currency interest bearing borrowing denominated in USD of RMB1,162 million, cash and cash equivalents denominated in USD and Euros of RMB253 million and RMB4 million.

EMPLOYEE REMUNERATION AND BENEFITS

During the Period, the average employee number of the Group was 6,693. The total amount of remuneration and benefit was about RMB801 million, increased by RMB223 million or 35.6% as compared to that of Last Year.

The strategy of human resource management of the Group is the consistency between performance culture and enterprise culture. To realize a win-win situation between the development of the Group and the development of staff, the Group has built a future-oriented resources plan, attracting talents with high-performance and high-potential, establishing diverse salary incentive policies and reinforcing the training as well as the career planning of employees.

During the Period, the Group develops the performance systems by breaking down the performance objectives into posts that matters most. It develops the compensation system by offering bonus to each subsidiary based on the completion of performance target and by adjusting employees' salary based on performance, capability, attitude and market situation. It develops the training system by providing performance improvement program and specialized training for low performance employees, so as to improve their knowledge, capability, skill and sense of belonging. The Group has also set up a share option scheme and a restricted share award scheme as a long-term incentive mechanism for core talented employee and excellent staff and senior and middle management in order to encourage them to grow with the Group.

To improve the competitive advantage of human resource, the Group will enhance the passion, potential and spirit of employees by perfecting the system and procedure, emphasizing the employee relationship management and developing personalized training plan for the years to come.

CORPORATE SOCIAL RESPONSIBILITY REPORT

Throughout the years, The Group has always upheld our corporate social responsibility principles of "gratitude, love, education, and enlightenment" as well as our Company's value of "giving back to society." We continue to actively take part in promoting workplace safety, environmental protection, talent cultivation, employee benefits, and social welfare. The Group considers these values during our corporate management and decision making processes. The Group wishes to facilitate the development of a peaceful relationship between our Company and the society with a view to guarantee the interests of our Shareholders, partners and employees. We also hope to develop sustainable energy all over the world to ensure that economic development and environmental protection may go hand in hand.

Honghua Group's land drilling rig production base — one of the largest land drilling rig production facilities in the world.

CONTINUOUS SUPPORT OF SOCIAL WELFARE

- January 2013: Our Sichuan Honghua Petroleum Equipment Co., Ltd. established the Sichuan Honghua Academicians and Experts Workstation. The Group started collaborating with professional teams of academicians from the Chinese Academy of Engineering, signifying a new era of global and Chinese ocean engineering equipment as well as the future development and utilization of ocean resources.

- April 2013: The Group and its employees immediately provided help to those in need after the Lushan earthquake occurred at Ya'an Lushan County, Sichuan. In total, the Company and its workers donated over RMB1.4 million to Tianquan Middle School in Ya'an through the "Honghua Education Foundation". The Group will continue to support education and charity work in Ya'an for the next three years.

- July 2013: The Group donated RMB1 million to the Wenchuan Earthquake reconstruction fund in addition to its donation of a total of RMB666,666 to the Honghua School of Foreign Language after its reconstruction during the period from 2010 to December 2013. The school's students and faculty members use the donation for studying abroad in the United States every summer.

CORPORATE SOCIAL RESPONSIBILITY REPORT

- July 2013: Employees of Honghua Company volunteered to donate blood. Since 2010, our employees have donated over 200,000 milliliters of blood over the past four years.

- September 2013: Honghua Company received the honorable title of “Respecting Advanced Collective in Education” to commend the Group’s continuous contribution to social welfare and charity work and the passion the Group shows towards education.

Summer of 2013: Student life in Vermont’s Mountain School Summer Camp in the United States.

Honghua School of Foreign Language: During recess, students browse new books at their recently constructed Book Hall.

Tianquan Middle School in Ya’an: Honghua Education Foundation Donation Ceremony.

Honghua employees donating blood: This employee has volunteered to donate blood for many years.

Liu Hongbao, Deputy Party Secretary of Deyang, presenting the Workstation License to Zhang Mi, Chairman and President of Honghua Group Limited.

CORPORATE SOCIAL RESPONSIBILITY REPORT

HEALTH, SAFETY, AND ENVIRONMENTAL PROTECTION (HSE)

As the first drilling rig manufacturer of China listed on the Stock Exchange in Hong Kong, the Company fully understands that guaranteeing production safety is the Company's most important responsibility to the society, our Shareholders, and our employees. Therefore, the Group and its subsidiaries have implemented standard guidelines for production safety on inspection, evaluation, supervision, and training. Through a standardized health, safety, and environmental protection (HSE) management system, the Company has been able to fully implement and manage production safety and raise the workplace safety awareness of all our workers.

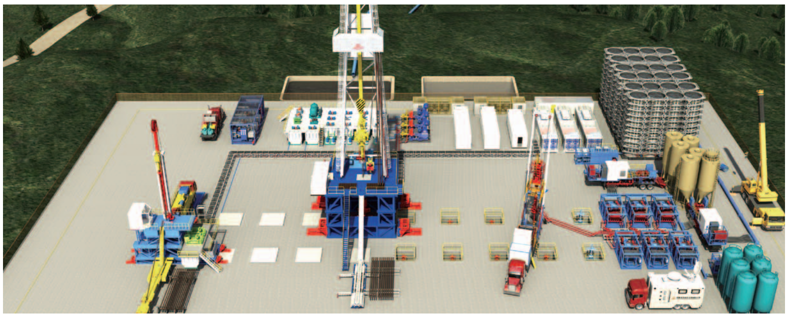
In January 2013, the Company's Land Drilling Rig production base passed the HSE expansion audit. While conforming to the occupational health, safety, and environmental protection requirements of international professional institutions, we will continue to optimize the development of our Company's workplace safety, improve product quality as well as the management of our production process and environment. Production safety plays an extremely important role in our Company's long-term development and is also our promise to the society, the environment, our Shareholders, partners, and employees.

EVENTS TO RAISE AWARENESS OF HEALTH AND SAFETY

We continue to conduct various promotion and educational activities, training, drills, and examinations to raise worker awareness of safety, occupational health, and environmental protection.

ENERGY-EFFICIENT R&D FOR ENVIRONMENTAL PROTECTION AND ENERGY CONSERVATION

The Company believes that environmental protection is an important aspect of a company's corporate social responsibility. As the world continues to promote the development of sustainable energy and environmental protection, the Group strives to research, develop and improve energy efficient and environmentally friendly product designs.



Honghua Products: Comprehensive shale gas solutions decrease 10% of fixed asset investment, 65% of production space, up to 80% of fuel costs, and at least 10% of overall development costs.

New Direct Drive Electro 6000 HP Fracturing Pump, a part of the comprehensive shale gas solution, is currently the most powerful of its kind on the market and only requires half of the production space of other fracturing pumps.

Flexible Water Tanks hold four-times the volume of traditional water tanks but only take up a quarter of the space.

CORPORATE SOCIAL RESPONSIBILITY REPORT

CULTIVATING A CREATIVE CULTURE AND PROMOTING BETTER PRODUCTION ATTITUDES

We realize that having an effective corporate culture and values can enhance our employee's sense of belonging, corporate identity and improves our competitiveness. In 2013, the Group greatly emphasized the creation of a corporate culture with a view of developing a better cultural atmosphere in order to take the creativity and productivity of our employees to new heights.

THE MAKING OF A ROLE MODEL AND CREATING A LEGACY

On 7 March, 2008, the Company was listed on the Stock Exchange in Hong Kong. Since then, every year on 7 March the Company holds "The Making of a Role Model" event — a ceremony for commending excellent employees. The event has not only pooled our staff's sense of belonging, but also allows us to pass down our corporate spirit and fully demonstrate Honghua's creative culture and productive spirit.

FOCUSING ON NEW KNOWLEDGE AND ENGAGING EMPLOYEE INTERESTS

In 2013, six issues of the Company's periodical "Honghua Man" were published. While reporting on news within the Company and introducing new management know-how, the editors also set up the "Orange Club" column to plan, launch, and report employee activities as an effort to promote a variety of activities for employees at our subsidiaries.

March 2013: Honghua employees at the Black Bear Rescue Center promoting harmony and animal protection.


March 2013: Honghua employee rock climbing event.

Family Day at Honghua: Family members get to know more about the Company. December 2013 was the first annual Family Day event.


November 2013: Honghua employees participating in the "China 365 Cycling Challenge".

CORPORATE SOCIAL RESPONSIBILITY REPORT

FOCUSING ON CULTIVATING TALENTED EMPLOYEES

The Company strongly believes that talented employees are the Company's most important asset and insists on providing long-term, on-the-job training for our employees. Through training, we strive to improve our employees work capacity and aim to cultivate more talents for the industry and society. Through our optimized salary management, performance evaluation, and bonus and disciplinary mechanisms, we are able to attract and keep talented employees and continue to provide them with different opportunities to further their career. These efforts cultivate positive attitudes and creativity in our employees and provide momentum for the Company towards new milestones.

In 2013, the Company organized 942 training sessions with 52,111 participants in total. The training curriculum included the strategic management and leadership training for junior and senior management personnel, training relating to the Company's management and supervision system, periodic training of business skill for various work modules, training for new employee and language classes.

EFFECTIVELY CAPITALIZING AVAILABLE SOURCES THROUGH UNIVERSITY-ENTERPRISE COOPERATION

The Company, with its focus on talent training, also attaches high values to the effective integration of production, education and research through extensive collaboration with university in China to deepen exchanges and cooperative relations in academic thinking, scientific research, talent training and university-enterprise cooperation. In 2013, the Company successfully held the first Talent Strategy Summit Forum focused on "gathering intelligence from governments, universities and enterprise to sharpen competitive edge in talents" in Chengdu, the PRC, which has created a high-level expert exchange platform to explore talents and intellectual sources. This platform is also beneficial for governments, universities and enterprises. In addition, the Group planned and organized two exciting theme activities for six Chinese Petroleum universities and eight "Project 985" colleges and universities, including Shanghai Jiao tong University and Harbin Institute of Technology. These theme activities, namely "Honghua Group 2013 Future Stars Career Counseling Training Camp Oil Institutions Special" and "Honghua Group 2013 Future Stars Career Counseling Camp 985 Colleges and Universities special", got a total of 150 teachers and students involved. In 2013, the Company was also awarded the title of "Top Ten Employer in Sichuan".

Employee career planning

Continued staff management training

Employees attending English workshops

BIOGRAPHICAL DETAILS OF DIRECTORS AND SENIOR MANAGEMENT

EXECUTIVE DIRECTORS

Mr. Zhang Mi (張弭先生), aged 57, has been Chairman of the Company and an Executive Director since June, 2007. He is also President of the Company.

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.

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.

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

Subsidiary	Position	Term of Office
Honghua Holdings Limited	director	Since 18 August 2006
	chairman, and chief executive officer	Since 8 September 2009
Sichuan Honghua Petroleum Equipment Co., Ltd.	director	Since 31 December 1997
Sichuan Honghua International Co., Ltd.	chairman	Since 13 January 2004
Honghua Offshore Oil & Gas Equipment (Jiangsu) Co., Ltd.	chairman	Since 8 June 2009
Shanghai Honghua Offshore Oil & Gas Equipment Co., Ltd.	executive director	Since 9 September 2009
Honghua (China) Investment Co, Ltd.	chairman, and general manager	Since 14 January 2010
Honghua Oil & Gas Engineering Services Co., Ltd.	director	Since 14 April 2009
Honghua America, LLC.	chairman	Since 11 October 2004
Egyptian Petroleum HH Rigs Manufacturing CO. S.A.E	director	Since 26 April 2007
Gansu Hongteng Oil & Gas Equipment Co., Ltd.	director	Since 28 December 2011

BIOGRAPHICAL DETAILS OF DIRECTORS AND SENIOR MANAGEMENT

Mr. Ren Jie (任杰先生), aged 47, 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, 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, and in 2012, he earned a Doctor's degree in Mechanical Design and Theory from Southwest Petroleum University. Mr. Ren is employed as an engineer by Honghua Company.

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

Subsidiary	Position	Term of Office
Honghua Holdings Limited	director	Since 18 August 2006
Sichuan Honghua Petroleum Equipment Co., Ltd.	director	Since 31 December 1997
	general manager	Since 1 July 2013
Sichuan Honghua International Co., Ltd.	director	Since 13 January 2004
	general manager	Since 24 April 2008 until 31 December 2013
Honghua Offshore Oil & Gas Equipment (Jiangsu) Co., Ltd.	director	Since 8 June 2009
Sichuan Honghua Electric 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
Egyptian Petroleum HH Rigs Manufacturing CO. S.A.E	director	Since 7 August 2009
Honghua America, LLC.	director	Since 10 October 2008

Mr. Liu Zhi (劉智先生), aged 50, has been an Executive Director of the Company since 26 May 2008. He is also a Vice-president of the Company.

Mr. Liu graduated from Southwest Petroleum University in 2003, with a Master 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 the Group's markets inside and outside of China.

BIOGRAPHICAL DETAILS OF DIRECTORS AND SENIOR MANAGEMENT

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
Bazhou Honghua Petroleum Applied Chemistry Co., Ltd.	chairman	Since 1 April 2013
Honghua (China) Investment Co., Ltd.	director	Since 14 January 2010
Honghua Oil & Gas Engineering and Technology Services (Sichuan) Co., Ltd.	chairman and general manager	Since 30 December 2010

NON-EXECUTIVE DIRECTORS

Mr. Siegfried Meissner, aged 61, has been a Non-executive Director of the Company since 26 May 2008. Mr. Meissner graduated from the Technical University of Clausthal-Zellerfeld, Germany as Dipl. Berging., specialized in drilling, reservoir and production engineering in 1982. Since 1993, Mr. Meissner joined the Nabors Group as President of Nabors Drilling International Limited. Mr. Meissner has been a director of Nabors International Management Limited since 29 December 2004.

Popin Su, aged 49, has been the alternate director to Siegfried Meissner, a Non-executive director of the Company, since 27 December 2012. Mr. Su has been the vice president and corporate treasurer of Nabors Industries since 2008. He acted as the vice president of Nabors Drilling International Ltd. from 1999 to 2007. Mr. Su holds a Bachelor of Science degree from National Taiwan University and a Master's degree in Business Administration from University of Texas at Austin.

INDEPENDENT NON-EXECUTIVE DIRECTORS

Mr. Liu Xiaofeng (劉曉峰先生), aged 51, 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 Kun Lun Energy Company Limited and Haier Electronics Group Co., Ltd.. He has 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 Southwest University of Finance and Economics in 1983.

BIOGRAPHICAL DETAILS OF DIRECTORS AND SENIOR MANAGEMENT

Mr. Qi Daqing (齊大慶先生), aged 50, has been an Independent Non-executive Director of the Company since 18 January 2008. Mr. Qi is also an independent non-executive director of Sohu.com Inc., AutoNavi Holdings Ltd., Bona Film Group Ltd., SinoMedia Holding Ltd. and China Vanke Co. Ltd.. Mr. Qi is currently a professor of Cheung Kong Graduate School of Business and a member of the American Accounting Association. Mr. Qi had worked for The Chinese University of Hong Kong, the Eli Broad Graduate School of Management at Michigan State University in the United States, the East-West Center in the United States and the China Features in Xinhua News Agency in the PRC. Mr. Qi graduated from Fudan University with a bachelor's degree of science in Biophysics and a bachelor's degree of arts in International Journalism. He obtained a master's degree in Management from the University of Hawaii and a doctoral degree in Accounting from the Eli Broad College of Business, Michigan State University in the United States.

Mr. Tai Kwok Leung, Alexander (戴國良先生), aged 56, has been an Independent Non-executive Director of the Company since 18 January 2008 and resigned with effect from 19 March 2014. Mr. Tai has extensive accounting, corporate finance and investment experience in Hong Kong and overseas. Mr. Tai is the managing director — corporate finance supervisor of Investec Capital Asia Limited (formerly known as "Access Capital Limited"), a licensed corporation under the SFO to conduct Type 1 (dealing in securities), Type 4 (advising on securities), Type 6 (advising on corporate finance) and Type 9 (asset management) regulated activities. Mr. Tai is currently an independent non-executive director of Luk Fook Holdings (International) Limited and Anhui Conch Cement Company Limited. 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. Chen Guoming (陳國明先生), aged 51, has been an Independent Non-executive Director of the Company since 18 January 2008. He is now a Professor, a Ph.D. candidate supervisor, a member of the Academic Committee, the Chief officer of Research Centre of Security technique of the Offshore Oil & Gas Equipment, the Chief officer of Professor Committee in the Department of Mechanical and Electrical Engineering of China University of Petroleum. Currently, Mr. Chen is the Chief officer of Shandong Key Laboratory of Petroleum Mechanical Engineering; 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. 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.

Mr. Shi Xingquan (史興全先生), aged 71, 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 has been appointed as the vice president of PetroChina Company Limited from 1999 until 2003. Mr. Shi was awarded the National Technology Advancement Award (First Prize) by the National Science and Technology Council of the PRC in 1997. In 2003, Mr. Shi was awarded the National Scientific and Technological Progress Award (First Prize) by State Council of the PRC. Mr. Shi was also granted the Middle-aged and Young Experts of the State with Outstanding Contribution by Ministry of Personnel of the PRC. Mr. Shi graduated from the Northeastern Petroleum College in 1965 and is a well-known petroleum engineering expert.

BIOGRAPHICAL DETAILS OF DIRECTORS AND SENIOR MANAGEMENT

Mr. Guo Yanjun (郭燕軍先生), aged 61, has been an Independent Non-executive Director of the Company since 20 June 2011. Mr. Guo is an independent non-executive director of Mei Ah Entertainment Group Limited and Strong Petrochemical Holdings Limited. Mr. Guo has extensive entrepreneurship experiences and experience of corporate operation and management. Mr. Guo is currently the chairman of Beijing Junxinda Economic Development Co., Ltd. and CNHK Media Limited. Mr. Guo graduated with a Diploma in Law from China People's University in 1984.

SENIOR MANAGEMENT

Mr. Zhao Ping (趙平先生), aged 57, has been a Vice-president of the Company since 27 April 2008. He has been a director of Honghua Company since 18 January 2010, and has been the chairman of Honghua Company since 1 January 2012. He was the general manager of Honghua Company from 18 January 2010 to 31 December 2011. From 1972 to 1999, Mr. Zhao worked in South-Sichuan Mining Area of Sichuan Petroleum Bureau. He was the head of Quality Management Office since 1993, and the director of Workshop No.1 from 1994 to 1996, and was the deputy factory director from 1997 to 1999. Mr. Zhao graduated from Machinery Department of Southwest Petroleum University, majoring in Petroleum & Minerals Machinery and is a qualified engineer.

Mr. Zhang Cong (張聰先生), aged 58, has been a Vice-president of the Company since 27 April 2008, and has been the chairman and general manager of Sichuan Honghua Electric Co.,Ltd. (formerly known as "Chengdu Hongtian Electric Drive Engineering Co., Ltd.") since June 2001. He has been a director of Honghua International Co., Ltd. since 1 August 2009, and has been the general manager of Honghua Offshore Oil & Gas Equipment (Jiangsu) Co., Ltd. and Shanghai Honghua Offshore Oil & Gas Equipment Co., Ltd. since 26 September 2011. Mr. Zhang was one of the initial founders of Sichuan Honghua Electric Co.,Ltd.. Mr. Zhang has helped Sichuan Honghua Electric Co.,Ltd. to sell DBS digital VFD system to major oil fields in China and a large number of products to the overseas market. In December 2006, Mr. Zhang was awarded "The Fourth session Excellent Start in Undertaking Entrepreneur of Chengdu". Mr. Zhang was a cadre in South-Sichuan Mining Area of Sichuan Petroleum Bureau from September 1985 to September 1994 and was the manager and director of Luzhou Huayou Compressed Gas Co., Ltd. form September 1994 to June 2001. Mr. Zhang graduated from Sichuan Radio TV University, majoring in electronic technology and is a qualified engineer.

Mr. Feng Shangfei (馮尚飛先生), aged 40, has been the Human Resources Director of the Company and Honghua (China) Investment Co., Ltd. since 1 June 2011, and was appointed as the general manager of Honghua Company from 1 January 2012 to 30 June 2013. Mr. Feng has over 10 years of experience in personnel, administration, corporate culture, senior management of large enterprise. For the period from October 2009 to March 2011, Mr. Feng worked for Anton Oilfield Services (Group) Ltd. as the Human Resources Director. For the period from April 2006 to September 2009, he worked for ENN Energy Holdings Limited (a holding group of a Hong Kong listed company), served as human resources director of the LNG Division, vice president of human resources of overseas business department and general manager of Vietnamese company. For the period from October 2000 to March 2005, Mr. Feng worked for Linuo Group Holdings Co., Ltd.. For the period from July 1995 to October 2000, he was a lecturer of Shandong University. Mr. Feng graduated from Shangdong University (formerly known as Shangdong Industry University) with a Bachelor's Degree of engineering in 1995, majoring in mechanical design and manufacture. He earned a Master's degree of Psychology from Beijing Normal University in 2000.

BIOGRAPHICAL DETAILS OF DIRECTORS AND SENIOR MANAGEMENT

Mr. Chung Kai Cheong (鍾啓昌先生), aged 36, has been the Financial Controller of the Company since 1 June 2011. Mr. Chung joined the Group in August 2008 as a director of financial centre of the Company. Mr. Chung has over 13 years of experience in accounting and auditing at international accounting firms and listed company. Mr. Chung also worked for KPMG from December 2003 to July 2008 with the then latest position as an audit manager. He also worked for BDO Limited (formerly known as BDO McCabe Lo & Co.) for the period from June 2000 to December 2003 with the then latest position as a senior associate. Mr. Chung obtained a Bachelor's Degree majoring in accountancy from The City University of Hong Kong in September 2000. He is currently a Fellow of the Hong Kong Institute of Certified Public Accountants.

Mr. Liu Gangqiang (劉剛強先生), aged 44, has been the Secretary of the Board of Directors and a Joint Company Secretaries of the Company since 21 January 2008 to 27 December 2013, the Secretary of the board of directors of Honghua Company from March 2004 to January 2011 and the chief operational officer of Honghua Holdings Limited since September 2009 to 27 December 2013. From February 2003 to September 2003, Mr. Liu conducted research on the development of state-owned enterprises, in the Work Technology Center of the Sichuan State-Owned Enterprise Supervisory Committee. From October 2000 to September 2003, he was an assistant general manager of Sichuan Aerospace High-tech Co., Ltd., and the general manager of Aerospace Network Communications System Engineering Co., Ltd.. From September 1997 to October 2000, he served as an economist in Sichuan Trust & Investment Co., Ltd. From September 1991 to May 1994, he was a technician at Beijing Yanshan Petroleum & Chemicals Co., Ltd.. Mr. Liu graduated from Chengdu Science and Technology University (now Sichuan University), with a Bachelor's Degree in high polymer material and engineering in 1991. He earned a Master's degree in Economics from Southwest University of Finance and Economics in 1997. In 2003, he received a Ph.D. in Economics from Southwest University of Finance and Economics.

Mr. He Bin (何斌先生), aged 40, has been the secretary of Board and a Joint Company Secretary of the Company since 27 December 2013. Mr. He joined the Group in 2008 as the director of Strategic Investment Department and assistant president of the Company. Mr. He has more than 10 years of investment and management experience, once was engaged in venture capital, investment consulting and other related work in Samsung Company. He holds a Bachelor's degree from Renmin University of China and a Master's degree in Business Administration from University of Alberta in Canada.

Ms. Corinna Leung (梁慧嫻女士), aged 46, has been a Joint Company Secretaries of the Company since 21 January 2008. She is a director of the corporate services department of Tricor Services Limited. She is a fellow member with the Institute of Chartered Secretaries and Administrators and the Hong Kong Institute of Chartered Secretaries. She provides corporate services to companies that are listed on the Main Board, Growth Enterprise Market of the Stock Exchange and private companies. She acts as the joint company secretary of SBI Holdings, Inc., a company listed on the Stock Exchange and Beijing Jingneng Clean Energy Co., Limited, a company listed on the Stock Exchange.

CORPORATE GOVERNANCE REPORT

The Board presents this Corporate Governance Report in the Group's annual report for the year ended 31 December 2013.

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 Corporate Governance Code (the "CG Code") contained in Appendix 14 to the Listing Rules.

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

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

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

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

The Company has complied with most of the code provisions as set out in the CG Code throughout the year ended 31 December 2013, save for certain deviations from the code provisions in respect of separation of roles of Chairman and President (Chief Executive Officer) and the dismissal of the Nomination Committee of the Company, 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.

MODEL CODE FOR SECURITIES TRANSACTIONS

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

Specific enquiry has been made of all Directors and all Directors have confirmed that they have complied with the Company Code and the Model Code throughout the year ended 31 December 2013.

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

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

THE BOARD OF DIRECTORS

BOARD COMPOSITION

The Board currently comprises 10 members, consisting of 3 Executive Directors, 1 Non-executive Director and his alternate and 5 Independent Non-executive Directors. The biographical details of Directors are set out under "Biographical Details of Directors and Senior Management" on pages 38 to 43.

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

CHAIRMAN AND PRESIDENT (CHIEF EXECUTIVE OFFICER "CEO")

Code provision A.2.1 of the CG Code stipulates that the roles of chairman and chief executive should be separate 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 in the industry and the related industries. The Board believes that vesting the roles of both Chairman and President (CEO) in 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 two 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.

CORPORATE GOVERNANCE REPORT

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.

INDEPENDENT NON-EXECUTIVE DIRECTORS

During the year ended 31 December 2013, the Board at all times met the requirements of the Listing Rules relating to the appointment of independent non-executive directors representing at least one-third of the board. The Company had six Independent Non-executive Directors with three of whom possessing appropriate professional qualifications or accounting or related financial management expertise so that there is a strong independent element on the Board, which can effectively make independent judgment. One of the Independent Non-executive Directors possessing appropriate professional qualification or accounting or related financial management expertise resigned with effect from 19 March 2014.

The Company has received written annual confirmation from each of the Independent Non-executive Directors in respect of his independence in accordance with the independence guidelines set out in Rule 3.13 of the Listing Rules. The Company considers all Independent Non-executive Directors are independent.

NON-EXECUTIVE DIRECTORS AND DIRECTORS' RE-ELECTION

Code provision A.4.1 of the CG Code stipulates that non-executive directors shall be appointed for a specific term, subject to re-election, whereas code provision A.4.2 states that all directors appointed to fill a casual vacancy shall be subject to election by shareholders at the first general meeting after appointment and that every director, including those appointed for a specific term, shall be subject to retirement by rotation at least once every three years.

Each of the Directors of the Company is appointed for a specific term of not exceeding 3 years and is subject to retirement by rotation at least once every three years.

RESPONSIBILITIES, ACCOUNTABILITIES AND CONTRIBUTIONS OF THE BOARD AND MANAGEMENT

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

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

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.

CORPORATE GOVERNANCE REPORT

All Directors have full and timely access to all the information of the Company as well as the services and advice from the company secretary and senior management. The Directors are always provided in a timely manner with comprehensive, accurate and detailed information on the Company's operation through monthly report, business operation report, important projects report and financial report so as to enable the Directors to make decisions and perform their duties and responsibilities. The Directors may, upon request, seek independent professional advice in appropriate circumstances, at the Company's expenses for discharging their duties to the Company.

The Directors shall disclose to the Company details of other offices held by them and the Board regularly reviews the contribution required from each Director to perform his responsibilities to the Company.

The Board reserves for its decision all major matters relating to policy matters, strategies and budgets, internal control and risk management, material transactions (in particular those that may involve conflict of interests), financial information, appointment of directors and other significant operational matters of the Company. Responsibilities relating to implementing decisions of the Board, directing and co-ordinating the daily operation and management of the Company are delegated to the management.

BOARD DIVERSITY

Code provision A.5.6 of the CG code that came into effect from 1 September 2013 stipulates that the board shall have a policy concerning the diversity of board members, and should disclose the policy or a summary of the policy in the corporate governance report.

The Board has adopted a board diversity policy for setting out the approach to achieve diversity on the Board and the board diversity policy has been made available on the Company's website.

In assessing the Board composition, the Board would take into account various aspects set out in the Board diversity policy, including but not limited to gender, age, cultural and educational background, professional qualifications, skills, knowledge and industry and regional experience. The Board would discuss and agree on measurable objectives for achieving diversity on the Board, where necessary.

TRAINING INDUCTION AND CONTINUOUS PROFESSIONAL DEVELOPMENT OF DIRECTORS

Directors keep abreast of responsibilities as a director of the Company and of the conduct, business activities and development of the Company.

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

Directors should participate in appropriate continuous professional development to develop and refresh their knowledge and skills to ensure that their contribution to the Board remains informed and relevant. Internally-facilitated briefings for Directors will be arranged and reading material on relevant topics will be issued to Directors where appropriate. All Directors are encouraged to attend relevant training courses at the Company's expenses.

CORPORATE GOVERNANCE REPORT

All the Directors have actively participated in the continuous professional development by way of attending seminar and/or conferences and/or forums and/or reading materials. The Company arranged training sessions for all the Directors with the topic of guidelines on disclosure of inside information on 19 March 2013.

During the year ended 31 December 2013, the following Directors attended seminars/training sessions/in-house briefing/reading materials:

Directors	Attending seminar and/or conferences and/or forums	Reading journals, updates, articles and/or materials, etc.
Executive Directors		
Zhang Mi	✓	✓
Ren Jie	✓	✓
Liu Zhi	✓	✓
Non-Executive Directors		
Siegfried Meissner	✓	✓
Popin Su (alternate director to Siegfried Meissner)	✓	✓
Huang Dongyang (resigned with effect from 19 March 2013)	✓	✓
Independent Non-Executive Directors		
Liu Xiaofeng	✓	✓
Qi Daqing	✓	✓
Tai Kwok Leung, Alexander (resigned with effect from 19 March 2014)	✓	✓
Chen Guoming	✓	✓
Shi Xingquan	✓	✓
Guo Yanjun	✓	✓

BOARD COMMITTEES

The Board has established 5 committees, namely, the Audit Committee, Nomination Committee, Corporate Governance Committee, Remuneration Committee and Strategic Investment and Risk Control Committee for overseeing particular aspects of the Company's affairs. All Board committees of the Company are established with defined written terms of reference. The terms of reference of the Board committees are posted on the Company's website and the Stock Exchange's website and are available to Shareholders upon request.

Nomination Committee and Corporate Governance Committee were both dismissed with effect from 19 March 2013.

The list of the chairman and members of each Board committee is set out under "Corporate Information" on page 2.

AUDIT COMMITTEE

The Audit Committee comprises 6 Independent Non-executive Directors, namely, Qi Daqing (Chairman), Liu Xiaofeng, Tai Kwok Leung, Alexander who resigned on 19 March 2014, Chen Guoming, Shi Xingquan and Guo Yanjun, including 3 Independent Non-executive Directors who possess the appropriate professional qualifications or accounting or related financial management expertise.

The main duties of the Audit Committee include the following:

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

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

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

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

During the Year under review, the Audit Committee has reviewed the Group's annual results and annual report for the year ended 31 December 2013, the financial reporting and compliance procedures, the report from the management on the Company's internal control and risk management systems and processes, and the re-appointment of the external auditors.

The Audit Committee held two meetings during the year ended 31 December 2013 and the attendance records are set out under "Directors' Attendance Records" on page 53.

CORPORATE GOVERNANCE REPORT

REMUNERATION COMMITTEE

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

The primary objectives of the Remuneration Committee include the following:

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

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

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

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

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

The Remuneration Committee held a meeting during the year ended 31 December 2013 and the attendance records are set out under "Directors' Attendance Records" on page 53.

The remuneration policies of the Group focus on the efficiency of the employees and the position-value index, with reference to the individual ability and experience of an employee as well as the market value of the labour market, and emphasize on incentive-orientation and also the establishment of a fair and competitive remuneration system. For long-term incentive policies, the Company has adopted the Share Option Scheme and Restricted Share Award Scheme for eligible participants. Details are set out under the paragraphs headed "Share Option Scheme" and "Restricted Share Award Scheme" in the Report of the Directors.

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

STRATEGIC INVESTMENT AND RISK CONTROL COMMITTEE

The Strategic Investment and Risk Control Committee was formed by Zhang Mi (Chairman), Ren Jie, Liu Zhi, Shi Xingquan and Liu Xiaofeng. Huang Dongyang has resigned and Liu Xiaofeng has been appointed as the member of the Strategic Investment and Risk Control Committee for replacement both with effect from 19 March 2013.

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 2013 and the attendance records are set out under "Directors' Attendance Records" on page 53.

NOMINATION COMMITTEE

The Nomination Committee, dismissed on 19 March 2013, comprised 3 members, Zhang Mi (Chairman), Liu Xiaofeng and Qi Daqing, the majority of them are Independent Non-executive Directors.

The Board has taken over the duties of Nomination Committee and reviewed its own structure, size and composition including taking into account of board diversity policy of the Company regularly to ensure that it has a balance of expertise, skills and experience and diversity of board members appropriate for the requirements of the business of the Company.

The following primary objectives of the Nomination Committee were taken over by the Board:

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

CORPORATE GOVERNANCE REPORT

The Nomination Committee held a meeting during the year ended 31 December 2013 prior to its dismissal and the attendance records are set out under "Directors' Attendance Records" on page 53.

CORPORATE GOVERNANCE COMMITTEE

The Corporate Governance Committee, dismissed on 19 March 2013, comprised all the 6 Independent Non-executive Directors, namely Liu Xiaofeng (Chairman), Qi Daqing, Tai Kwok Leung Alexander (resigned with effect from 19 March 2014), Chen Guoming, Shi Xingquan and Guo Yanjun.

The Audit Committee has taken over the duties of the Corporate Governance Committee and would be responsible for reviewing the compliance of the corporate governance issues, the corporate governance report and the corporate governance policy.

The following main duties of the Corporate Governance Committee were taken over by the Audit Committee:

- 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 held a meeting during the year ended 31 December 2013 prior to its dismissal and the attendance records are set out under "Directors' Attendance Records" on page 53.

ATTENDANCE RECORD OF DIRECTORS AND COMMITTEE MEMBERS

During the year ended 31 December 2013, five Board meetings including 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.

CORPORATE GOVERNANCE REPORT

The attendance record of each Director at the meetings of the Board, the Audit Committee, the Nomination Committee, the Remuneration Committee, the Corporate Governance Committee and the Strategic Investment and Risk Control Committee during the year ended 31 December 2013 are set out below:

	Attendance/Number of Meetings						
Name of Director	Board	Nomination Committee**	Remuneration Committee	Audit Committee	Corporate Governance Committee**	Strategic Investment and Risk Control Committee	Annual General Meeting
Zhang Mi	05/05	01/01	01/01	–	–	02/02	01/01
Ren Jie	04/05 01*/05	–	–	–	–	02/02	01/01
Liu Zhi	05/05	–	–	–	–	02/02	0/01
Siegfried Meissner	0/05	–	–	–	–	–	0/01
Popin Su (the alternate director to Siegfried Meissner)	04/05	–	–	–	–	–	0/01
Huang Dongyang#	01/01	–	–	–	–	01/01	–
Liu Xiaofeng	05/05	01/01	01/01	02/02	01/01	01+/02	01/01
Qi Daqing	03/05 01*/05	01/01	01/01	02/02	01/01	–	0/01
Tai Kwok Leung, Alexander##	05/05	–	–	02/02	01/01	–	01/01
Chen Guoming	05/05	–	–	02/02	01/01	–	0/01
Shi Xingquan	05/05	–	–	02/02	01/01	02/02	0/01
Guo Yanjun	04/05	–	–	02/02	01/01	–	0/01

* Director had appointed proxy to attend meeting
** dismissed with effect from 19 March 2013
# resigned with effect from 19 March 2013
+ appointed with effect from 19 March 2013
resigned with effect from 19 March 2014

Apart from regular Board meetings, the Chairman also held meetings with the Non-executive Directors (including Independent Non-executive Directors) without the presence of Executive Directors during the Year.

CORPORATE GOVERNANCE REPORT

DIRECTORS' RESPONSIBILITY FOR FINANCIAL REPORTING IN RESPECT OF THE FINANCIAL STATEMENTS

The Directors acknowledge their responsibility for preparing the financial statements of the Company for the year ended 31 December 2013.

The Directors are not aware of any material uncertainties relating to events or conditions that may cast significant doubt upon the Company's ability to continue as a going concern.

The statement of the independent auditors of the Company about their reporting responsibilities on the financial statements is set out in the Independent Auditors' Report on pages 80 to 81.

Where appropriate, a statement will be submitted by the Audit Committee explaining its recommendation regarding the selection, appointment, resignation or dismissal of external auditors and the reasons why the Board has taken a different view from that of the Audit Committee.

AUDITORS' REMUNERATION

During the year ended 31 December 2013, the remuneration paid to the Company's auditors, Messrs KPMG, is set out below:

Category of Service	Fees (in Renminbi)
Audit Services	2,304,000
Non-audit Services	
— Reviewing interim financial statements	758,000
— Other	50,000
Total	3,112,000

The auditors' remuneration disclosed in note 6(c) to the consolidated financial statements included the remuneration paid to KPMG as detailed above and the remuneration paid to domestic auditors of the Company's subsidiaries.

INTERNAL CONTROLS

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

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 Group has, under the guidance and supervision of the Board and its Committees, conducted the construction of the following internal control and taken the following measures to strengthen its internal control.

FINANCIAL MANAGEMENT

The Company attaches great importance to the construction and improvement of the internal control system of financial management, proactively constructs and completes each of the internal controls of financial management system, revises and improves them as and when appropriate according to the development needs and changes of external and internal environment of the Group and ensures to effectively perform each of the internal controls of financial management system through perspective plans, procedural control and result examination.

The internal control system of the financial management of the Company mainly includes:

1. Financial organization and management: the Company has formulated the functional division organism for the financial system of the Group, proactively improved the financial management structure of the Group and ensured a scientific and clear-cut functional division of the financial management of the Group, which has ensured the efficiency and effectiveness of the financial management of the Company.

2. Financial calculation and analysis management: the Company has formulated accounting calculation methods and rules as well as other management systems for the Group, and proactively strengthened the financial calculation and analysis work of the Group, which has ensured the truthfulness, accuracy and completeness of the financial information of the Company.

3. Funds management: the Company implements an unified and centralized funds management system and proactively intensifies the risk management and control work for funds, and has on this basis formulated and improved relevant management system. As for the organizational structure, duties and responsibilities, authorization, approval and payment procedures, account management and other matters, the Company has provided detailed rules to ensure the safety of using funds and smooth turnover of fund in order to enhance the efficiency in the use of funds.

CORPORATE GOVERNANCE REPORT

4. Budget management: the Company implements an comprehensive budget management system with unified planning and tiered administration. An annual budget of the Group will be adopted subject to the passing of approval of the Board, and then implemented and tracked for analysis on a monthly basis. The implementation of completed budget will be analyzed periodically with an analysis report to be incorporated in the result performance system of the Group for assessment and rewards or punishment.

5. Financial risk management: the Company takes the risk control very seriously, executes a prudent financial management policy and sound risk control rules to ensure that each risk be at an acceptable level for the Group, and maintains and constantly reinforces the capability of sustainable development. The Company prudently manages the status of debt balance, and through the integration of use of its own fund and other external financing to maintain the flexibility of finance, and vigorously exploits diverse financing channels.

INTERNAL AUDIT

The Company has specially established an internal audit and supervision department responsible for the internal control of the Group.

The internal audit and supervision department conducts regular supervision and examination over the business of the Group and also carries out the special supervision and examination for significant projects to regulated the management of the Group.

The internal audit and supervision department reports its work to the Audit Committee on a periodical basis while the Audit Committee reviews and approves the internal audit reports and the annual plan for internal audit annually. The audit opinions will be reported to the Board through the Audit Committee.

The Company has set up an independent reporting channel through which the staff of the Company can report the corrupt conducts of other staffs of the Company directly to the internal audit and supervision department, so that the Company can be held harmless from frauds and other misconducts.

MANAGEMENT OF PROCUREMENT AND LOGISTICS

The Company has planned and formulated a series of institutional documents for procurement and logistics regarding the supplier management, tendering and bidding management and the acts of the procurement and logistics personnel, the management of procurement, and improved the procurement procedures, all of which are helpful to enhancing the efficiency of the supply chain in the supply system.

The Company has proactively attempted the financing from the supply chain to make the payment methods more flexible, to effectively reduce pressure of the operational cash flow and to facilitate and promote the capacity of value-increasing of the supply chain.

The Company is actively exploring a set of replicated standards in line with the logistic model of the Company in order to create a sustained improvement atmosphere to provide a high efficient logistic services for production.

INFORMATION DISCLOSURE

The Company has formulated a set of continuing disclosure obligation procedures in response to the inside information provisions under the SFO and the Listing Rules.

During the Year, the Company had organized trainings for senior management and staff for several times regarding the information disclosure to strengthen their awareness of compliance so as to ensure that any one or more staff can timely identify, assess and report any material information of which once they are aware.

The Company proactively publishes voluntary announcements for the matters of significance involving the current development status of the Company so that Shareholders and investors can be timely aware of the current status of the business development of the Company.

The Company will continue to improve and enhance the internal control of the Company, review its effectiveness and introduce practices and procedures that can help strengthening the internal risk control.

COMPANY SECRETARIES

Corinna Leung of Tricor Services Limited, an external service provider, has been engaged by the Company as one of its Joint Company Secretaries. The Company's primary contact person was Mr. Liu Gangqiang, one of the Joint Company Secretaries of the Company, who resigned on 27 December 2013. The current primary contact person at the Company is He Bin who was appointed on 27 December 2013 as one of the Joint Company Secretaries of the Company.

Corinna Leung, the Joint Company Secretary, and Liu Ganqiang, the former Joint Company Secretary, have complied with Rule 3.29 of the Listing Rules by taking no less than 15 hours of the relevant professional training during the Year.

SHAREHOLDERS' RIGHTS

To safeguard Shareholder 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 poll results will be posted on the websites of the Company and of the Stock Exchange after Shareholders' meeting.

CORPORATE GOVERNANCE REPORT

CONVENING AN EXTRAORDINARY GENERAL MEETING BY SHAREHOLDERS

The Board may, whenever it thinks fit, convene an extraordinary general meeting. Extraordinary general meetings may be convened by the Board on requisition of one or more Shareholders' holding, at the date of deposit of the requisition, not less than one tenth of the paid up capital of the Company having the right of voting at general meetings. Such requisition shall be made in writing to the Board or the Secretary for the purpose of requiring an extraordinary general meeting to be called by the Board for the transaction of any business specified in such requisition. Such meeting shall be held within 2 months after the deposit of such requisition. If within 21 days of such deposit, the Board fails to proceed to convene such meeting, the requisitionist(s) himself (themselves) may do so in the same manner, and all reasonable expenses incurred by the requisitionist(s) as a result of the failure of the Board shall be reimbursed to the requisitionist(s) by the Company.

PUTTING FORWARD PROPOSALS AT GENERAL MEETINGS

There is no provision allowing Shareholders to move new resolutions at general meetings under the Cayman Islands Companies Law or the Articles of Association of the Company. Shareholders who wish to move a resolution may request the Company to convene a general meeting following the procedures set out in the preceding paragraph.

As regards, proposing a person for election as a director, please refer to the procedures available on the website of the Company.

PUTTING FORWARD ENQUIRIES TO THE BOARD

For putting forward any enquiries to the Board of the Company, Shareholders may send written enquiries to the Company.

Note: The Company will not normally deal with verbal or anonymous enquiries.

CONTACT DETAILS

Shareholders may send their enquiries or requests as mentioned above to the following:

Address: Room 2508, Harcourt House, 39 Gloucester Road, Wan Chai, Hong Kong

Email: shareholder@hhcp.com.cn

For the avoidance of doubt, Shareholders must deposit and send the original duly signed written requisition, notice or statement, or enquiry (as the case may be) to the above address or 99 East Road, Information Park, Jinniu District, Chengdu, Shichuan, People's Republic of China and provide their full name, contact details and identification in order to give effect thereto. Shareholders' information may be disclosed as required by law.

COMMUNICATION 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 Audit Committee, Nomination Committee, Remuneration Committee, Corporate Governance Committee and Strategic Investment and Risk Control 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 of Shareholders. Notices to Shareholders for annual general meetings and all other general meetings will be sent to the Shareholders before such meetings pursuant to the requirement of the Listing Rules.

Information relating to the Company's financial results, corporate details, major projects and events are disseminated through publications of interim and annual reports, announcements, circulars and other corporate communications and publications available on the websites of the Stock Exchange and the Company.

During the Year under review, the Company has not made any changes to its Articles of Association. An up-to-date version of the Company's Articles of Association is also available on the websites of the Stock Exchange and the Company.

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.

REPORT OF THE DIRECTORS

The Board presents this annual report, together with the audited consolidated financial statements of the Group for the year ended 31 December 2013.

PRINCIPAL ACTIVITIES

The Company is an investment holding company. The Group principally engages in research, design, manufacture, setting and sale of land drilling rigs and related parts and components, design and manufacture the offshore drilling modules. 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 2013 are set out in the consolidated financial statements on pages 82 to 182 of this annual report.

The Board recommended a final dividend of HK6 cents per Share for the year ended 31 December 2013, which is subject to the approval of the shareholders of the Company at the forthcoming annual general meeting. The final dividend will be payable on or around 18 June 2014 to the shareholders of the Company whose names appear in the register of members of the Company as on 4 June 2014.

CLOSURE OF REGISTER OF THE MEMBERS

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

1. from Thursday, 15 May 2014 to Wednesday, 21 May 2014, both days inclusive, for the purpose of ascertaining shareholders' entitlement to attend and vote at the forthcoming annual general meeting. In order to be eligible to attend and vote at the forthcoming annual general meeting, all transfer documents accompanied by the relevant share certificates must be lodged for registration with the Hong Kong branch share registrar and transfer office of the Company, Computershare Hong Kong Investor Services Limited, at Shops 1712-1716, 17th floor, Hopewell Centre, 183 Queen's Road East, Wanchai, Hong Kong for registration not later than 4:30 p.m. on Wednesday, 14 May 2014; and

2. from Thursday, 29 May 2014 to Wednesday, 4 June 2014, both days inclusive, for the purpose of ascertaining shareholder's entitlement to the proposed final dividend. The record date for shareholder's entitlement to the proposed final dividend is Wednesday, 4 June 2014. In order to establish entitlements to the proposed final dividend, all transfer documents accompanied by the relevant share certificates must be lodged for registration with the Hong Kong branch share registrar and transfer office of the Company, Computershare Hong Kong Investor Services Limited, at Shops 1712–1716, 17th floor, Hopewell Centre, 183 Queen's Road East, Wanchai, Hong Kong for registration not later than 4:30 p.m. on Wednesday, 28 May 2014.

SHARE CAPITAL

Changes in the share capital of the Company during the Year are set out in note 33 to the consolidated 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

Save as the Trustee of the Restricted Share Award Scheme set out in note 29(d) to the consolidated financial statements, neither the Company nor any of its subsidiaries has purchased, sold or redeemed any of the Company's shares during the year ended 31 December 2013.

RESERVES

As of 31 December 2013, the Group has a total of approximately RMB4,463 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 consolidated financial statements.

SUBSIDIARIES

Details of the Company's principal subsidiaries as of 31 December 2013 are set out in note 16 to the consolidated financial statements.

SIGNIFICANT CONTRACT

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

DIRECTORS

The existing Directors of the Company during the Year and as of the date of this annual report are set out on page 2 the section "Corporate Information" of this annual report.

All the Directors of the Company holding their offices during the Year are set out in the section "Corporate Information".

In accordance with the Articles of Association, one third of the Directors (or closest to but not less than one third if the number 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. Liu Zhi, Mr. Qi Daqing and Mr. Guo Yanjun will retire from office by rotation at the forthcoming annual general meeting and will be eligible for re-election.

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

REPORT OF THE DIRECTORS

DIRECTORS' SERVICE CONTRACTS

Each of the Director of the Company is engaged on a service contract for a term of 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.

None of the Directors has a service contract with the Company which is not determinable 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 as 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 2013, details of remuneration for the Directors and Senior Management of the Company are set out in notes 8 and 37(f) to the consolidated financial statements.

The emoluments of the Executive Directors and Senior Management of the Company by bands are as follows:

	2013 Number of individuals
RMB0 to RMB1,000,000	–
RMB1,000,001 to RMB2,000,000	1
RMB2,000,001 to RMB3,000,000	1
RMB3,000,001 to RMB4,000,000	2
RMB4,000,001 to RMB5,000,000	3
RMB5,000,001 to RMB6,000,000	–
RMB6,000,001 to RMB7,000,000	–
RMB7,000,001 to RMB8,000,000	1

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 2013, the interests and short positions of each Director and Chief Executive in the Shares and underlying Shares of the Company and its associated corporations (within the meaning of the SFO), as recorded in the register required to be kept by the Company under Section 352 of Part XV of the SFO or as notified to the Company and the Stock Exchange pursuant to the Model Code contained in Appendix 10 to the Listing Rules were as follows:

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

	Long/Short position	Nature of interest	Number of shares held	% of the issued share capital of the Company
Mr. Zhang Mi	Long	Personal interest, corporate interest and settlor of a discretionary trust	1,520,879,331(1)(5)	46.95%
Mr. Ren Jie	Long	Personal interest, corporate interest and settlor of a discretionary trust	1,520,879,331(2)(5)	46.95%
Mr. Liu Zhi	Long	Personal interest, Corporate interest and settlor of a discretionary trust	1,520,879,331(3)(5)	46.95%
Mr. Guo Yanjun	Long	Corporate interest	2,100,000(4)	0.06%

(1) Zhang Mi individually owns 3,050,000 Shares. Yi Langlin, spouse of Zhang Mi owns 2,156,000 Shares. Zhang Mi is a member of the Concert Group. He is the settlor of a discretionary trust, The ZYL Family Trust, whose trustee, through Wealth Afflux Limited, holds the entire issued share capital of Ally Smooth Investments Limited, which in turn is the beneficial owner of 36% of the issued share capital of Ample Chance International Limited, which in turn is the beneficial owner of the entire issued share capital of Ally Giant Limited which holds 1,187,727,837 Shares. The Trustee of The ZYL Family Trust owns 157,800,000 Shares.

Ren Jie, another member of the Concert Group and the settlor of a discretionary trust, The RJDJ Victory Trust, individually owns 1,549,000 Shares. The Trustee of The RJDJ Victory Trust owns 33,227,200 Shares. The Trustee of a discretionary trust, The LZWM Family Trust, whose settlor is Liu Zhi, another member of the Concert Group, individually owns 1,250,000. The Trustee of The LZWM Family Trust owns 23,150,000 Shares. The Trustee of a discretionary trust, The FBX Family Trust, whose settlor is Fan Bing, another member of the Concert Group, individually owns 30,000 Shares. The Trustee of The FBX Family Trust owns 18,581,000 Shares. The Trustee of a discretionary trust, The ZHH Family Trust, whose settlor is Zuo Huixian, another member of the Concert Group, individually owns 210,000 Shares. The Trustee of The ZHH Family Trust owns 18,804,400 Shares. The Trustee of a discretionary trust, The Hong Xu Family Trust, whose settlor is Zhang Xu, another member of the Concert Group, individually owns 22,118 Shares. The Trustee of The Hong Xu Family Trust owns 13,557,400 Shares. The Trustee of a discretionary trust, The LXYY Family Trust, whose settlor is Liu Xuetian (deceased), another member of the Concert Group, owns 6,052,400 Shares. The other members of the Concert Group totally own 53,711,976 Shares.

REPORT OF THE DIRECTORS

(2) Ren Jie individually owns 1,549,000 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 1,187,727,837 Shares. The Trustee of The RJDJ Victory Trust owns 33,227,200 Shares.

Zhang Mi, another member of the Concert Group and the settlor of a discretionary trust, The ZYL Family Trust, individually owns 3,050,000 Shares. The Trustee of The ZYL Family Trust owns 157,800,000 Shares. Yi Langlin, spouse of Zhang Mi owns 2,156,000 Shares. The Trustee of a discretionary trust, The LZWM Family Trust, whose settlor is Liu Zhi, another member of the Concert Group, individually owns 1,250,000 Shares. The Trustee of The LZWM Family Trust owns 23,150,000 Shares. The Trustee of a discretionary trust, The FBX Family Trust, whose settlor is Fan Bing, another member of the Concert Group, individually owns 30,000 Shares. The Trustee of The FBX Family Trust owns 18,581,000 Shares. The Trustee of a discretionary trust, The ZHH Family Trust, whose settlor is Zuo Huixian, another member of the Concert Group, individually owns 210,000 Shares. The Trustee of The ZHH Family Trust owns 18,804,400 Shares. The Trustee of a discretionary trust, The Hong Xu Family Trust, whose settlor is Zhang Xu, another member of the Concert Group, individually owns 22,118 Shares. The Trustee of The Hong Xu Family Trust owns 13,557,400 Shares. The Trustee of a discretionary trust, The LXYY Family Trust, whose settlor is Liu Xuetian (deceased), another member of the Concert Group, owns 6,052,400 Shares. The other members of the Concert Group totally own 53,711,976 Shares.

(3) Liu Zhi individually owns 1,250,000 Shares. 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 1,187,727,837 Shares. The Trustee of The LZWM Family Trust owns 23,150,000 Shares.

Zhang Mi and Ren Jie, the other two members of the Concert Group, collectively hold 4,599,000 Shares. The Trustees of the two discretionary trusts, whose settlors are Zhang Mi and Ren Jie respectively, collectively own 191,027,200 Shares. Yi Langlin, spouse of Zhang Mi owns 2,156,000 Shares. The Trustee of a discretionary trust, The FBX Family Trust, whose settlor is Fan Bing, another member of the Concert Group, individually owns 30,000 Shares. The Trustee of The FBX Family Trust owns 18,581,000 Shares. The Trustee of a discretionary trust, The ZHH Family Trust, whose settlor is Zuo Huixian, another member of the Concert Group, individually owns 210,000 Shares. The Trustee of The ZHH Family Trust owns 18,804,400 Shares. The Trustee of a discretionary trust, The Hong Xu Family Trust, whose settlor is Zhang Xu, another member of the Concert Group, individually owns 22,118 Shares. The Trustee of The Hong Xu Family Trust owns 13,557,400 Shares. The Trustee of a discretionary trust, The LXYY Family Trust, whose settlor is Liu Xuetian (deceased), another member of the Concert Group, owns 6,052,400 Shares. The other members of the Concert Group totally own 53,711,976 Shares.

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

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

(B) SHARE OPTIONS OF THE COMPANY

	Long/ Short Position	Number of options held — Personal interest	Number of options held — Interest of the Concert Group
Mr. Zhang Mi	Long	13,837,000	26,046,000
Mr. Ren Jie	Long	5,687,000	34,196,000
Mr. Liu Zhi	Long	5,173,000	34,710,000
Mr. Qi Daqing	Long	2,000,000	–
Mr. Liu Xiaofeng	Long	2,000,000	–
Mr. Tai Kwok Leung, Alexander (Resigned with effect from 19 March 2014)	Long	1,700,000	–
Mr. Chen Guoming	Long	1,500,000	–
Mr. Shi Xingquan	Long	1,500,000	–
Mr. Guo Yanjun	Long	850,000	–

Saved as disclosed above, at 31 December 2013, 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.

REPORT OF THE DIRECTORS

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 2013, 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.

Name	Long/ Short Position	Number of Shares held: Personal interest: Share option	Personal interest: Shares Interest	Corporate interest	Corporate interest and settlor of a discretionary trust	Interest of the Concert Group	Total	% of the issued share capital of the Company
Ally Giant Limited	Long	–	1,187,727,837	–	–	373,034,494	1,560,762,331[1]	48.18%
Ample Chance International Limited	Long	–	–	1,187,727,837	–	373,034,494	1,560,762,331[2]	48.18%
Wealth Afflux Limited	Long	–	–	1,187,727,837	–	373,034,494	1,560,762,331[3]	48.18%
Ally Smooth Investments Limited	Long	–	–	1,187,727,837	–	373,034,494	1,560,762,331[3]	48.18%
Equity Trustee Limited	Long	–	–	–	1,504,258,237	–	1,504,258,237 [3] [5] [6] [9] [10] [14] [20] [22]	46.43%
Charm Moral International Limited	Long	–	–	1,187,727,837	–	373,034,494	1,560,762,331[4]	48.18%
Mowbray Worldwide Limited	Long	–	–	1,187,727,837	–	373,034,494	1,560,762,331[5]	48.18%
Ecotech Enterprises Corporation	Long	–	–	1,187,727,837	–	373,034,494	1,560,762,331[6]	48.18%
Mr. Zheng Yong	Long	2,085,000	20,100,903	1,187,727,837	–	350,848,591	1,560,762,331[7]	48.18%
Beauty Clear Holdings Limited	Long	–	–	1,187,727,837	–	373,034,494	1,560,762,331[8]	48.18%
Mr. Zuo Huixian	Long	1,734,000	210,000	–	1,206,532,237	352,286,094	1,560,762,331[9]	48.18%
Vast & Fast Corporation	Long	–	–	1,187,727,837	–	373,034,494	1,560,762,331[9]	48.18%
Mr. Zhang Xu	Long	1,833,000	22,118	–	1,201,285,237	357,621,976	1,560,762,331[10]	48.18%
Cavendish Global Corporation	Long	–	–	1,187,727,837	–	373,034,494	1,560,762,331[10]	48.18%
Elegant Scene International Limited	Long	–	–	1,187,727,837	–	373,034,494	1,560,762,331[11]	48.18%
Mr. Wang Jiangyang	Long	1,191,000	6,752,600	1,187,727,837	–	365,090,894	1,560,762,331[11]	48.18%
Mr. Chen Jun	Long	872,000	4,091,677	1,187,727,837	–	368,070,817	1,560,762,331[12]	48.18%
Believe Power International Limited	Long	–	–	1,187,727,837	–	373,034,494	1,560,762,331[13]	48.18%
Mr. Fan Bing	Long	1,744,000	30,000	–	1,206,308,837	352,679,494	1,560,762,331[14]	48.18%
Brondesbury Enterprises Limited	Long	–	–	1,187,727,837	–	373,034,494	1,560,762,331[14]	48.18%
Mr. Zhang Yanyong	Long	1,480,000	5,561,720	1,187,727,837	–	365,992,774	1,560,762,331[15]	48.18%
Mr. Ao Pei	Long	440,000	1,493,450	1,187,727,837	–	371,101,044	1,560,762,331[16]	48.18%
Mr. Tian Diyong	Long	550,000	1,050,400	1,187,727,837	–	371,434,094	1,560,762,331[17]	48.18%
Mr. Shen Dingjian	Long	262,000	1,285,720	1,187,727,837	–	371,486,774	1,560,762,331[18]	48.18%
Benefit Way International Limited	Long	–	–	1,187,727,837	–	373,034,494	1,560,762,331[19]	48.18%
Mr. Liu Xuetian (deceased)	Long	–	–	–	1,193,780,237	366,982,094	1,560,762,331[20]	48.18%
Dobson Global Inc.	Long	–	–	1,187,727,837	–	373,034,494	1,560,762,331[20]	48.18%
Ms. Qu Yihong	Long	–	–	1,193,780,237	–	366,982,094	1,560,762,331[21]	48.18%
Ms. Liu Ying	Long	–	–	1,193,780,237	–	366,982,094	1,560,762,331[21]	48.18%
Mr. Zhou Bing	Long	1,445,000	9,038,974	–	1,187,727,837	362,550,520	1,560,762,331[22]	48.18%

REPORT OF THE DIRECTORS

Name	Long/ Short Position	Personal interest: Share option	Personal interest: Shares Interest	Corporate interest	Corporate interest and settlor of a discretionary trust	Interest of the Concert Group	Total	% of the issued share capital of the Company
				Number of Shares held				
Darius Enterprises Limited	Long	–	–	1,187,727,837	–	373,034,494	1,560,762,331[22]	48.18%
Ms. Lu Lan	Long	520,000	1,395,892	1,187,727,837	–	371,118,602	1,560,762,331[23]	48.18%
Mr. Tian Yu	Long	330,000	1,623,240	1,187,727,837	–	371,081,254	1,560,762,331[24]	48.18%
Mr. Li Hanqiang	Long	215,000	611,000	1,187,727,837	–	372,208,494	1,560,762,331[25]	48.18%
Mr. Liu Yingguo	Long	242,000	240,000	1,187,727,837	–	372,552,494	1,560,762,331[26]	48.18%
Mrs. Liu Lulu	Long	243,000	466,400	1,187,727,837	–	372,325,094	1,560,762,331[27]	48.18%
The Capital Group Companies, Inc.	Long	–	–	230,071,000	–	–	230,071,000[28]	7.10%
Yi Langlin	Long	–	2,156,000 1,558,606,331 (family interest)		–	–	1,560,762,331[29]	48.18%

(1) Ally Giant Limited is wholly-owned by Ample Chance International Limited and holds 1,187,727,837 Shares.

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

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

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

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

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

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

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

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

REPORT OF THE DIRECTORS

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

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

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

(13) Believe Power International Limited is owned approximately 32.72% by Brondesbury Enterprises Limited, approximately 29.16% by Zhang Yanyong, approximately 7.30% by Ao Pei, approximately 2.85% by Tian Diyong, approximately 2.24% by Shen Dingjian, and a total of approximately 25.73% 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 7.30% of the issued share capital of Believe Power International Limited, which in turn is the beneficial owner of approximately 12.71% of the issued share capital of Ample Chance International Limited. Ao Pei is a member of the Concert Group.

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

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

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

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

(21) Qu Yihong and Liu Ying, family members of Liu Xuetian (deceased), are deemed to be interested in 1,193,780,237 Shares as directors of Dobson Global Inc..

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

REPORT OF THE DIRECTORS

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

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

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

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

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

(28) The Capital Group Companies, Inc is the holding Company of Capital Group International, Inc., which is the holding company of various subsidiaries collectively holding 230,071,000 Shares.

(29) Yi Langlin, spouse of Zhang Mi, is deemed to be interested in 1,560,762,331 Shares.

Save as disclosed above, to the best of the Directors and the Chief Executives of the Company's knowledge, as at 31 December 2013, 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 2013, none of the grantees has exercised the share options granted to him under the Pre-IPO share option scheme and 3,316,000 shares options have been lapsed.

Each share option granted under the Pre-IPO share option scheme is exercisable within a period of five years commencing from 7 March 2008 (the "Listing Date") and the vesting period is ten years from the date of grant. As at 31 December 2013, the total number of the share options granted (if not cancelled) or 60,000,000 share options can be exercised under the Pre-IPO share option scheme.

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

REPORT OF THE DIRECTORS

(B) SHARE OPTION SCHEME AFTER LISTING

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

Purpose

The Company operates the Share Option Scheme for the purpose of providing incentive and rewards to participants who contribute to the success of the Group's operation and/or for the purpose that the Group may recruit or retain high calibre employees and attract people for the Group. The Share Option Scheme may provide the participants with opportunity of holding the Shares of the Company individually, and (a) facilitate the participants to use their best effort to improve their performance and effectiveness; and (b) attract and retain participants who are significant to long term development and profitability of the Group.

Participants

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

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

The total number of Shares available for issue under the Share Option Scheme upon exercise of all outstanding share options granted and yet to be exercised (excluding share options lapsed in accordance with the terms of the Share Option Scheme) was 65,480,000 Shares, representing approximately 2.02% of the issued share capital of the Company as at the date of this annual report.

Maximum entitlement of each participant

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

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

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

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

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

Amounts to be paid on acceptance of share options

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

Basis of determining the exercise price

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

REPORT OF THE DIRECTORS

Condition and Termination of the share options

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

The remaining life of the Share Option Scheme

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

Details of the grant under the Share Option Scheme ended 31 December 2013 were as follows:

Date of grant	Number of share options granted	Exercise price per Share (HK$)	Exercise period of share options	Valid period of the share options
15 April 2009	60,000,000	1.27	up to 30% of the share options granted to each grantee from 1 December 2009 to 14 April 2010; up to 60% of the share options granted to each grantee on or before 14 April 2011; all the remaining share options granted to each grantee on or after 15 April 2011	up to 14 April 2019
11 October 2010	2,200,000	1.05	up to 40% of the share options granted to each grantee from 25 October 2010 to 10 October 2011; up to 70% of the share options granted to each grantee on or before 10 October 2012; all the remaining share options granted to each grantee on or after 11 October 2012	up to 10 October 2020
20 June 2011	7,600,000	0.83	up to 30% of the share options granted to each grantee from 19 July 2011 to 19 June 2012; up to 60% of the share options granted to each grantee on or before 19 June 2013; all the remaining share options granted to each grantee on or after 20 June 2013	up to 19 June 2021
5 April 2012	15,400,000	1.19	up to 30% of the share options granted to each grantee from 5 April 2013 to 4 April 2014; up to 60% of the share options granted to each grantee on or before 4 April 2015; all the remaining share options granted to each grantee on or after 5 April 2015	up to 4 April 2022

REPORT OF THE DIRECTORS

Particulars and movements of share options under the Share Option Scheme during the year ended 31December 2013 were as follows:

NUMBER OF SHARE OPTIONS

Name or category of participant	Number of share options						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$
	Outstanding as at 01/01/2013	Granted during the year ended 31 December 2013	Exercised during the year ended 31 December 2013	Forfeited/ lapsed during the year ended 31 December 2013	Cancelled during the year ended 31 December 2013	Outstanding as at 31/12/2013				
Directors										
Mr. Zhang Mi	3,937,000	–	–	–	–	3,937,000	15/04/2009	01/12/2009-14/04/2019	1.27	1.29
Mr. Liu Zhi	2,373,000	–	–	–	–	2,373,000	15/04/2009	01/12/2009-14/04/2019	1.27	1.29
Mr. Ren Jie	2,587,000	–	–	–	–	2,587,000	15/04/2009	01/12/2009-14/04/2019	1.27	1.29
Mr. Chen Guoming	750,000	–	–	–	–	750,000	15/04/2009	01/12/2009-14/04/2019	1.27	1.29
	750,000	–	–	–	–	750,000	20/06/2011	19/07/2011-19/06/2021	0.83	0.79
Mr. Liu Xiaofeng	1,000,000	–	–	–	–	1,000,000	15/04/2009	01/12/2009-14/04/2019	1.27	1.29
	1,000,000	–	–	–	–	1,000,000	20/06/2011	19/07/2011-19/06/2021	0.83	0.79
Mr. Qi Daqing	1,000,000	–	–	–	–	1,000,000	15/04/2009	01/12/2009-14/04/2019	1.27	1.29
	1,000,000		–	–	–	1,000,000	20/06/2011	19/07/2011-19/06/2021	0.83	0.79
Mr. Tai Kwok Leung,	850,000	–	–	–	–	850,000	15/04/2009	01/12/2009-14/04/2019	1.27	1.29
Alexander (Resigned with effect from 19 March 2014)	850,000	–	–	–	–	850,000	20/06/2011	19/07/2011-19/06/2021	0.83	0.79
Mr. Shi Xingquan	750,000	–	–	–	–	750,000	15/04/2009	01/12/2009-14/04/2019	1.27	1.29
	750,000	–	–	–	–	750,000	20/06/2011	19/07/2011-19/06/2021	0.83	0.79
Mr. Guo Yanjun	850,000	–	–	–	–	850,000	20/06/2011	19/07/2011-19/06/2021	0.83	0.79
Sub-total	18,447,000	–	–	–	–	18,447,000				
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
	250,000	–	–	–	–	250,000	05/04/2012	05/04/2013-04/04/2022	1.19	1.20
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. Tian Diyong	195,000	–	–	–	–	195,000	15/04/2009	01/12/2009-14/04/2019	1.27	1.29
Mr. Shen Dingjian	87,000	–	–	–	–	87,000	15/04/2009	01/12/2009-14/04/2019	1.27	1.29
Mr. Zhou Bing	695,000	–	–	–	–	695,000	15/04/2009	01/12/2009-14/04/2019	1.27	1.29
Ms. Lv Lan	174,000	–	174,000	–	–	0	15/04/2009	01/12/2009-14/04/2019	1.27	1.29
	250,000	–	75,000	–	–	175,000	05/04/2012	05/04/2013-04/04/2022	1.19	1.20
Mr. Tian Yu	275,000	–	275,000	–	–	0	15/04/2009	01/12/2009-14/04/2019	1.27	1.29
	90,000	–	–	–	–	90,000	05/04/2012	05/04/2013-04/04/2022	1.19	1.20
Mr. Li Hanqiang	130,000	–	130,000	–	–	0	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	6,064,000	–	654,000	–	–	5,410,000				
Other										
Employee	31,854,500	–	6,636,300	48,000	–	25,170,200	15/04/2009	01/12/2009-14/04/2019	1.27	1.29
Employee	400,000	–	149,000	–	–	251,000	11/10/2010	25/10/2010-10/10/2020	1.05	1.01
Employee	2,300,000	–	207,000	–	–	2,093,000	20/06/2011	19/07/2011-19/06/2021	0.83	0.79
Employee	14,810,000	–	388,000	119,000	–	14,303,000	05/04/2012	05/04/2013-04/04/2022	1.19	1.20
Sub-total	49,364,500	–	7,380,300	167,000	–	41,817,200				
Total	73,875,500	–	8,034,300	167,000	–	65,674,200				

REPORT OF THE DIRECTORS

RESTRICTED SHARE AWARD SCHEME

On 30 December 2011, the Board approved and adopted a restricted share award scheme in which Selected Participant(s) including any Employee or Director (including, without limitation, any Executive Directors, Non-executive Directors or Independent Non-executive Directors), any consultant or adviser (whether on any employment or contractual or honorary basis and whether paid or unpaid) of the Company or any member of the Group, who in the absolute opinion of the Board, have contributed to the Company or the Group. Pursuant to the Scheme Rules, existing Shares will be purchased by the Trustee from the market out of cash contributed by the Company and be held in trust for the relevant Selected Participant until such Shares are vested with the relevant Selected Participants in accordance with the Scheme Rules. The Scheme shall be effective for a term of 10 years commencing on the Adoption Date subject to any early termination as may be determined by the Board. The Board will implement the Scheme in accordance with the Scheme Rules including providing necessary funds to the Trustee to purchase for Shares up to 5% of the issued share capital of the Company from time to time. The Selected Participant is not entitled to receive any income or distribution, such as dividend derived from the Restricted Shares allocated to him, prior to the vesting of the Restricted Shares in the Selected Participants. As at 31 December 2013, the Trustee has purchased 97,817,000 of the Company's Shares, accounting for 3.01% of the issued share capital of the Company and a total of 35,917,700 shares were granted to the Selected Participants.

Particulars and movements of the Restricted Share Award Scheme during the year ended 31 December 2013 were as follows:

		Number of Shares						
Date of grant	Grant price Per Share HK$	Outstanding as at 01/01/2013	Purchased during the year ended 31 December 2013	Granted during the year ended 31 December 2013	Vested during the year ended 31 December 2013	Cancelled during the year ended 31 December 2013	Outstanding as at 31/12/2013	Vesting period
20/03/2013	1.27	47,817,000	49,000,000	34,917,700	34,727,700	190,000	62,089,300	50% of the Restricted Shares granted were vested on 20 May 2013; the remaining 50% were vested on 20 December 2013
04/07/2013	1.27	–	1,000,000	1,000,000	1,000,000	–	–	100% were Vested on 20 December 2013
Total		47,817,000	50,000,000	35,917,700	35,727,700	190,000	62,089,300	

CONTINUING CONNECTED TRANSACTIONS

During the Year, the Group has the following continuing connected transactions which are required to be disclosed in this report in accordance with Chapter 14A of the Listing Rules. For items 1 and 2, disclosure by way of announcement and independent shareholder's approval have been made and obtained in compliance with the requirement of Chapter 14A of the Listing Rules. Nabors Group is not a related party as defined in the Group's accounting policy in note 2(z) to the consolidated financial statements. Accordingly, the transactions with Nabors Group included in items 1 and 2 were not included in the material related party transactions as disclosed in note 37(b) to the consolidated financial statements. For item 3, the Purchase Framework Agreement and item 4, the Supplementary Agreement (as defined below) were disclosed by way of announcements in accordance with requirement of Chapter 14A of the Listing Rules and included in Note 37(b) to the consolidated financial statements as they constituted material related party transactions. Certain related party transactions disclosed in Note 37(b) to the consolidated financial statements were not disclosed below as they fulfilled the exemption requirements of Chapter 14A of the Listing Rules.

The equity interests held by Nabors Group in the Company fell below 10% since 27 March 2013 based on the information publicly available to the Company. Accordingly, Nabors Group no longer met the definition of connected person under Chapter 14A of the Listing Rules from 27 March 2013 and up to the date of this report.

1. SALES FRAMEWORK AGREEMENT ENTERED INTO WITH NABORS GROUP

Nabors Group comprises of Nabors Industries Ltd. and its subsidiaries. Nabors Group, through Nabors International II Limited, held approximately 13.96% equity interests in the Company as at the time when the Company and Nabors Industries Ltd. entered into the renewal sales framework agreement and the renewal purchases framework agreement (the "Renewal Sales Framework Agreement") and (the "Renewal Purchases Framework Agreement") on 19 November 2010 respectively and hence was a connected person of the Company under Chapter 14A of the Listing Rules.

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

During the period from 1 January 2013 to 27 March 2013 the total income received by the Group from Nabors Group in respect of sales of the Products and provision of the Services amounted to RMB30,716,979.

REPORT OF THE DIRECTORS

2. PURCHASES FRAMEWORK AGREEMENT ENTERED INTO WITH NABORS GROUP

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

During the period from 1 January 2013 to 27 March 2013, no purchases of the Products and Services was made by the Group from Nabors Group.

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 and Hongtai Company entered into a purchase framework agreement on 26 June 2012 to renew the Renewal Purchases Framwork Agreement made on 16 December 2009 (the “Purchase Framework Agreement”) for a term of three years commencing from 1 January 2013 and ending on 31 December 2015.

Pursuant to the Purchase Framework Agreement, Honghua Company shall purchase low value consumables, auxiliary accessories, tools, welding materials and work-protection items from Hongtai Company. The approved annual caps payable by Honghua Company to Hongtai Company under the Purchase Framework Agreement shall not exceed RMB26 million for each of the three financial years ending 31 December 2015 respectively.

During the Year, the total purchases made by the Group from Hongtai Company amounted to RMB21,066,664.

4. PURCHASE FRAMEWORK AGREEMENT AND SUPPLEMENTARY AGREEMENT ENTERED INTO WITH SHENYUAN COMPANY

Shenyuan Company is owned as to 34% by the spouse of Mr. Zhang Mi, the Executive Director of the Company. In this connection, Shenyuan Company is a connected person of the Company under Rule 14A.11(4) of the Listing Rules.

Honghua Oil & Gas Engineering and Shenyuan Company entered into a purchase framework agreement on 30 June 2012 (the “Purchase Framework Agreement”) for a term commencing from 30 June 2012 to 31 December 2014 pursuant to which Honghua Oil & Gas Engineering shall purchase from Shenyuan Company PDC drills. The approved annual caps payable by Honghua Oil & Gas Engineering to Shenyuan Company under the Purchase Framework Agreement is RMB2.8 million for each of the three financial years ended 31 December 2012, 31 December 2013 and ending 31 December 2014.

The continuing connected transactions contemplated under the Purchase Framework Agreement constituted exempted continuing connected transactions for the Company as they were de minimis transactions under Chapter 14A of the Listing Rules and were therefore exempted from the reporting, announcement, annual review and independent shareholders' approval requirements.

Given that Honghua Oil & Gas Engineering has a rapid development of well drilling contracting business and an increasing demand for drilling equipments and perishable goods in the process of drilling, the annual caps determined in the Purchase Framework Agreement no longer met Honghua Oil & Gas Engineering's need for the drills. In this regards, the Board of the Company approved Honghua Oil & Gas Engineering to enter into a supplementary agreement to the Purchase Framework Agreement (the "Supplementary Agreement") with Shenyuan Company.

On 25 March 2013, the Supplementary Agreement has been entered into between Honghua Oil & Gas Engineering and Shenyuan Company for a term commencing from 25 March 2013 and expiring on 31 December 2015.

According to the Supplementary Agreement, Honghua Oil & Gas Engineering will purchase PDC drills from Shenyuan Company. The approved annual caps payable by Honghua Oil & Gas Engineering to Shenyuan Company under the Supplementary Agreement are RMB12 million, RMB15 million and RMB18 million for each of the three financial years ending 31 December 2015 respectively. According to the applicable percentage ratios calculated, the continuing connected transactions contemplated under the Supplementary Agreement are subject to reporting, announcement and annual review requirements but exempt from independent shareholders' approval requirement under Chapter 14A of the Listing Rules. Announcement was published on 25 March 2013 regarding the continuing connected transactions contemplated under the Supplementary Agreement in accordance with the Listing Rules.

During the Year, the total purchases made by the Group from Shenyuan Company amounted to RMB7,565,000.00.

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

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

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

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

REPORT OF THE DIRECTORS

In accordance with Rule 14A.38 of the Listing Rules, the Company is required to obtain a letter from its auditor to confirm that these continuing connected transactions:

(1) have received the approval of the Board of Directors of the Company;

(2) were made in accordance with the pricing policy of the Company;

(3) were conducted pursuant to the relevant agreement governing those transactions;

(4) have not exceeded the annual caps disclosed in previous announcements.

The Company's auditors were engaged to report on the Group's continuing connected transactions in accordance with Hong Kong Standard on Assurance Engagements 3000 "Assurance Engagements Other Than Audits or Reviews of Historical Financial Information" and with reference to Practice Note 740 "Auditor's Letter on Continuing Connected Transactions under the Hong Kong Listing Rules" issued by the Hong Kong Institute of Certified Public Accountants. The auditors have issued to the Board an unqualified letter containing their findings and conclusions in respect of the continuing connected transactions disclosed by the Group in pages 75 to 77 of this annual report in accordance with Rule 14A.38 of Listing Rules. A copy of the auditor's letter has also been provided to the Stock Exchange.

BANK LOANS

Details of our bank loans and other borrowings are set out in notes 26 and 34(c) to the consolidated financial statements.

FINANCIAL SUMMARY

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

STAFF RETIREMENT AND BENEFIT SCHEME

Details of the staff retirement and benefit scheme are set out in notes 6(b), 28 and 29 to the consolidated financial statements.

FIXED ASSETS

Details of the changes of the fixed assets of the Group are set out in note 12 to the consolidated financial statements.

MAJOR CUSTOMERS AND SUPPLIERS

1. During the Year, the Group's five largest suppliers in total accounted for approximately 22.2% of total purchase, and the largest supplier accounted for approximately 5.9% of total purchase. Because there are a number of suppliers, the aggregate amount of purchase from the Group's five largest suppliers is less than 30% of total purchase.

2. During the Year, the Group's five largest customers accounted for approximately 53.3% of total sales and the largest customer accounted for approximately 27.2% of revenue.

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 2013, 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 income tax rate are set out in note 7 to the consolidated financial statements.

SUFFICIENCY OF PUBLIC FLOAT

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

MANAGEMENT CONTRACTS

There was no contracts concerning the management or administration of the whole or any substantial part of the business of the Company which was entered into or existed during the Year.

AUDITOR

The financial statements of the Group for the year ended 31 December 2013 have been audited by KPMG who will retire at the forthcoming annual general meeting and being eligible, offer themselves for re-appointment. A resolution to renew the appointment of KPMG as auditor of the Company will be proposed at the forthcoming annual general meeting of the Company.

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

Hong Kong, 19 March 2014

INDEPENDENT AUDITOR'S REPORT

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") and its subsidiaries (together the "Group") set out on pages 82 to 182, which comprise the consolidated and company statements of financial position as at 31 December 2013, the consolidated statements of profit or loss, the consolidated statement of profit or loss and other comprehensive income, the consolidated statement of changes in equity and the consolidated cash flow statement for the year then ended and a summary of significant accounting policies and other explanatory information.

DIRECTORS' RESPONSIBILITY FOR THE CONSOLIDATED FINANCIAL STATEMENTS

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

AUDITOR'S RESPONSIBILITY

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

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

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

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

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 2013 and of the Group's profit and cash flows for the year then ended in accordance with International Financial Reporting Standards and have been properly prepared in accordance with the disclosure requirements of the Hong Kong Companies Ordinance.

KPMG
Certified Public Accountants

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

19 March 2014

CONSOLIDATED STATEMENT OF PROFIT OR LOSS

for the year ended 31 December 2013 (Expressed in Renminbi)

	Note	2013 RMB'000	2012 RMB'000
Turnover	4(a)	**8,047,108**	5,068,447
Cost of sales		**(6,141,643)**	(3,321,440)
Gross profit		**1,905,465**	1,747,007
Other revenue	5	**176,469**	63,333
Other net income		**7,435**	2,084
Selling expenses		**(524,053)**	(553,623)
General and administrative expenses		**(595,508)**	(526,562)
Other operating expenses		**(121,442)**	(59,546)
Profit from operations		**848,366**	672,693
Finance income		**66,688**	74,737
Finance expenses		**(206,106)**	(45,478)
Net finance (expenses)/income	6(a)	**(139,418)**	29,259
Share of loss from joint ventures	17	**(7,948)**	(156)
Share of profit from an associate	18	**–**	7,662
Profit before taxation	6	**701,000**	709,458
Income tax	7(a)	**(125,750)**	(167,683)
Profit for the year		**575,250**	541,775
Attributable to:			
Equity shareholders of the Company		**537,617**	529,458
Non-controlling interests		**37,633**	12,317
Profit for the year		**575,250**	541,775
Earnings per Share (RMB cents)	11		
— Basic		**16.99**	16.58
— Diluted		**16.77**	16.54

The notes on pages 93 to 182 form part of these financial statements. Details of dividends payable to equity shareholders of the Company attributable to the profit for the year are set out in note 33(b).

CONSOLIDATED STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME

for the year ended 31 December 2013 (Expressed in Renminbi)

	2013 RMB'000	2012 RMB'000
Profit for the year	**575,250**	541,775
Other comprehensive income for the year:		
Items that may be reclassified subsequently to profit or loss:		
Net movement in the fair value reserve of available-for sale securities	**602**	–
Exchange differences on translation of financial statements of operations outside the PRC, net of tax	**(53,539)**	(10,967)
Total comprehensive income for the year	**522,313**	530,808
Attributable to:		
Equity shareholders of the Company	**484,312**	518,452
Non-controlling interests	**38,001**	12,356
Total comprehensive income for the year	**522,313**	530,808

The notes on pages 93 to 182 form part of these financial statements.

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

at 31 December 2013 (Expressed in Renminbi)

	Note	2013 RMB'000	2012 RMB'000
Non-current assets			
Fixed assets			
— Property, plant and equipment	12	2,148,103	1,142,122
— Interests in leasehold land held for own use under operating leases	12	361,890	303,410
— Freehold land	12	4,916	5,068
	12	2,514,909	1,450,600
Deposits paid for acquisition of leasehold land		147,320	152,006
Construction in progress	13	728,019	827,290
Intangible assets	14	213,637	201,806
Goodwill	15	13,484	–
Interests in joint ventures	17	47,924	57,181
Interest in an associate	18	9,000	–
Other investment	19	74,053	72,609
Trade and other receivables	21	676,050	370,002
Deferred tax assets	30(b)	123,975	96,407
Total non-current assets		4,548,371	3,227,901
Current assets			
Inventories	20	2,801,307	2,730,940
Trade and other receivables	21	3,961,427	2,105,804
Gross amount due from customers for contract work	22	176,158	–
Amounts due from related companies	37(c)	44,819	55,970
Current tax recoverable	30(a)	16,406	1,502
Other financial assets	23	804,102	315,036
Pledged bank deposits	24	593,337	424,592
Bank deposits maturing over three months		8,619	–
Cash and cash equivalents	25	1,274,509	984,131
Total current assets		9,680,684	6,617,975

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

at 31 December 2013 (Expressed in Renminbi)

	Note	**2013 RMB'000**	2012 RMB'000
Current liabilities			
Interest-bearing borrowings	26	**3,273,544**	1,245,505
Trade and other payables	27	**4,240,962**	3,112,337
Amounts due to related companies	37(d)	**27,465**	5,593
Current tax payable	30(a)	**51,453**	96,311
Provisions	31	**168,421**	57,732
Total current liabilities		**7,761,845**	4,517,478
Net current assets		**1,918,839**	2,100,497
Total assets less current liabilities		**6,467,210**	5,328,398
Non-current liabilities			
Interest-bearing borrowings	26	**1,457,953**	737,514
Deferred tax liabilities	30(b)	**50,611**	2,157
Total non-current liabilities		**1,508,564**	739,671
NET ASSETS		**4,958,646**	4,588,727

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

at 31 December 2013 (Expressed in Renminbi)

	Note	2013 RMB'000	2012 RMB'000
CAPITAL AND RESERVES	33		
Share capital		**300,833**	300,192
Reserves		**4,462,518**	4,155,819
Total equity attributable to equity shareholders of the Company		**4,763,351**	4,456,011
Non-controlling interests		**195,295**	132,716
TOTAL EQUITY		**4,958,646**	4,588,727

Approved and authorised for issue by the board of directors on 19 March 2014

Zhang Mi
Director

Ren Jie
Director

The notes on pages 93 to 182 form part of these financial statements.

STATEMENT OF FINANCIAL POSITION

at 31 December 2013 (Expressed in Renminbi)

	Note	2013 RMB'000	2012 RMB'000
Non-current assets			
Intangible assets	14	153,311	192,005
Investments in subsidiaries	16	2,910,554	2,554,422
Total non-current assets		3,063,865	2,746,427
Current assets			
Other receivables		6,070	90
Amount due from subsidiaries	32	505,920	84,226
Amounts due from related parties		27	27
Cash and cash equivalents	25	19,570	22,378
Total current assets		531,587	106,721
Current liabilities			
Interest-bearing borrowings	26	179,428	–
Other payables	27	3,293	64,650
Total current liabilities		182,721	64,650
Net current assets		348,866	42,071
Total assets less current liabilities		3,412,731	2,788,498
Non-current liabilities			
Interest-bearing borrowings	26	717,711	–
Total non-current liabilities		717,711	–
NET ASSETS		2,695,020	2,788,498

STATEMENT OF FINANCIAL POSITION

at 31 December 2013 (Expressed in Renminbi)

	Note	2013 RMB'000	2012 RMB'000
CAPITAL AND RESERVES	33		
Share capital		**300,833**	300,192
Reserves		**2,394,187**	2,488,306
TOTAL EQUITY		**2,695,020**	2,788,498

Approved and authorised for issue by the board of directors on 19 March 2014

Zhang Mi
Director

Ren Jie
Director

The notes on pages 93 to 182 form part of these financial statements.

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

for the year ended 31 December 2013 (Expressed in Renminbi)

		Attributable to equity shareholders of the Company										
	Note	Share capital (note 33(c)) RMB'000	Share premium (note 33(d)(i)) RMB'000	Other reserve (note 33(d)(ii)) RMB'000	Capital reserve (note 33(d)(iii)) RMB'000	Surplus reserve (note 33(d)(iv)) RMB'000	Exchange reserve (note 33(d)(v)) RMB'000	Shares held for share award scheme (note 29(d)) RMB'000	Retained profits RMB'000	Sub-total RMB'000	Non-controlling interests RMB'000	Total equity RMB'000
At 1 January 2012		299,593	2,477,519	57,472	493,810	220,033	(193,135)	–	703,291	4,058,583	116,275	4,174,858
Changes in equity for 2012:												
Profit for the year		–	–	–	–	–	–	–	529,458	529,458	12,317	541,775
Other comprehensive income		–	–	–	–	–	(11,006)	–	–	(11,006)	39	(10,967)
Total comprehensive income		–	–	–	–	–	(11,006)	–	529,458	518,452	12,356	530,808
Acquisition of a business		–	–	–	–	–	–	–	–	–	36,000	36,000
Acquisition of non-controlling interests		–	–	(5,880)	–	–	–	–	–	(5,880)	(23,081)	(28,961)
Liquidation of a subsidiary		–	–	–	–	–	–	–	–	–	981	981
Capital contribution arising on shareholders' indemnity	31(a)	–	–	–	27,469	–	–	–	–	27,469	–	27,469
Shares purchased under share award scheme	29(d)	–	–	–	–	–	–	(49,973)	–	(49,973)	–	(49,973)
Equity-settled share-based transactions arising from the share option schemes	29	–	–	–	4,809	–	–	–	–	4,809	–	4,809
Shares issued under share option schemes	29	599	9,469	–	(2,817)	–	–	–	–	7,251	–	7,251
Options lapsed under share option schemes	29	–	–	–	(736)	–	–	–	736	–	–	–
Dividends approved in respect of the previous financial year	33(b)	–	–	–	–	–	–	–	(104,700)	(104,700)	–	(104,700)
Dividends paid to non-controlling interests		–	–	–	–	–	–	–	–	–	(9,815)	(9,815)
Appropriation to surplus reserve		–	–	–	–	91,448	–	–	(91,448)	–	–	–
At 31 December 2012		300,192	2,486,988	51,592	522,535	311,481	(204,141)	(49,973)	1,037,337	4,456,011	132,716	4,588,727

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

for the year ended 31 December 2013 (Expressed in Renminbi)

		Attributable to equity shareholders of the Company											
	Note	Share capital (note 33(c)) RMB'000	Share premium (note 33(d)(i)) RMB'000	Other reserve (note 33(d)(ii)) RMB'000	Capital reserve (note 33(d)(iii)) RMB'000	Surplus reserve (note 33(d)(iv)) RMB'000	Exchange reserve (note 33(d)(v)) RMB'000	Fair value reserve (note 33(d)(vi)) RMB'000	Shares held for share award scheme (note 29(d)) RMB'000	Retained profits RMB'000	Sub-total RMB'000	Non-controlling interests RMB'000	Total equity RMB'000
At 1 January 2013		300,192	2,486,988	51,592	522,535	311,481	(204,141)	–	(49,973)	1,037,337	4,456,011	132,716	4,588,727
Changes in equity for 2013:													
Profit for the year		–	–	–	–	–	–	–	–	537,617	537,617	37,633	575,250
Other comprehensive income		–	–	–	–	–	(53,860)	555	–	–	(53,305)	368	(52,937)
Total comprehensive income		–	–	–	–	–	(53,860)	555	–	537,617	484,312	38,001	522,313
Acquisition of subsidiaries	35	–	–	–	–	–	–	–	–	–	–	31,432	31,432
Disposal of a subsidiary		–	–	(382)	–	–	–	–	–	–	(382)	1,399	1,017
Liquidation of a subsidiary		–	–	–	–	–	–	–	–	–	–	(1,903)	(1,903)
Shares purchased under share award scheme	29(d)	–	–	–	–	–	–	–	(146,233)	–	(146,233)	–	(146,233)
Amortisation arising from share award scheme	29(d)	–	–	–	73,466	–	–	–	–	–	73,466	–	73,466
Vested shares transferred from share award scheme	29(d)	–	–	–	(73,466)	–	–	–	71,588	37,722	35,844	–	35,844
Equity-settled share-based transactions arising from share option schemes	29	–	–	–	2,430	–	–	–	–	–	2,430	–	2,430
Shares issued under share option schemes	29	641	10,711	–	(3,347)	–	–	–	–	–	8,005	–	8,005
Options lapsed under share option schemes	29	–	–	–	(508)	–	–	–	–	508	–	–	–
Dividends approved in respect of the previous financial year	33(b)	–	–	–	–	–	–	–	–	(150,102)	(150,102)	–	(150,102)
Dividends paid to non-controlling interests		–	–	–	–	–	–	–	–	–	–	(6,350)	(6,350)
Appropriation to surplus reserve		–	–	–	–	38,267	–	–	–	(38,267)	–	–	–
At 31 December 2013		300,833	2,497,699	51,210	521,110	349,748	(258,001)	555	(124,618)	1,424,815	4,763,351	195,295	4,958,646

The notes on pages 93 to 182 form part of these financial statements.

CONSOLIDATED CASH FLOW STATEMENT

for the year ended 31 December 2013 (Expressed in Renminbi)

	Note	2013 RMB'000	2012 RMB'000
Operating activities			
Profit before taxation		**701,000**	709,458
Adjustments for:			
Amortisation and depreciation			
— intangible assets	14	**35,731**	34,647
— leasehold land held for use under operating leases	12(a)	**12,127**	6,560
— other fixed assets	12(a)	**193,535**	106,796
Gain on disposal of other financial assets	6(a)	**(6,345)**	(19,654)
Interest income		**(60,343)**	(34,650)
Interest expenses		**148,440**	30,791
Share of losses from joint ventures		**7,948**	156
Share of profit from an associate		**–**	(7,662)
Loss on disposals of fixed assets		**899**	639
Net loss on disposal/liquidation of subsidiaries		**1,000**	–
Gain on de-recognition of investment in an associate		**–**	(1,542)
Equity-settled share-based payment expenses arising from share option schemes and share award scheme		**75,896**	4,809
Foreign exchange loss/(gain)		**25,513**	(12,755)
Changes in working capital:			
Increase in inventories		**(60,616)**	(1,569,399)
Increase in trade and other receivables		**(2,223,993)**	(869,450)
Decrease in amounts due from related companies		**11,151**	8,884
Increase in pledged bank deposits		**(168,745)**	(358,980)
Increase in trade and other payables		**1,015,080**	1,553,207
Increase/(decrease) in amounts due to related companies		**21,872**	(22,697)
Increase in provisions		**110,689**	36,489
Cash used in operations		**(159,161)**	(404,353)
Income tax paid		**(164,991)**	(103,601)
Net cash used in operating activities		**(324,152)**	(507,954)

CONSOLIDATED CASH FLOW STATEMENT

for the year ended 31 December 2013 (Expressed in Renminbi)

	Note	2013 RMB'000	2012 RMB'000
Investing activities			
Payment for addition of fixed assets and construction in progress (excluding interests in leasehold land)		**(1,176,791)**	(498,416)
Proceeds from disposals of fixed assets		**1,748**	1,185
Payment for acquisition of subsidiaries	35	**(48,099)**	(27,000)
Payment for development project costs		**(31,697)**	(406)
Payment for acquisition of leasehold land		**–**	(84,792)
Interest received		**57,504**	18,172
Net (payment)/proceeds from sales and purchase of other financial assets and other investment		**(483,563)**	382,618
Capital contributions to joint ventures		**–**	(17,510)
Proceeds from bank deposits maturing over three months		**30,511**	9,100
Payment for bank deposits maturing over three months		**(39,130)**	–
Net cash used in investing activities		**(1,689,517)**	(217,049)
Financing activities			
Proceeds from new bank loans		**4,002,401**	2,232,505
Repayment of bank loans		**(1,253,923)**	(1,129,104)
Proceeds from shares issued under share option schemes		**8,005**	7,251
Proceeds from shares granted under share award scheme		**35,844**	–
Payment for purchase of shares under share award scheme	29(d)	**(146,233)**	(49,973)
Interest paid		**(176,760)**	(61,791)
Dividends paid to non-controlling interests		**(6,350)**	(9,815)
Dividends paid to equity shareholders of the Company	33(b)	**(150,102)**	(104,700)
Payment for acquisition of non-controlling interests		**–**	(28,961)
Net cash generated from financing activities		**2,312,882**	855,412
Net increase in cash and cash equivalents		**299,213**	130,409
Cash and cash equivalents at 1 January		**984,131**	851,847
Effect of foreign exchange rate changes		**(8,835)**	1,875
Cash and cash equivalents at 31 December	25	**1,274,509**	984,131

The notes on pages 93 to 182 form part of these financial statements.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

1 GENERAL INFORMATION

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

The consolidated financial statements for the year ended 31 December 2013 comprise the Company and its subsidiaries (collectively referred to as the "Group") and the Group's interests in an associate and joint ventures.

2 SIGNIFICANT ACCOUNTING POLICIES

(a) STATEMENT OF COMPLIANCE

These financial statements have been prepared in accordance with all applicable International Financial Reporting Standards ("IFRSs"), which collective term includes all applicable individual International Financial Reporting Standards, International Accounting Standards ("IASs") and Interpretations issued by the International Accounting Standards Board ("IASB") and the disclosure requirements of the Hong Kong Companies Ordinance. These financial statements also comply with the applicable disclosure provisions of the Rules Governing the Listing of Securities on the Stock Exchange of Hong Kong Limited. A summary of the significant accounting policies adopted by the Group is set out below.

The IASB has issued certain new and revised IFRSs that are first effective or available for early adoption for the current accounting period of the Group and the Company. Note 2(c) provides information on any changes in accounting policies resulting from initial application of these developments to the extent that they are relevant to the Group for the current and prior accounting periods reflected in these financial statements.

(b) BASIS OF PREPARATION OF THE FINANCIAL STATEMENTS

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

The measurement basis used in the preparation of the financial statements is the historical cost basis except that other financial assets are stated at their fair value as explained in the accounting policies set out in note 2(g).

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

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 3.

(c) CHANGES IN ACCOUNTING POLICIES

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

— Amendments to IAS 1, Presentation of financial statements — Presentation of items of other comprehensive income

— IFRS 10, Consolidated financial statements

— IFRS 11, Joint arrangements

— IFRS 12, Disclosure of interests in other entities

— IFRS 13, Fair value measurement

— Amendments to IFRS 7 — Disclosures — Offsetting financial assets and financial liabilities

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

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

(c) CHANGES IN ACCOUNTING POLICIES (continued)

Amendments to IAS 1, Presentation of financial statements — Presentation of items of other comprehensive income

The amendments require entities to present separately the items of other comprehensive income that would be reclassified to profit or loss in the future if certain conditions are met from those that would never be reclassified to profit or loss. The Group's presentation of other comprehensive income in the consolidated statement of profit or loss and other comprehensive income in these financial statements has been modified accordingly.

In addition, the Group has chosen to use the new titles "statement of profit or loss" and "statement of profit or loss and other comprehensive income" as introduced by the amendments in these financial statements.

IFRS 10, Consolidated financial statements

IFRS 10 replaces the requirements in IAS 27, Consolidated and separate financial statements relating to the preparation of consolidated financial statements and SIC 12 Consolidation — Special purpose entities. It introduces a single control model to determine whether an investee should be consolidated, by focusing on whether the entity has power over the investee, exposure or rights to variable returns from its involvement with the investee and the ability to use its power to affect the amount of those returns.

As a result of the adoption of IFRS 10, the Group has changed its accounting policy with respect to determining whether it has control over an investee. The adoption does not change any of the control conclusions reached by the Group in respect of its involvement with other entities as at 1 January 2013.

IFRS 11, Joint arrangements

IFRS 11, which replaces IAS 31, Interests in joint ventures, divides joint arrangements into joint operations and joint ventures. Entities are required to determine the type of an arrangement by considering the structure, legal form, contractual terms and other facts and circumstances relevant to their rights and obligations under the arrangement. Joint arrangements which are classified as joint operations under IFRS 11 are recognised on a line-by-line basis to the extent of the joint operator's interest in the joint operation. All other joint arrangements are classified as joint ventures under IFRS 11 and are required to be accounted for using the equity method in the Group's consolidated financial statements. Proportionate consolidation is no longer allowed as an accounting policy choice.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

(c) CHANGES IN ACCOUNTING POLICIES (continued)

IFRS 11, Joint arrangements (continued)

As a result of the adoption of IFRS 11, the Group has reclassified the investment from jointly controlled entity to joint venture. The investment continues to be accounted for using the equity method and therefore this reclassification does not have any material impact on the financial position and the financial result of the Group.

IFRS 12, Disclosure of interests in other entities

IFRS 12 brings together into a single standard all the disclosure requirements relevant to an entity's interests in subsidiaries, joint arrangements, associates and unconsolidated structured entities. The disclosures required by IFRS 12 are generally more extensive than those previously required by the respective standards. To the extent that the requirements are applicable to the Group, the Group has provided those disclosures in notes 16, 17 and 18.

IFRS 13, Fair value measurement

IFRS 13 replaces existing guidance in individual IFRSs with a single source of fair value measurement guidance. IFRS 13 also contains extensive disclosure requirements about fair value measurements for both financial instruments and non-financial instruments. To the extent that the requirements are applicable to the Group, the Group has provided those disclosures in note 34. The adoption of IFRS 13 does not have any material impact on the fair value measurements of the Group's assets and liabilities.

Amendments to IFRS 7 — Disclosures — Offsetting financial assets and financial liabilities

The amendments introduce new disclosures in respect of offsetting financial assets and financial liabilities. Those new disclosures are required for all recognised financial instruments that are set off in accordance with IAS 32, Financial instruments: Presentation and those that are subject to an enforceable master netting arrangement or similar agreement that covers similar financial instruments and transactions, irrespective of whether the financial instruments are set off in accordance with IAS 32.

The adoption of the amendments does not have an impact on these financial statements because the Group has not offset financial instruments, nor has it entered into master netting arrangement or similar agreement which is subject to the disclosures of IFRS 7 during the periods presented.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

(d) SUBSIDIARIES AND NON-CONTROLLING INTERESTS

Subsidiaries are entities controlled by the Group. The Group controls an entity when it is exposed, or has rights, to variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. When assessing whether the Group has power, only substantive rights (held by the Group and other parties) are considered.

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, transactions and cash flows 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.

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

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

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

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

In the Company's statement of financial position, an investment in a subsidiary is stated at cost less impairment losses (see note 2(l)).

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

(e) ASSOCIATES AND JOINT VENTURES

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

A joint venture is an arrangement whereby the Group or Company and other parties contractually agree to share control of the arrangement, and have rights to the net assets of the arrangement.

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

When the Group's share of losses exceeds its interest in the associate or the joint venture, 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 investee. For this purpose, the Group's interest is the carrying amount of the investment under the equity method together with the Group's long-term interests that in substance form part of the Group's net investment in the associate or the joint venture.

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

If an investment in an associate becomes an investment in a joint venture or vice versa, retained interest is not remeasured. Instead, the investment continues to be accounted for under the equity method.

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

(e) ASSOCIATES AND JOINT VENTURES (continued)

In all other cases, when the Group ceases to have significant influence over an associate or joint control over a joint venture, it is accounted for as a disposal of the entire interest in that investee, with a resulting gain or loss being recognised in profit or loss. Any interest retained in that former investee at the date when significant influence or joint control is lost is recognised at fair value and this amount is regarded as the fair value on initial recognition of a financial asset (see note 2(g)).

In the Company's statement of financial position, investments in associates and joint venture are stated at cost less impairment losses (see note 2(l)), unless classified as held for sale (or included in a disposal Group that is classified as held for sale) (see note 2(g)).

(f) GOODWILL

Goodwill represents the excess of

(i) the aggregate of the fair value of the consideration transferred, the amount of any non-controlling interest in the acquiree and the fair value of the Group's previously held equity interest in the acquiree; over

(ii) the net fair value of the acquiree's identifiable assets and liabilities measured as at the acquisition date.

When (ii) is greater than (i), then this excess is recognised immediately in profit or loss as a gain on a bargain purchase.

Goodwill is stated at cost less accumulated impairment losses. Goodwill arising on a business combination is allocated to each cash-generating unit, or Groups of cash generating units, that is expected to benefit from the synergies of the combination and is tested annually for impairment (see note 2(l)).

On disposal of a cash generating unit during the year, any attributable amount of purchased goodwill is included in the calculation of the profit or loss on disposal.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

(g) OTHER INVESTMENTS IN DEBT AND EQUITY SECURITIES

The Group's policies for investments in debt and equity securities, other than investments in subsidiaries, associates and joint ventures, are as follows:

Investments in debt and equity securities are initially stated at fair value, which is their transaction price unless it is determined that the fair value at initial recognition differs from the transaction price and that fair value is evidenced by a quoted price in an active market for an identical asset or liability or based on a valuation technique that uses only data from observable markets. Cost includes attributable transaction costs, except where indicated otherwise below. These investments are subsequently accounted for as follows, depending on their classification:

Investments in securities held for trading are classified as current assets. Any attributable transaction costs are recognised in profit or loss as incurred. At the end of the reporting period the fair value is remeasured, with any resultant gain or loss being recognised in profit or loss. The net gain or loss recognised in profit or loss does not include any dividends or interest earned on these investments as these are recognised in accordance with the policies set out in notes 2(v)(vii) and 2(v)(iii).

Dated debt securities that the Group has the positive ability and intention to hold to maturity are classified as held-to-maturity securities. Held-to-maturity securities are stated at amortised cost less impairment losses (see note 2(l)).

Investments in securities which do not fall into any of the above categories are classified as available-for-sale securities. At the end of each reporting period the fair value is remeasured, with any resultant gain or loss being recognised in other comprehensive income and accumulated separately in equity in the fair value reserve. As an exception to this, investments in equity securities that do not have a quoted price in an active market for an identical instrument and whose fair value cannot otherwise be reliably measured are recognised in the statement of financial position at cost less impairment losses (see note 2(l)). Dividend income from equity securities and interest income from debt securities calculated using the effective interest method are recognised in profit or loss in accordance with the policies set out in notes 2(v)(vii) and 2(v)(iii), respectively. Foreign exchange gains and losses resulting from changes in the amortised cost of debt securities are also recognised in profit or loss.

When the investments are derecognised or impaired (see note 2(l)), the cumulative gain or loss recognised in equity is reclassified to profit or loss. Investments are recognised/derecognised on the date the Group commits to purchase/sell the investments or they expire.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

(h) FIXED ASSETS AND DEPRECIATION

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

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

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

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

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

Where parts of an item of fixed asset have different useful lives, the cost of the item is allocated on a reasonable basis between the parts and each part is depreciated separately. Both the useful life of an asset and its residual value, if any, are reviewed annually.

(i) CONSTRUCTION IN PROGRESS

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

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

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

(j) INTANGIBLE ASSETS (OTHER THAN GOODWILL)

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

Other intangible assets represent the technology licences acquired from business combination granted by the holding company and are stated in the statement of financial position initially at fair value and subsequently at cost less accumulated amortisation and impairment losses (see note 2(l)).

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

— Capitalised development costs . . . . 10 years
— Technical know-how . . . . 10 years

Both the period and method of amortisation are reviewed annually.

(k) OPERATING LEASE CHARGES

Leases which do not transfer substantially all the risks and rewards of ownership of assets to the Group are accounted for as operating leases.

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

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

(l) IMPAIRMENT OF ASSETS

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

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

— significant financial difficulty of the debtor;

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

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

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

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

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

— For investments in associates and joint ventures accounted for under the equity method in the consolidated financial statements (see note 2(e)), the impairment loss is measured by comparing the recoverable amount of the investment with its carrying amount in accordance with note 2(l)(ii). The impairment loss is reversed if there has been a favourable change in the estimates used to determine the recoverable amount in accordance with note 2(l)(ii).

— For unquoted equity securities carried at cost, the impairment loss is measured as the difference between the carrying amount of the financial asset and the estimated future cash flows, discounted at the current market rate of return for a similar financial asset where the effect of discounting is material. Impairment losses for equity securities carried at cost are not reversed.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

(l) IMPAIRMENT OF ASSETS (continued)

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

— 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 effective of discounting is material. This assessment is made collectively where these financial assets share similar risk characteristics, such as similar past due status, and have not been individually assessed as impaired. Future cash flows for financial assets which are assessed for impairment collectively are based on historical loss experience for assets with credit risk characteristics similar to the collective group.

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

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

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

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

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

(l) IMPAIRMENT OF ASSETS (continued)

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

Impairment losses are written off against the corresponding assets directly, except for impairment losses recognised in respect of trade debtors and bills receivable 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 and bill receivables directly and any amounts held in the allowance account relating to that debt are reversed. Subsequent recoveries of amounts previously charged to the allowance account are reversed against the allowance account. Other charges in the allowance account and subsequent recoveries of amounts previously written off directly are recognised in profit or loss.

(ii) Impairment of other assets

Internal and external sources of information are reviewed at the end of each reporting period to identify indications that the following assets may be impaired or, except in the case of goodwill, an impairment loss previously recognised no longer exists or may have decreased:

— fixed assets;

— construction in progress;

— intangible assets;

— goodwill;

— deposits paid for acquisition of leasehold land; and

— investments in subsidiaries.

If any such indication exists, the asset's recoverable amount is estimated. In addition, for goodwill, the recoverable amount is estimated annually whether or not there is any indication of impairment.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

(I) IMPAIRMENT OF ASSETS (continued)

(ii) Impairment of other assets (continued)

— Calculation of recoverable amount

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

— Recognition of impairment losses

An impairment loss is recognised in profit or loss if the carrying amount of an asset, or the cash-generating unit to which it belongs, exceeds its recoverable amount. Impairment losses recognised in respect of cash-generating units are allocated first to reduce the carrying amount of any goodwill allocated to the cash-generating unit (or group of units) and then, 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 of disposal (if measurable) or value in use (if determinable).

— Reversals of impairment losses

In respect of assets other than goodwill, an impairment loss is reversed if there has been a favourable change in the estimates used to determine the recoverable amount. An impairment loss in respect of goodwill is not reversed.

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.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

(l) IMPAIRMENT OF ASSETS (continued)

(iii) Interim financial reporting and impairment

Under the Rules Governing the Listing of Securities on the Stock Exchange of Hong Kong Limited, the Group is required to prepare an interim financial report in compliance with IAS 34, Interim financial reporting, in respect of the first six months of the financial year. At the end of the interim period, the Group applies the same impairment testing, recognition, and reversal criteria as it would at the end of the financial year (see notes 2(l)(i) and (ii)).

Impairment losses recognised in an interim period in respect of goodwill, available-for-sale equity securities and unquoted equity securities carried at cost are not reversed in a subsequent period. This is the case even if no loss, or a smaller loss, would have been recognised had the impairment been assessed only at the end of the financial year to which the interim period relates. Consequently, if the fair value of an available-for-sale equity security increases in the remainder of the annual period, or in any other period subsequently, the increase is recognised in other comprehensive income and not profit or loss.

(m) INVENTORIES

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

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

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

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

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

(n) CONSTRUCTION CONTRACTS

Construction contracts are contracts specifically negotiated with a customer for the construction of an asset or a group of assets, where the customer is able to specify the major structural elements of the design. The accounting policy for contract revenue is set out in note 2(v)(ii). When the outcome of a construction contract can be estimated reliably, contract costs are recognised as an expense by reference to the stage of completion of the contract at the end of the reporting period. When it is probable that total contract costs will exceed total contract revenue, the expected loss is recognised as an expense immediately. When the outcome of a construction contract cannot be estimated reliably, contract costs are recognised as an expense in the period in which they are incurred.

Construction contracts in progress at the end of the reporting period are recorded at the net amount of costs incurred plus recognised profit less recognised losses and progress billings, and are presented in the statement of financial position as the "Gross amount due from customers for contract work" (as an asset) or the "Gross amount due to customers for contract work" (as a liability), as applicable. Progress billings not yet paid by the customer are included under "Trade and other receivables". Amounts received before the related work is performed are presented as "Receipts in advance" under "Trade and other payables".

(o) TRADE AND OTHER RECEIVABLES

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

(p) 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.

(q) TRADE AND OTHER PAYABLES

Trade and other payables (including amounts due from related companies) 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.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

(r) 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.

(s) EMPLOYEE BENEFITS

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

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

(ii) Share-based payments

The fair value of share options/share awards granted to employees is recognised as an employee cost with a corresponding increase in a capital reserve within equity. The fair value of the share options is measured at grant date using the binomial option price model, taking into account the terms and conditions under which the options were granted. The fair value of share awards is measured with reference to the share price on the grant date. Where the employees have to meet vesting conditions before becoming unconditionally entitled to the options/share awards, the total estimated fair value of the options is spread over the vesting period, taking into account the probability that the options/share awards 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/share awards 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/the share award is rested (when it is transferred to the share premium account) or the option expires (when it is released directly to retained profits).

Share-based payment transactions in which the Company grants share options/share awards to subsidiaries' employees are accounted for as an increase in value of investment in subsidiary in the Company's statement of financial position which is eliminated on consolidation.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

(t) INCOME TAX

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

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted or substantively enacted at the end of the reporting period, 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 limited exceptions to recognition of deferred tax assets and liabilities are those temporary differences arising from goodwill not deductible for tax purpose, the initial recognition of assets or liabilities that affect neither accounting nor taxable profit (provided they are not part of a business combination), and temporary differences relating to investments in subsidiaries to the extent that, in the case of taxable differences, the Group controls the timing of the reversal and it is probable that the differences will not reverse in the foreseeable future, or in the case of deductible differences, unless it is probable that they will reverse in the future.

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 end of the reporting period. Deferred tax assets and liabilities are not discounted.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

(t) INCOME TAX (continued)

The carrying amount of a deferred tax asset is reviewed at the end of each reporting period 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.

Additional income taxes that arise from the distribution of dividends are recognised when the liability to pay the related dividends is recognised.

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.

(u) 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.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

(v) 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 for each separate company within a transaction, 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 goods and 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) Contract revenue

When the outcome of a construction contract can be estimated reliably:

— revenue from a fixed price contract is recognised using the percentage of completion method, measured by reference to the percentage of contract costs incurred to date to estimated total contract costs for the contract; and

— revenue from a cost plus contract is recognised by reference to the recoverable costs incurred during the period plus an appropriate proportion of the total fee, measured by reference to the proportion that costs incurred to date bear to the estimated total costs of the contract.

When the outcome of a construction contract cannot be estimated reliably, revenue is recognised only to the extent of contract costs incurred that it is probable will be recoverable.

(iii) Interest income

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

(iv) Government grants

Government grants are recognised in the statement of financial position 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.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

(v) REVENUE RECOGNITION (continued)

(v) Rendering of oil and gas engineering services

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

(vi) Rendering of repairing services

Revenue is recognised when the service has been rendered.

(vii) Dividend income

Dividend income from unlisted investments is recognised when the shareholder's right to receive payment is established.

(w) 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 end of the reporting period. Exchange gains and losses are recognised in profit or loss.

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

The results of operations outside the PRC are translated into the presentation currency at the exchange rates approximating the foreign exchange rates ruling at the dates of the transactions. Statement of financial position items, including goodwill arising on consolidation of foreign operations acquired, are translated into the presentation currency at the closing foreign exchange rates ruling at the end of the reporting period. 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.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

(x) 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.

(y) 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.

(z) RELATED PARTIES

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

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

(ii) has significant influence over the Group; or

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

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

2 SIGNIFICANT ACCOUNTING POLICIES (continued)

(z) RELATED PARTIES (continued)

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

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

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

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

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

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

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

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

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

(aa) SEGMENT REPORTING

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

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

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

3 SIGNIFICANT ACCOUNTING ESTIMATES AND JUDGEMENTS

KEY SOURCES OF ESTIMATION UNCERTAINTY

Note 29 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, fixed assets and construction in progress

If circumstances indicate that the carrying value of intangible assets, fixed assets and construction in progress may not be recoverable, these assets may be considered impaired, and an impairment loss may be recognised in accordance with IAS 36, Impairment of assets. 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.

3 SIGNIFICANT ACCOUNTING ESTIMATES AND JUDGEMENTS (continued)

KEY SOURCES OF ESTIMATION UNCERTAINTY (continued)

(b) Write down of inventories

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

(c) 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.

(d) 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.

(e) 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 for tax losses not yet used and temporary deductible differences 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.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

3 SIGNIFICANT ACCOUNTING ESTIMATES AND JUDGEMENTS (continued)

KEY SOURCES OF ESTIMATION UNCERTAINTY (continued)

(f) Construction contracts

As explained in the accounting policy notes 2(n) and 2(v)(ii), revenue and profit recognition on an incompleted project is dependent on estimating the total outcome of the construction contract, as well as the work done to date. Based on the Group's recent experience and the nature of the construction activity undertaken by the Group, the Group makes estimates of the point at which it considers the work is sufficiently advanced such that the costs to complete and revenue can be reliably estimated.

Based on the latest information available in respect of the market environment, the Group prepares budgets for construction contracts individually and the budget, which is used in the Group's financial reporting, is reviewed regularly. Foreseeable losses are provided when identified. In preparing the financial statements for the year ended 31 December 2013, the directors of the Company have reviewed the construction contracts and consider that no provision is required. Material adjustments to the budgeted costs may occur in future if there is a significant change in the market environment.

(g) Litigation provision

The Group has been involved in several legal proceedings. The Group has recognised provisions or disclosed as contingent liabilities based on its legal assessment. Further development of the proceedings or decisions made by the court may result in different assessments of the financial consequences in subsequent years and require an increase or decrease in the recorded liabilities. Further details of the proceedings are disclosed in notes 31(a), 31(b) and 39.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

4 TURNOVER AND SEGMENT REPORTING

(a) TURNOVER

The principal activities of the Group are manufacturing, sale and trading of land drilling rigs, offshore drilling rigs, parts and components and provision of oil and gas engineering services. Turnover represents revenue recognised for the sales value of goods supplied, revenue from construction contracts and oil and gas engineering services provided to customers net of value-added tax, returns and trade discounts. The amount of each significant category of revenue recognised in turnover during the year is as follows:

	2013 RMB'000	2012 RMB'000
Sales of rigs, parts and components	**7,441,796**	4,896,436
Provision of oil and gas engineering services	**408,703**	172,011
Revenue from construction contracts	**196,609**	–
	8,047,108	5,068,447

For the year ended 31 December 2013, the Group's customer base includes two customers (2012: one customer) with whom transactions have exceeded 10% of the Group's revenue. In 2013, revenue from sales of land drilling rigs and related parts and components to two customers (2012: one customer), amounted to approximately RMB3,027 million (2012: RMB2,350 million) and arose in the Middle East and America (2012: America).

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

4 TURNOVER AND SEGMENT REPORTING (continued)

(b) SEGMENT REPORTING

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

Land drilling rigs	—	This segment manufactures and sells land drilling rigs.
Offshore drilling rigs	—	This segment manufactures and sells offshore drilling rigs and related parts and components.
Parts, components and others	—	This segment manufactures, sells and trades parts and components of petroleum equipment.
Oil and gas engineering services	—	This segment provides oil and gas engineering services.

(i) Segment results, assets and liabilities

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

Segment assets include all tangible assets, goodwill, intangible assets and current assets with the exception of interests in an associate and joint ventures, other investment, deferred tax assets, current tax recoverable, other financial assets and other corporate assets. Segment liabilities include trade payables, accruals, provision for product warranties and bills payable attributable to the manufacturing and sales activities of the individual segments with the exception of 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 "adjusted profit from operations". To arrive at adjusted profit from operations, the Group's profit from operations are further adjusted for items not specifically attributed to individual segments, such as directors' remuneration and other head office or corporate administration costs.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

4 TURNOVER AND SEGMENT REPORTING (continued)

(b) SEGMENT REPORTING (continued)

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

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 2013 and 2012 is set out below.

	Land drilling rigs		Offshore drilling rigs		Parts, components and others		Oil and gas engineering services		Total	
	2013 RMB'000	2012 RMB'000	2013 RMB'000	2012 RMB'000	2013 RMB'000	2012 RMB'000	2013 RMB'000	2012 RMB'000	2013 RMB'000	2012 RMB'000
Revenue from external customers	5,664,602	3,750,575	196,609	157,275	1,777,194	988,586	408,703	172,011	8,047,108	5,068,447
Inter-segment revenue	–	–	24,741	–	1,552,075	1,108,763	–	–	1,576,816	1,108,763
Reportable segment revenue	5,664,602	3,750,575	221,350	157,275	3,329,269	2,097,349	408,703	172,011	9,623,924	6,177,210
Reportable segment profit/(loss)	787,370	779,856	(27,772)	(35,439)	109,797	74,365	32,864	14,001	902,259	832,783
Depreciation and amortisation for the year	43,837	40,918	65,026	42,875	39,257	30,164	92,470	33,311	240,590	147,268
Impairment of trade and other receivables	6,022	15,810	–	–	37,843	16,846	–	4,766	43,865	37,422
Write-down of inventories	35,101	9,284	–	–	14,456	13,196	–	–	49,557	22,480
Reportable segment assets	4,410,606	3,288,992	2,576,282	1,605,724	3,293,331	2,263,578	1,518,241	628,033	11,798,460	7,786,327
Additions to non-current segment assets during the year	195,416	83,470	384,314	598,282	41,992	60,090	630,554	386,827	1,252,276	1,128,669
Reportable segment liabilities	2,039,009	1,988,432	838,141	520,246	1,821,167	650,598	597,543	91,564	5,295,860	3,250,840

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

4 TURNOVER AND SEGMENT REPORTING (continued)

(b) SEGMENT REPORTING (continued)

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

	2013 RMB'000	2012 RMB'000
Profit		
Reportable segment profit	**902,259**	832,783
Elimination of inter-segment profits	**(21,852)**	(100,287)
Reportable segment profit derived from Group's external customers	**880,407**	732,496
Share of profit from an associate	**–**	7,662
Share of losses from joint ventures	**(7,948)**	(156)
Other revenue, other net income and other operating expenses	**62,462**	5,871
Net finance (expenses)/income	**(139,418)**	29,259
Unallocated head office and corporate expenses	**(94,503)**	(65,674)
Consolidated profit before taxation	**701,000**	709,458
Assets		
Reportable segment assets	**11,798,460**	7,786,327
Elimination of inter-segment receivables	**(917,027)**	(409,590)
	10,881,433	7,376,737
Interests in joint ventures	**47,924**	57,181
Interest in an associate	**9,000**	–
Current tax recoverable	**16,406**	1,502
Deferred tax assets	**123,975**	96,407
Other investment	**74,053**	72,609
Other financial assets	**804,102**	315,036
Unallocated head office and corporate assets	**2,272,162**	1,926,404
Consolidated total assets	**14,229,055**	9,845,876
Liabilities		
Reportable segment liabilities	**5,295,860**	3,250,840
Elimination of inter-segment payables	**(917,027)**	(409,590)
	4,378,833	2,841,250
Current tax payable	**51,453**	96,311
Deferred tax liabilities	**50,611**	2,157
Unallocated head office and corporate liabilities	**4,789,512**	2,317,431
Consolidated total liabilities	**9,270,409**	5,257,149

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

4 TURNOVER AND SEGMENT REPORTING (continued)

(b) SEGMENT REPORTING (continued)

(iii) Geographic information

The following table sets out information about the geographical location of (i) the Group's revenue from external customers and (ii) the Group's non-current trade and other receivables, fixed assets, construction in progress, intangible assets, goodwill, deposits paid for acquisition of leasehold land and interests in joint ventures and an associate ("specified non-current assets"). The geographical location of customers is based on the location at which the services were provided or the goods are delivered. The geographical location of the specified non-current assets is based on the physical location of the asset, in the case of fixed assets, the location of the operation to which they are allocated, in the case of goodwill and intangible assets, and the location of operations, in the case of interests in joint ventures and an associate.

	Revenue from external customers		Specified non-current assets	
	2013 RMB'000	2012 RMB'000	**2013 RMB'000**	2012 RMB'000
PRC (country of domicile)	**1,825,912**	1,032,161	**3,553,366**	2,324,904
Americas	**1,190,687**	2,791,664	**122,336**	123,215
Middle East	**2,921,498**	46,917	**239,198**	169,076
Europe and Central Asia	**1,666,094**	763,895	**389,789**	387,274
South Asia and South East Asia	**354,485**	219,177	**–**	–
Others	**88,432**	214,633	**45,654**	54,416
	8,047,108	5,068,447	**4,350,343**	3,058,885

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

5 OTHER REVENUE

	2013 RMB'000	2012 RMB'000
Sales of scrap materials	21,775	289
Repair services income	13,423	16,507
Government grants (note (i))	30,421	32,166
Settlement income (note (ii))	82,000	–
Rental income	14,874	8,232
Others	13,976	6,139
	176,469	63,333

Notes:

(i) Government grants are subsidies received from government mainly for industry development encouragement.

(ii) Sichuan Honghua Petroleum Equipment Co., Ltd (四川宏華石油設備有限公司) ("Honghua Company") entered into several sales contracts with a customer during the year ended 31 December 2009 and received advance payment of RMB82,000,000 which were subsequently suspended by the customer. The sales contracts were terminated by the customer during the year ended 31 December 2013. As a result of the termination, Honghua Company recognised the receipts in advance of RMB82,000,000 as a settlement income pursuant to the terms of the sales contracts.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

6 PROFIT BEFORE TAXATION

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

	2013 RMB'000	2012 RMB'000
(a) Net finance expenses/(income)		
Foreign exchange loss/(gain), net	26,549	(20,434)
Interest income on bank deposits	(22,441)	(23,830)
Interest income from long-term receivables	(37,902)	(10,820)
Fair value change of other financial assets	(6,345)	(19,654)
Interest on interest-bearing borrowings wholly repayable within five years	179,923	62,858
Bank charges	26,550	13,847
Others	4,567	841
	170,901	2,808
Less: Interest expense capitalised into assets under construction*	(31,483)	(32,067)
	139,418	(29,259)

* The borrowing costs have been capitalised at a rate of per annum 1.17% to 7.80% (2012: 1.17% to 7.04%).

	2013 RMB'000	2012 RMB'000
(b) Staff costs		
Contributions to defined contribution retirement schemes	91,474	57,996
Equity-settled share-based payment expenses (note 29)	75,896	4,809
Salaries, wages and other benefits	633,262	515,198
	800,632	578,003

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

6 PROFIT BEFORE TAXATION (continued)

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

	2013 RMB'000	2012 RMB'000
(c) Other items		
Operating lease charges:		
— properties	11,196	8,193
— plant and machinery	8,897	–
Provision for a legal claim (note 31)	99,078	32,317
Amortisation and depreciation		
— leasehold land held for own use under operating leases	12,127	6,560
— property, plant and equipment	193,535	106,796
— intangible assets	35,731	34,647
	241,393	148,003
Impairment losses on trade and other receivables	43,865	37,422
Write down on inventories	49,557	22,480
Auditors' remuneration		
— audit services	3,402	2,511
— tax services	–	40
— other services	808	700
	4,210	3,251
Research and development costs*	90,565	58,053
Less: Amount capitalised into intangible assets	(31,697)	(406)
	58,868	57,647

* The amounts included staff costs of the Research and Development Department of RMB49,770,000 (2012: RMB45,193,000), which are included in the total staff costs as disclosed in note 6(b).

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

7 INCOME TAX IN THE CONSOLIDATED INCOME STATEMENT

(a) TAXATION IN THE CONSOLIDATED STATEMENT OF PROFIT OR LOSS REPRESENTS:

	2013 RMB'000	2012 RMB'000
Current tax — Hong Kong Profits Tax		
Provision for the year	17,064	3,583
Current tax — PRC		
Provision for the year	78,987	190,176
Under-provision in respect of prior years	5,370	828
Sub-total	84,357	191,004
Current tax — other jurisdictions		
Provision for the year	6,565	1,774
Current tax — total	107,986	196,361
Deferred tax		
Origination and reversal of temporary differences	17,764	(28,678)
Income tax expenses	125,750	167,683

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

7 INCOME TAX IN THE CONSOLIDATED INCOME STATEMENT (continued)

(a) TAXATION IN THE CONSOLIDATED STATEMENT OF PROFIT OR LOSS REPRESENTS: (continued)

(i) Hong Kong

The provision for Hong Kong Profits Tax for 2013 is calculated at 16.5% (2012: 16.5%) of the estimated assessable profits of the subsidiaries incorporated in Hong Kong for the year.

(ii) PRC

Pursuant to the income tax rules and regulations of the PRC, the subsidiaries in the PRC are liable to PRC enterprise income tax at a rate of 25% (2012: 25%) during the year ended 31 December 2013, except for the following companies:

(a) Honghua Company

Income tax for Honghua Company is provided at a tax rate of 15% (2012: 15%) applicable for Hi-Tech Enterprises pursuant to the relevant PRC tax rules and regulations during the year ended 31 December 2013.

(b) Sichuan Honghua Electric Co., Ltd. (四川宏華電氣有限公司) (formerly known as Chengdu Hongtian Electric Drive Engineering Co., Ltd.(成都宏天電傳有限公司) ("Honghua Electric")

On 27 July 2011, the Ministry of Finance, the General Administration of Customs and the State Administration of Taxation jointly issued CaiShui [2011] No.58 which states that enterprises within encouraged industries and located in the Western Region are entitled to a preferential tax rate of 15% for the period from 1 January 2011 to 31 December 2020 ("Tax Concession"). The Tax Concession needs to be applied annually. Honghua Electric applied for and successfully obtained the Tax Concession with 15% preferential income tax rate for the 12 months ended 31 December 2012. The directors of the Company assess that it is highly probable that the subsidiary will continue to be granted with the Tax Concession upon their application for renewal, and accordingly provision for PRC enterprise income tax for the subsidiary was made at the preferential rate of 15% in these financial statements.

(iii) Others

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

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

7 INCOME TAX IN THE CONSOLIDATED INCOME STATEMENT (continued)

(b) WITHHOLDING TAX

Under the PRC tax law and its Implementation Rules, dividends receivable by non-PRC resident enterprises from PRC enterprises are subject to withholding tax at a rate of 10%, unless reduced by tax treaties or arrangements, for profits earned since 1 January 2008. Pursuant to a tax arrangement between the PRC and Hong Kong, a qualified Hong Kong tax resident will be liable for withholding tax at a reduced rate of 5% for dividend income derived from the PRC. During the year ended 31 December 2013, the Company's PRC subsidiaries obtained approval from the respective tax authority for paying withholding tax of dividend income at the reduced rate of 5%. Accordingly, a reversal of withholding tax was recognised during 2013 to reflect the reduction of withholding tax rate from 10% to 5% and the provision for withholding tax at the end of the reporting period was made at 5%. Deferred tax liabilities have been recognised for undistributed retained profits of the Group's subsidiaries established in the PRC earned since 1 January 2008 to the extent that profits are likely to be distributed in the foreseeable future.

(c) RECONCILIATION BETWEEN TAX EXPENSES AND ACCOUNTING PROFIT AT APPLICABLE TAX RATES:

	2013 RMB'000	2012 RMB'000
Profit before taxation	**701,000**	709,458
Notional tax on profit before taxation, calculated at the rates applicable to profits in the countries concerned	**120,861**	115,715
Tax effect of non-deductible expenses	**3,779**	9,440
Tax effect of non-taxable income	**(2,453)**	(669)
Unrecognised tax losses	**13,749**	3,585
Withholding tax on expected profits distribution from PRC subsidiaries	**(15,556)**	38,784
Under-provision in respect of prior years	**5,370**	828
Actual tax expenses	**125,750**	167,683

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

8 DIRECTORS' REMUNERATION

Details of directors' remuneration are set out below:

	2013					
	Fees RMB'000	Basic salaries, allowances and other benefits in kind RMB'000	Contributions to defined contribution retirement scheme RMB'000	Discretionary bonuses RMB'000	Equity-settled share-based payment expenses RMB'000	Total RMB'000
Chairman and Executive Director						
Zhang Mi	–	1,230	42	1,543	4,433	7,248
Executive Directors						
Ren Jie	–	1,008	35	664	2,845	4,552
Liu Zhi	–	1,056	35	506	2,577	4,174
Non-executive Directors						
Siegfried Meissner	–	–	–	–	–	–
Huang Dongyang (resigned on 19 March 2013)	–	–	–	–	–	–
Popin Su (the alternate director to Siegfried Meissner)	–	–	–	–	–	–
Independent Non-executive Directors						
Qi Daqing	160	–	–	–	209	369
Liu Xiaofeng	160	–	–	–	209	369
Chen Guoming	80	–	–	–	146	226
Tai Kwok Leung, Alexander (resigned on 19 March 2014)	120	–	–	–	178	298
Shi Xingquan	80	–	–	–	157	237
Guo Yanjun	120	–	–	–	157	277
Total	720	3,294	112	2,713	10,911	17,750

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

8 DIRECTORS' REMUNERATION (continued)

	2012					
	Fees RMB'000	Basic salaries, allowances and other benefits in kind RMB'000	Contributions to defined contribution retirement scheme RMB'000	Discretionary bonuses RMB'000	Equity-settled share-based payment expenses RMB'000	Total RMB'000
Chairman and Executive Director						
Zhang Mi	–	1,079	38	3,811	324	5,252
Executive Directors						
Ren Jie	–	882	37	1,788	101	2,808
Liu Zhi	–	929	37	1,413	92	2,471
Non-executive Directors						
Siegfried Meissner	–	–	–	–	–	–
Huang Dongyang	–	–	–	–	–	–
Popin Su (the alternate director to Siegfried Meissner)	–	–	–	–	–	–
Independent Non-executive Directors						
Qi Daqing	163	–	–	–	181	344
Liu Xiaofeng	163	–	–	–	181	344
Chen Guoming	81	–	–	–	125	206
Tai Kwok Leung, Alexander	122	–	–	–	154	276
Shi Xingquan	81	–	–	–	136	217
Guo Yanjun	122	–	–	–	136	258
Total	732	2,890	112	7,012	1,430	12,176

During the year, no amount was paid or payable by the Group to the directors or any of the five highest paid individuals set out in note 9 below as an inducement to join or upon joining the Group or as compensation for loss of office. Except for Siegfried Meissner who has waived to receive his remuneration amounting to RMB122,000 (2012: RMB122,000), there was no arrangement under which a director waived or agreed to waive any remuneration during the year (2012: RMB Nil).

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

9 INDIVIDUAL WITH HIGHEST EMOLUMENTS

The five highest paid individuals of the Group include three directors during the year ended 31 December 2013 (2012: three) whose emoluments are disclosed in note 8. Details of remuneration paid to the remaining two (2012: two) highest individuals of the Group are as follows:

	2013 RMB'000	2012 RMB'000
Basic salaries, allowances and other benefits in kind	1,512	1,497
Discretionary bonuses	1,682	2,963
Contributions to defined contribution retirement schemes	77	53
Share-based payments	4,902	194
	8,173	4,707

The emoluments of these two (2012: two) individuals with highest emoluments are within the following bands:

	2013	2012
HKD2,500,001 to HKD3,000,000	–	2
HKD4,500,001 to HKD5,000,000	1	–
HKD5,000,001 to HKD5,500,000	1	–

10 PROFIT ATTRIBUTABLE TO EQUITY SHAREHOLDERS OF THE COMPANY

The consolidated profit attributable to equity shareholders of the Company includes a loss of RMB78,345,000 (2012: loss of RMB82,405,000) which has been dealt with in the financial statements of the Company.

Reconciliation of the above amount to the Company's profit for the year:

	2013 RMB'000	2012 RMB'000
Amount of consolidated loss attributable to equity shareholders dealt with in the Company's financial statements	(78,345)	(82,405)
Final dividends from subsidiaries attributable to the profits of the previous financial year, approved and paid during the year	246,671	244,251
Company's profit for the year (note 33(a))	168,326	161,846

Details of dividends paid and payable to equity shareholders of the Company are set out in note 33(b).

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

11 EARNINGS PER SHARE

(a) BASIC EARNINGS PER SHARE

The calculation of basic earnings per Share is based on the profit attributable to ordinary equity shareholders of the Company of RMB537,617,000 (2012: RMB529,458,000) and the weighted average number of 3,165,015,000 (2012: 3,193,876,000) ordinary shares in issue during the year, calculated as follows:

Weighted average number of ordinary shares

	2013	2012
Issued ordinary shares at 1 January	3,231,133,000	3,223,798,000
Effect of the share award scheme	(71,950,000)	(30,625,000)
Effect of share options exercised	5,832,000	703,000
Weighted average number of ordinary shares at 31 December	3,165,015,000	3,193,876,000

(b) DILUTED EARNINGS PER SHARE

The calculation of diluted earnings per Share is based on the profit attributable to ordinary equity shareholders of the Company of RMB537,617,000 (2012: RMB529,458,000) and the weighted average number of 3,206,578,000 (2012: 3,201,348,000) ordinary shares, calculated as follows:

Weighted average number of ordinary shares (diluted)

	2013	2012
Weighted average number of ordinary shares at 31 December	3,165,015,000	3,193,876,000
Effect of deemed issue of shares under the Company's share option scheme	41,563,000	7,472,000
Weighted average number of ordinary shares (diluted) at 31 December	3,206,578,000	3,201,348,000

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

12 FIXED ASSETS

(a) THE GROUP

	Freehold land RMB'000	Interests in leasehold land held for own use under operating leases RMB'000	Buildings held for own use RMB'000	Plant and machinery RMB'000	Fixtures, fitting and equipment RMB'000	Motor vehicles RMB'000	Total RMB'000
Cost:							
At 1 January 2012	5,080	190,754	397,699	298,304	174,138	49,392	1,115,367
Additions	–	98,629	5,521	53,119	46,129	15,482	218,880
Acquisition of a business	–	30,152	5,980	38,133	258	477	75,000
Transfer from construction in progress (note 13)	–	–	26,862	9,132	504	–	36,498
Transfer from inventories	–	–	–	366,760	6,030	–	372,790
Disposals	–	–	(2,072)	(210)	(2,385)	(3,415)	(8,082)
Exchange difference	(12)	–	(238)	(2,103)	(154)	(28)	(2,535)
At 31 December 2012	5,068	319,535	433,752	763,135	224,520	61,908	1,807,918
Accumulated amortisation and depreciation:							
At 1 January 2012	–	9,565	63,755	76,161	74,867	26,153	250,501
Charge for the year	–	6,560	21,943	49,354	28,209	7,290	113,356
Written back on disposals	–	–	(1,446)	(159)	(2,035)	(2,618)	(6,258)
Exchange difference	–	–	(30)	(214)	(28)	(9)	(281)
At 31 December 2012	–	16,125	84,222	125,142	101,013	30,816	357,318
Net book value:							
At 31 December 2012	5,068	303,410	349,530	637,993	123,507	31,092	1,450,600

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

12 FIXED ASSETS (continued)

(a) THE GROUP (continued)

	Freehold land RMB'000	Interests in leasehold land held for own use under operating leases RMB'000	Buildings held for own use RMB'000	Plant and machinery RMB'000	Fixtures, fitting and equipment RMB'000	Motor vehicles RMB'000	Total RMB'000
Cost:							
At 1 January 2013	5,068	319,535	433,752	763,135	224,520	61,908	1,807,918
Additions	–	60,895	22,749	127,567	100,222	17,612	329,045
Acquisition of subsidiaries (note 35)	–	9,712	25,121	9,641	1,255	2,624	48,353
Transfer from construction in progress (note 13)	–	–	491,545	359,735	1,778	–	853,058
Transfer from inventories	–	–	–	55,854	–	–	55,854
Disposals	–	–	–	(1,115)	(2,746)	(4,076)	(7,937)
Exchange difference	(152)	–	(1,995)	(11,167)	(1,406)	(877)	(15,597)
At 31 December 2013	4,916	390,142	971,172	1,303,650	323,623	77,191	3,070,694
Accumulated amortisation and depreciation:							
At 1 January 2013	–	16,125	84,222	125,142	101,013	30,816	357,318
Charge for the year	–	12,127	33,851	114,104	37,276	8,304	205,662
Written back on disposals	–	–	–	(977)	(1,160)	(3,153)	(5,290)
Exchange difference	–	–	(331)	(927)	(449)	(198)	(1,905)
At 31 December 2013	–	28,252	117,742	237,342	136,680	35,769	555,785
Net book value:							
At 31 December 2013	4,916	361,890	853,430	1,066,308	186,943	41,422	2,514,909

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

12 FIXED ASSETS (continued)

(b) THE ANALYSIS OF NET BOOK VALUE OF PROPERTIES IS AS FOLLOWS:

	The Group	
	2013	2012
	RMB'000	RMB'000
Outside Hong Kong		
— freehold	**4,916**	5,068
— medium-term leases	**1,215,320**	652,940
	1,220,236	658,008
Representing:		
Freehold land	**4,916**	5,068
Interest in leasehold land held for own use under operating leases	**361,890**	303,410
Buildings held for own use	**853,430**	349,530
	1,220,236	658,008

13 CONSTRUCTION IN PROGRESS

	The Group	
	2013	2012
	RMB'000	RMB'000
At 1 January	**827,290**	402,065
Additions	**711,966**	461,753
Acquisition of subsidiaries (note 35)	**41,911**	–
Transfer to fixed assets (note 12)	**(853,058)**	(36,498)
Exchange difference	**(90)**	(30)
At 31 December	**728,019**	827,290

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

14 INTANGIBLE ASSETS

	The Group			The Company
	Technical know-how RMB'000	Development cost RMB'000	Total RMB'000	Technical know-how RMB'000
Cost:				
At 1 January 2012	338,749	10,234	348,983	338,749
Addition through internal development	–	406	406	–
Exchange difference	84	–	84	84
At 31 December 2012	338,833	10,640	349,473	338,833
At 1 January 2013	338,833	10,640	349,473	338,833
Addition through internal development	–	31,697	31,697	–
Acquisition of subsidiaries (note 35)	21,200	–	21,200	–
Exchange difference	(10,308)	–	(10,308)	(10,308)
At 31 December 2013	349,725	42,337	392,062	328,525
Accumulated amortisation:				
At 1 January 2012	112,917	72	112,989	112,917
Charge for the year	33,880	767	34,647	33,880
Exchange difference	31	–	31	31
At 31 December 2012	146,828	839	147,667	146,828
At 1 January 2013	146,828	839	147,667	146,828
Charge for the year	34,949	782	35,731	33,359
Exchange difference	(4,973)	–	(4,973)	(4,973)
At 31 December 2013	176,804	1,621	178,425	175,214
Net book value:				
At 31 December 2013	172,921	40,716	213,637	153,311
At 31 December 2012	192,005	9,801	201,806	192,005

The amortisation charge for the year is included in "general and administrative expenses" in the consolidated statement of profit or loss.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

15 GOODWILL

	The Group	
	2013	2012
	RMB'000	RMB'000
Cost	**13,484**	–

IMPAIRMENT TEST FOR CASH-GENERATING UNIT CONTAINING GOODWILL

Goodwill is allocated to the oil and gas engineering services segment.

The recoverable amount of the CGU is determined based on value-in-use calculation. This calculation uses cash flow projection based on financial budgets approved by management covering a five-year period. Cash flows beyond the five-year period are extrapolated using the estimated rate stated below. The growth rate does not exceed the long-term average growth rate for the business in which the CGU operates.

Key assumptions used for value-in-use calculation:

	The Group	
	2013	2012
— Gross margin	**25%**	–
— Growth rate	**3%**	–
— Discount rate	**16%**	–

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

16 INVESTMENTS IN SUBSIDIARIES

	The Company	
	2013	2012
	RMB'000	RMB'000
Unlisted equities, at cost	**196,550**	202,713
Cumulative fair value of share options granted to employees of subsidiaries	**86,267**	86,736
Long-term receivables from subsidiaries	**2,627,737**	2,264,973
	2,910,554	2,554,422

The long-term receivables from subsidiaries are unsecured, interest-free and have no fixed terms of repayment. The Company has given undertaking not to demand for repayment within one year from the end of the reporting period.

Details of the principal subsidiaries at 31 December 2013 are set out below:

Name of company	Place of incorporation/ establishment and operation	Issued and paid-up capital	Attributable equity interest Direct	Attributable equity interest Indirect	Principal activities
Honghua Holdings Limited ("Honghua Holdings")	Hong Kong	HKD1	100%	–	Investment holding
Honghua Company (notes (i) and (iii))	The PRC	RMB1,350,112,000	–	100%	Manufacturing of petroleum equipment
Honghua Electric (notes (i) and (iii))	The PRC	RMB100,000,000	–	80%	Manufacturing of panel of drilling rigs
Honghua International Co., Ltd (四川宏華國際科貿有限公司) (notes (i) and (iii))	The PRC	RMB51,200,000	–	85%	Trading of drilling rigs and related parts

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

16 INVESTMENTS IN SUBSIDIARIES (continued)

Name of company	Place of incorporation/ establishment and operation	Issued and paid-up capital	Attributable equity interest		Principal activities
			Direct	Indirect	
Honghua (China) Investment Co., Ltd. 宏華(中國)投資有限公司 (notes (ii) and (iii))	The PRC	USD200,000,000	–	100%	Investment holding
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) and (iii))	The PRC	RMB874,992,609	–	100%	Manufacturing of offshore drilling platform and related products
Newco (H.K.) Limited	Hong Kong	HKD1,000	–	100%	Trading of drilling rigs and related parts
Russia Honghua Co., Ltd.	Russia Federation	RUB10,000	–	100%	Trading of drilling rigs and elated parties
Honghua America, LLC ("Honghua America")	United States of America ("US")	USD3,414,407	–	85%	Trading of drilling rigs and related parts

Notes:

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

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

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

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

17 INTERESTS IN JOINT VENTURES

	The Group	
	2013	2012
	RMB'000	RMB'000
Share of net assets	**47,924**	57,181

Details of the Group's interests in joint ventures, which is accounted for using the equity method in the consolidated financial statements, are as follows:

Name of company	Place of establishment	Issued capital	Paid up capital	Group's effective interest held by a subsidiary	Principal activities
Egyptian Petroleum HH Rigs Manufacturing Co. S.A.E. ("HH Egyptian Company")	Egypt	USD18,000,000	USD18,000,000	50%	Manufacturing and sale of drilling rigs, parts and components
Honghua Oil Equipment Trading Company	Hong Kong	USD1,290	USD1,290	50%	Trading of drilling rigs, parts and components
Honghua CIS Ltd.	Russia Federation	RUB32,000,000	RUB32,000,000	50%	Manufacturing and sale of drilling rigs, parts and components

The joint ventures in which the Group participates are unlisted corporate entities whose market price is not available.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

17 INTERESTS IN JOINT VENTURES (continued)

Each individual joint venture does not have a significant financial impact on the Group's results of operations and financial position. Aggregate financial information of joint ventures that are individually immaterial is as follows:

	The Group	
	2013	2012
	RMB'000	RMB'000
Carrying amount in the consolidated financial statements	**47,924**	57,181
The Group's effective share of those joint ventures		
Loss for the year	**(7,948)**	(156)
Other comprehensive income for the year	**(1,309)**	(139)
Total comprehensive income for the year	**(9,257)**	(295)

18 INTEREST IN AN ASSOCIATE

	The Group	
	2013	2012
	RMB'000	RMB'000
Share of net assets	**9,000**	–

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

18 INTEREST IN AN ASSOCIATE (continued)

Particulars of the associate as at 31 December 2013, which is an unlisted corporate entity, were as follows:

Name of company	Place of establishment	Issued capital	Paid up capital	Group's effective interest held by a subsidiary	Principal activities
Hongdaojianyuan Marine Science and Technology Co., (Sansha) Ltd. (三沙宏道建遠海洋科技有限公司) ("Sansha Hongdao") (note)	The PRC	RMB30,000,000	Nil	30%	Designing and manufacturing of offshore equipment

Note: The official name of the Company is in Chinese. The English translation of the Company name is for reference only.

The above associate is accounted for using the equity method in the consolidated financial statements. Sansha Hongdao has not commenced business during the year 31 December 2013.

The associate does not have a significant financial impact on the Group's results of operations and financial position. Financial information of the associate is as follows:

	2013 RMB'000	2012 RMB'000
Carrying amount in the consolidated financial statements	9,000	–
The Group's effective share of the associate		
Profit and total comprehensive income for the year	–	7,662

19 OTHER INVESTMENT

	The Group	
	2013 RMB'000	2012 RMB'000
Available-for-sale equity securities	74,053	72,609

The equity securities do not have a quoted price in an active market whose fair value cannot be reliably measured, accordingly, they are stated at cost less impairment losses.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

20 INVENTORIES

(a) INVENTORIES IN THE STATEMENT OF FINANCIAL POSITION COMPRISE:

	2013 RMB'000	2012 RMB'000
Raw materials	728,381	884,862
Work in progress	971,630	1,070,858
Finished goods	811,381	420,135
Goods in transit	289,915	355,085
	2,801,307	2,730,940

(b) AN ANALYSIS OF THE AMOUNT OF INVENTORIES RECOGNISED AS AN EXPENSE IS AS FOLLOWS:

	2013 RMB'000	2012 RMB'000
Carrying amount of inventories sold	5,652,588	3,267,497
Write-down of inventories	49,557	22,480
	5,702,145	3,289,977

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

21 TRADE AND OTHER RECEIVABLES

	2013 RMB'000	2012 RMB'000
Trade receivables	3,287,696	1,627,568
Bills receivable	35,328	80,769
Less: Allowance for doubtful debts (note 21(b))	(206,250)	(167,151)
Sub-total	3,116,774	1,541,186
Value-added tax recoverable	275,664	245,567
Prepayments	899,616	520,365
Other receivables (note (i))	345,423	168,688
	4,637,477	2,475,806
Representing:		
Current portion	3,961,427	2,105,804
Non-current portion (note (ii))	676,050	370,002
	4,637,477	2,475,806

Notes:

(i) Included in other receivables of the Group as at 31 December 2013 is an amount of RMB32,317,000 (2012: RMB32,317,000), being the amount indemnified by certain shareholders in relation to a legal claim, details of which are set in note 31(a).

(ii) Non-current trade and other receivables represent trade receivables and bills receivable of RMB441,908,000 (2012: RMB306,126,000) from instalment sales receivable after 1 year from the end of the reporting period at market interest rate, prepayments for acquisition of fixed assets of RMB191,673,000 (2012: RMB63,876,000) and deposits placed for loans borrowed of RMB42,469,000 (2012: RMB Nil).

The current trade and other receivables are expected to be recovered or recognised as expense within one year.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

21 TRADE AND OTHER RECEIVABLES (continued)

(a) AGEING ANALYSIS

As of the end of the reporting period, the ageing analysis of trade receivables and bill receivable, based on the invoice date (or date of revenue recognition, if earlier) and net of allowance for doubtful debts, is as follows:

	2013 RMB'000	2012 RMB'000
Within 1 month	**1,570,944**	1,246,810
1 to 2 months	**299,679**	24,433
2 to 3 months	**181,472**	25,139
3 to 12 months	**719,894**	110,244
Over 1 year	**344,785**	134,560
	3,116,774	1,541,186

Trade receivables and bill receivable are due within 90 days from the date of billing. Further details on the Group's credit policy are set out in note 34(a).

(b) ALLOWANCE FOR DOUBTFUL DEBTS

Impairment losses in respect of trade receivables and bills receivable are recorded using an allowance account unless the Group is satisfied that recovery of the amount is remote, in which case the impairment loss is written off against trade receivables and bills receivable directly (see note 2(l)).

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

	2013 RMB'000	2012 RMB'000
At 1 January	**167,151**	140,099
Provision for impairment losses	**43,865**	37,422
Uncollectible amounts written off	**(4,766)**	(10,370)
At 31 December	**206,250**	167,151

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

21 TRADE AND OTHER RECEIVABLES (continued)

(b) ALLOWANCE FOR DOUBTFUL DEBTS (continued)

At 31 December 2013, the Group's trade receivables and bills receivable of RMB261,841,000 (2012: RMB259,698,000) were individually determined to be impaired. The individually impaired receivables related to customers that were in financial difficulties and management assessed that only a portion of the receivables is expected to be recovered. Consequently, specific allowances for doubtful debts of RMB206,250,000 (2012: RMB167,151,000) were recognised. The Group does not hold any collateral over these balances.

(c) TRADE RECEIVABLES THAT ARE NOT IMPAIRED

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

	The Group	
	2013	2012
	RMB'000	RMB'000
Neither past due nor impaired	**2,539,623**	1,246,810
Less than 1 month past due	**167,104**	24,433
1 to 3 months past due	**56,211**	25,139
More than 3 months but less than 12 months past due	**216,522**	110,244
More than 1 year past due	**81,723**	42,013
	521,560	201,829

Receivables that were neither past due nor impaired relate to a wide range of customers for whom there was no recent history of default.

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

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

22 CONSTRUCTION CONTRACTS

The revenue from contract work performed recognised during the year ended 31 December 2013 is RMB196,609,000 (2012: RMB Nil). The aggregate amount of costs incurred plus recognised profits less recognised losses to date, included in gross amount due from customers for contract work at 31 December 2013 is RMB196,609,000 (2012: RMB Nil). Advances received from customers under open construction contracts amounted to RMB20,451,000 (2012: RMB Nil).

23 OTHER FINANCIAL ASSETS

As at 31 December 2013, other financial assets consisted of principal-protected structural deposits placed in several commercial banks in the PRC.

24 PLEDGED BANK DEPOSITS

The deposits are pledged to banks as security against interest bearing borrowings (see note 26) and bills payable (see note 27).

25 CASH AND CASH EQUIVALENTS

	The Group		The Company	
	2013 RMB'000	2012 RMB'000	**2013 RMB'000**	2012 RMB'000
Cash at bank and in hand	**1,274,509**	984,131	**19,570**	22,378

As at 31 December 2013, deposits that were placed with banks in the PRC and included in the cash and cash equivalents above amounted to RMB796,834,000 (2012: RMB678,768,000). Remittance of funds out of the PRC is subject to the exchange restrictions imposed by the PRC government.

During the year ended 31 December 2013, inventories of RMB55,854,000 (2012: RMB 372,790,000) were transferred to fixed assets for the provision of oil and gas services.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

26 INTEREST-BEARING BORROWINGS

At 31 December 2013, the interest-bearing borrowings of the Group and the Company were secured as follows:

	The Group		The Company	
	2013	2012	**2013**	2012
	RMB'000	RMB'000	**RMB'000**	RMB'000
Bank loans				
— secured	**1,294,961**	535,435	**–**	–
— unsecured	**3,436,536**	1,434,384	**897,139**	–
	4,731,497	1,969,819	**897,139**	–
Loan from other financial institution				
— secured	**–**	13,200	**–**	–
	4,731,497	1,983,019	**897,139**	–

Interest-bearing borrowings of RMB1,294,961,000 (2012: RMB548,635,000) were secured by land use rights of RMB227,002,000 (2012: RMB99,474,000), fixed assets of RMB462,933,000 (2012: RMB96,844,000), bank deposits of RMB230,811,000 (2012: RMB213,200,000), trade and other receivables of RMB184,678,000 (2012: RMB Nil) and all assets of a subsidiary with an aggregate carrying value of RMB Nil (2012: RMB290,993,000).

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

26 INTEREST-BEARING BORROWINGS (continued)

At 31 December 2013, the interest-bearing borrowings of the Group and the Company were repayable as follows:

	The Group		The Company	
	2013 RMB'000	2012 RMB'000	2013 RMB'000	2012 RMB'000
Within 1 year or on demand	3,273,544	1,245,505	179,428	–
After 1 year but within 2 years	1,142,648	623,768	454,746	–
After 2 years but within 5 years	315,305	113,746	262,965	–
	1,457,953	737,514	717,711	–
	4,731,497	1,983,019	897,139	–

Certain banking facilities of the Group are subject to the fulfilment of covenants as are commonly found in lending arrangements with financial institutions. If the Group were to breach 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 34(b). As at 31 December 2013 and 2012, none of the covenants relating to drawn down facilities had been breached.

27 TRADE AND OTHER PAYABLES

	The Group		The Company	
	2013 RMB'000	2012 RMB'000	2013 RMB'000	2012 RMB'000
Trade payables	1,823,918	779,873	–	–
Bills payable	937,008	504,291	–	–
Receipts in advance	1,005,880	1,332,245	–	–
Other payables	474,156	495,928	3,293	64,650
	4,240,962	3,112,337	3,293	64,650

Bills payable as at 31 December 2013 and 2012 were secured by certain pledged bank deposits as disclosed in note 24. All of the trade and other payables are expected to be settled or recognised as income within one year or are repayable on demand.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

27 TRADE AND OTHER PAYABLES (continued)

At the end of the reporting period, the ageing analysis of the trade and bills payable (which are included in trade and other payables) based on the invoice date is as follows:

	The Group	
	2013	2012
	RMB'000	RMB'000
Within 3 months	**1,793,608**	880,065
3 months to 6 months	**642,406**	242,885
6 months to 1 year	**168,282**	69,397
Over 1 year	**156,630**	91,817
	2,760,926	1,284,164

28 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% (2012: 20% to 22%) of the standard wages determined by the relevant authorities in the PRC during the year ended 31 December 2013. The local government authority is responsible for the entire pension obligations payable to retired employees.

The Group operates a Mandatory Provident Fund Scheme ("the MPF scheme") under the Hong Kong Mandatory Provident Fund Schemes Ordinance for employees employed under the jurisdiction of the Hong Kong Employment Ordinance. The MPF scheme is a defined contribution retirement scheme administered by independent trustees. Under the MPF Scheme, the Group and its employees are each required to make contributions to the scheme at 5% of the employees' relevant income, subject to a cap of monthly relevant income of HKD25,000. Contributions to the scheme vest immediately.

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

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

29 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 options to subscribe for shares in the Company. 60,000,000 options were granted on 21 January 2008.

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

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

	2013		2012	
	Exercise price	**Number of options ('000 shares)**	Exercise price	Number of options ('000 shares)
Outstanding at the beginning of the year	**HKD3.83**	**57,089**	HKD3.83	57,344
Lapsed during the year	**HKD3.83**	**(405)**	HKD3.83	(255)
Outstanding at the end of the year	**HKD3.83**	**56,684**	HKD3.83	57,089
Exercisable at the end of the year	**HKD3.83**	**56,684**	HKD3.83	57,089

The options outstanding at 31 December 2013 had a weighted average remaining contractual life of 4.08 years (2012: 5.08 years).

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

29 EQUITY-SETTLED SHARE-BASED PAYMENTS (continued)

(b) SHARE OPTION SCHEME

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

	Number of options ('000 shares)		Vesting conditions	Contractual life of options
Options granted:				
— on 15 April 2009	60,000	(i)	30% on 1 December 2009	10 years
		(ii)	30% on 14 April 2010	
		(iii)	40% on 15 April 2011	
— on 11 October 2010	2,200	(i)	40% on 25 October 2010	10 years
		(ii)	30% on 11 October 2011	
		(iii)	30% on 11 October 2012	
— on 20 June 2011	7,600*	(i)	30% on 19 July 2011	10 years
		(ii)	30% on 20 June 2012	
		(iii)	40% on 20 June 2013	
— on 5 April 2012	15,400	(i)	30% on 5 April 2013	10 years
		(ii)	30% on 5 April 2014	
		(iii)	40% on 5 April 2015	
Total share options	85,200			

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

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

29 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:

	2013 Weighted average exercise price	2013 Number of options ('000 shares)	2012 Weighted average exercise price	2012 Number of options ('000 shares)
Outstanding at the beginning of the year	**HKD1.21**	**73,876**	HKD1.21	66,723
Granted during the year	**–**	**–**	HKD1.19	15,400
Exercised during the year	**HKD1.25**	**(8,034)**	HKD1.21	(7,334)
Forfeited during the year	**HKD1.19**	**(119)**	–	–
Lapsed during the year	**HKD1.27**	**(48)**	HKD1.27	(913)
Outstanding at the end of the year	**HKD1.20**	**65,675**	HKD1.21	73,876
Exercisable at the end of the year	**HKD1.20**	**55,013**	HKD1.23	55,436

The options outstanding at 31 December 2013 had an exercise price in the range of HKD0.83 to HKD1.27 (2012: HKD0.83 to HKD1.27) and a weighted average remaining contractual life of 6.23 years (2012: 7.14 years).

The weighted average share price at the date of exercise for share options exercised during the year ended 31 December 2013 was HKD3.70 (2012: HKD2.23).

(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.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

29 EQUITY-SETTLED SHARE-BASED PAYMENTS (continued)

(d) SHARE AWARD SCHEME

On 30 December 2011, the board of directors approved to adopt a Restricted Share Award Scheme (the "Scheme"). Under the Scheme, the Company may grant shares of the Company to certain selected participants at specified consideration.

Pursuant to the Scheme rules, existing issued shares will be purchased by the trustee of the Scheme (the "Trustee") from the market out of funds provided by the Company in accordance with the Scheme rules.

During the year ended 31 December 2012, 47,817,000 shares were acquired by the Trustee through purchases from the open market, at a total cost of approximately RMB49,973,000 (equivalent to HKD61,518,000).

During the year ended 31 December 2013, the Trustee acquired the Company's ordinary shares on The Stock Exchange of Hong Kong Limited as follows:

Month/year	Number of shares repurchased	Highest price paid per share HKD	Lowest price paid per share HKD	Aggregate price paid HKD'000
March 2013	5,751,000	4.02	3.92	22,852
April 2013	38,236,000	3.96	3.26	137,147
May 2013	6,013,000	3.80	3.74	22,657
				182,656

During the year ended 31 December 2013, the Company granted restricted shares in respect of a total of 4,780,000 and 31,137,700 ordinary shares of the Company through purchases by the Trustee to the directors and selected employees at a price of HK$1.27 each, of which 190,000 restricted shares granted to selected employees were forfeited. 50% of the restricted shares were vested on 20 May 2013 and the remaining 50% were vested on 20 December 2013.

The fair value of restricted shares granted to employees is measured with reference to the closing price of the ordinary share of the Company at the grant date and recognised as staff costs with a corresponding increase in the capital reserve within equity.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

30 INCOME TAX IN THE STATEMENT OF FINANCIAL POSITION

(a) CURRENT TAXATION IN THE STATEMENT OF FINANCIAL POSITION REPRESENTS:

	The Group	
	2013 RMB'000	2012 RMB'000
Current tax recoverable	**(16,406)**	(1,502)
Current tax payable	**51,453**	96,311
	35,047	94,809

(b) DEFERRED TAX ASSETS AND LIABILITIES RECOGNISED

The components of deferred tax assets/(liabilities) recognised in the Group's statement of financial position and the movements during the year are as follows:

	Write-down of inventories RMB'000	Provision for product warranties RMB'000	Unrealised profit on inventories RMB'000	Allowance for doubtful debts RMB'000	Accruals RMB'000	Tax losses RMB'000	Withholding tax on dividends RMB'000	Insurance premium paid RMB'000	Intangible assets RMB'000	Interest capitalisation RMB'000	Total RMB'000
Deferred tax arising from:											
At 1 January 2012	18,763	2,943	19,612	20,656	1,906	20,373	(14,692)	(4,013)	–	–	65,548
Credited/(charged) to profit or loss (note 7(a))	639	120	27,647	2,831	27,374	8,851	(38,784)	–	–	–	28,678
Exchange difference	–	–	–	–	–	–	–	24	–	–	24
At 31 December 2012	19,402	3,063	47,259	23,487	29,280	29,224	(53,476)	(3,989)	–	–	94,250
At 1 January 2013	**19,402**	**3,063**	**47,259**	**23,487**	**29,280**	**29,224**	**(53,476)**	**(3,989)**	**–**	**–**	**94,250**
Acquisition of subsidiaries (note 35)	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**(3,180)**	**–**	**(3,180)**
Credited/(charged) to profit or loss (note 7(a))	**(7,822)**	**2,491**	**(33,328)**	**10,038**	**(5,338)**	**7,371**	**15,556**	**3,931**	**–**	**(10,663)**	**(17,764)**
Exchange difference	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**58**	**–**	**–**	**58**
At 31 December 2013	**11,580**	**5,554**	**13,931**	**33,525**	**23,942**	**36,595**	**(37,920)**	**–**	**(3,180)**	**(10,663)**	**73,364**

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

30 INCOME TAX IN THE STATEMENT OF FINANCIAL POSITION (continued)

(b) DEFERRED TAX ASSETS AND LIABILITIES RECOGNISED (continued)

	The Group	
	2013	2012
	RMB'000	RMB'000
Deferred tax assets recognised on the statement of financial position	**123,975**	96,407
Deferred tax liabilities recognised on the statement of financial position	**(50,611)**	(2,157)
	73,364	94,250

(c) DEFERRED TAX ASSETS NOT RECOGNISED

In accordance with the accounting policy set out in note 2(t), the Group has not recognised deferred tax assets in respect of tax losses of RMB92,377,000 as at 31 December 2013 (2012: RMB56,631,000) as it is not probable that future taxable profits against which the losses can be utilised will be available in the relevant tax jurisdictions and entities. The tax losses of RMB87,975,000 (2012: RMB41,475,000) would be expired in 5 to 20 years while the tax losses of RMB4,402,000 (2012: RMB15,156,000) do not expire under current tax legislations of the entities.

(d) DEFERRED TAX LIABILITIES NOT RECOGNISED

At 31 December 2013, temporary differences relating to the undistributed profits of subsidiaries amounted to RMB2,166,857,000 (2012: RMB1,531,350,000). Deferred tax liabilities of RMB70,423,000 (2012: RMB99,659,000) have not been recognised in respect of the tax that would be payable on the distribution of these retained profits as the Company controls the dividend policy of these subsidiaries and it has been determined that it is probable that profits will not be distributed in the foreseeable future.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

31 PROVISIONS

	The Group	
	2013	2012
	RMB'000	RMB'000
Provision for a legal claim with former shareholders (note (a))	**32,317**	32,317
Provision for a legal claim with a former sales agency (note (b))	**99,078**	–
Provision for product warranties (note (c))	**37,026**	25,415
	168,421	57,732

(a) PROVISION FOR A LEGAL CLAIM WITH FORMER SHAREHOLDERS

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

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

On 11 December 2007, 57 out of the 64 original investors initiated legal proceedings at the Intermediate Peoples' Court of Chengdu City, Sichuan Province.

On 18 April 2012, Honghua Company received the first instance judgment ((2008) Cheng Min Chu Zi no. 53) from Chengdu Intermediate Court as follows: (1) Honghua Company shall pay to the plaintiffs' the economic loss of RMB20,728,750 and dividend of RMB296,125 together with their respective interests thereon (for the period from 26 April 2006 to the date when the payment is fully paid, based on the current interest rate of one year term loan of the People's Bank of China); (2) Honghua Company shall pay to the plaintiffs' other economic loss of RMB100,000; (3) the plaintiffs' other claims were dismissed. For the proceedings acceptance fee of RMB1,751,549, RMB200,000 shall be borne by the plaintiffs, and RMB1,551,549 shall be borne by Honghua Company.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

31 PROVISIONS (continued)

(a) PROVISION FOR A LEGAL CLAIM WITH FORMER SHAREHOLDERS (continued)

The management take the view that Honghua Company's repurchase of the equity interest and capital reduction were conducted under the PRC law. Honghua Company has therefore filed an appeal to the Sichuan Higher People's Court on 3 May 2012. The hearing by the court has been held in November 2012, the result of the hearing is expected to be issued in 2014.

A deed of indemnity in respect of the dispute and risk dated 15 February 2008 was entered into between some beneficiary owners of the Company (herein as defined "Indemnifiers") in favour of the Group pursuant to which each of the Indemnifiers jointly and severally provide an indemnity to any members of the Group for potential damages that the Company may suffer as result of the legal proceedings initiated by the 57 plaintiffs or the dispute with the 64 individuals.

As a result of the judgement made by the court, a provision for the above legal claim of RMB32,317,000 has been made during 2012. Pursuant to the deed of indemnity, the Group has the right to claim from the Indemnifiers the same amount of loss suffered from the legal claim. Accordingly, receivables from the Indemnifiers of the same amount and the corresponding credit to capital reserve (net of tax) have been recognised in the financial statements. There is no impact on both the net assets and cashflow of the Group.

(b) PROVISION FOR A LEGAL CLAIM WITH A FORMER SALES AGENCY

A sales agency filed lawsuits against Honghua Company and Honghua America on 22 September 2011. The court ordered the parties to arbitrate the dispute at the International Centre for Dispute Resolution of the American Arbitration Association ("ICDR").

On 27 November 2013, the Company received the final arbitration award from the ICDR. ICDR made an award against Honghua Company and Honghua America ordering Honghua Company and Honghua America to compensate the sales agency an aggregate sum of commissions, attorney's fees and other related fees in a sum of approximately USD16,000,000 (equivalent to RMB99,078,000). The arbitration award was confirmed by the U.S. court on 7 March 2014 subsequent to the year end.

As a result of the judgement made by the ICDR and the subsequent confirmation of the U.S. court, a provision for the above legal claim of RMB99,078,000 has been made during the year ended 31 December 2013.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

31 PROVISIONS (continued)

(c) PROVISION FOR PRODUCT WARRANTIES

	The Group	
	2013	2012
	RMB'000	RMB'000
At 1 January	**25,415**	21,243
Provision made	**31,809**	25,508
Utilised during the year	**(20,198)**	(21,336)
At 31 December	**37,026**	25,415

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.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

32 AMOUNTS DUE FROM SUBSIDIARIES

(a) MOVEMENTS IN COMPONENTS OF EQUITY

The amounts due from subsidiaries are unsecured, interest-free and repayable on demand.

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 33(c))	Share premium RMB'000 (note 33(d)(i))	Other reserve RMB'000 (note 33(d)(ii))	Capital reserve RMB'000 (note 33(d)(iii))	Exchange reserve RMB'000 (note 33(d)(v))	Shares held for share award scheme RMB'000 (note 29(d))	(Accumulated Losses)/ retained profits RMB'000	Total RMB'000
At 1 January 2012		299,593	2,477,519	389,691	95,100	(378,899)	–	(113,630)	2,769,374
Changes in equity for 2012:									
Profit for the year		–	–	–	–	–	–	161,846	161,846
Comprehensive income for the year		–	–	–	–	627	–	–	627
Total comprehensive income for the year		–	–	–	–	627	–	161,846	162,473
Shares purchased under share award scheme	29(d)	–	–	–	–	–	(49,973)	–	(49,973)
Equity-settled share-based transactions	29	–	–	–	4,809	–	–	–	4,809
Shares issued under share option schemes	29	599	9,469	–	(2,817)	–	–	–	7,251
Options lapsed under share option schemes	29	–	–	–	(736)	–	–	–	(736)
Dividends approved in respect of the previous year	33(b)	–	–	–	–	–	–	(104,700)	(104,700)
At 31 December 2012		300,192	2,486,988	389,691	96,356	(378,272)	(49,973)	(56,484)	2,788,498
At 1 January 2013		300,192	2,486,988	389,691	96,356	(378,272)	(49,973)	(56,484)	2,788,498
Changes in equity for 2013:									
Profit for the year		–	–	–	–	–	–	168,326	168,326
Comprehensive income for the year		–	–	–	–	(85,214)	–	–	(85,214)
Total comprehensive income for the year		–	–	–	–	(85,214)	–	168,326	83,112
Shares purchased under share award scheme	29(d)	–	–	–	–	–	(146,233)	–	(146,233)
Amortisation arising from share award scheme	29(d)	–	–	–	73,466	–	–	–	73,466
Vested shares transferred from share award scheme	29(d)	–	–	–	(73,466)	–	71,588	37,722	35,844
Equity-settled share-based transactions arising from share option schemes	29	–	–	–	2,430	–	–	–	2,430
Shares issued under share option schemes	29	641	10,711	–	(3,347)	–	–	–	8,005
Options lapsed under share option schemes	29	–	–	–	(508)	–	–	508	–
Dividends approved in respect of the previous year	33(b)	–	–	–	–	–	–	(150,102)	(150,102)
At 31 December 2013		300,833	2,497,699	389,691	94,931	(463,486)	(124,618)	(30)	2,695,020

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

33 CAPITAL, RESERVES AND DIVIDENDS (continued)

(b) DIVIDENDS

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

	2013 RMB'000	2012 RMB'000
Final dividend proposed after the end of the reporting period of HKD0.06 (2012: HKD0.06) per ordinary share	**151,983**	150,102

The final dividend proposed after the end of the reporting period has not been recognised as a liability at the end of the reporting period.

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

	2013 RMB'000	2012 RMB'000
Final dividend in respect of the previous financial year, approved and paid during the year, of HKD0.06 (2012: HKD0.04) per ordinary share	**150,102**	104,700

(c) SHARE CAPITAL

Authorised and issued share capital

	2013 Number of shares	2013 Amount '000	2012 Number of shares	2012 Amount '000
Authorised:				
Ordinary shares of HKD0.1 each	**10,000,000,000**	**HKD1,000,000**	10,000,000,000	HKD1,000,000
Equivalent to:		**RMB968,739**		RMB968,739

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

33 CAPITAL, RESERVES AND DIVIDENDS (continued)

(c) SHARE CAPITAL (continued)

Authorised and issued share capital (continued)

	2013 Number of shares	2013 Amount RMB'000	2012 Number of shares	2012 Amount RMB'000
Ordinary shares, issued and fully paid:				
At 1 January	**3,231,133,000**	**300,192**	3,223,799,000	299,593
Shares issued under share option schemes (note 29(b)(ii))	**8,034,000**	**641**	7,334,000	599
At 31 December	**3,239,167,000**	**300,833**	3,231,133,000	300,192

(d) NATURE AND PURPOSE OF RESERVES

(i) Share premium

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

(ii) Other reserve

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

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

33 CAPITAL, RESERVES AND DIVIDENDS (continued)

(d) NATURE AND PURPOSE OF RESERVES (continued)

(iii) Capital reserve

Capital reserve represents the value of employee services in respect of the equity-settled share-based payment as set out in note 29, waiver of debts by the immediate holding company and capital contribution arising on shareholders' indemnity.

(iv) Surplus reserve

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

(v) Exchange reserve

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

(vi) Fair value reserve

The fair value reserve comprises the cumulative net change in the fair value of available-for-sale securities held at the end of the reporting period and is dealt with in accordance with the accounting policies in notes 2(g) and 2 (l)(i).

(e) DISTRIBUTABILITY OF RESERVES

The Company's reserves available for distribution to its shareholders amounted to RMB2,518,805,000 as at 31 December 2013 (2012: RMB2,538,279,000). Under the Companies Law (Revised) of the Cayman Islands, the share premium of the Company is available for paying distributions or dividends to shareholders subject to the provisions of its memorandum and articles of association and provided that immediately following the payment of distribution or dividends, the Company is able to pay its debts as they fall due in the ordinary course of business. In accordance with the Company's articles of association, distributions shall be payable out of the profits or other reserves, including the share premium account, of the Company.

33 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 statement of financial position.

During 2013, the Group's strategy, which was unchanged from 2012, 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 2013 and 2012 are 1.89 and 1.14 respectively.

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

34 FINANCIAL RISK MANAGEMENT AND FAIR VALUE

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

(a) CREDIT RISK

The Group's credit risk is primarily attributable to trade and other receivables. Management has a credit policy in place and the exposures to these credit risks are monitored on an on-going basis.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

34 FINANCIAL RISK MANAGEMENT AND FAIR VALUE (continued)

(a) CREDIT RISK (continued)

In respect of trade and other receivables, individual credit evaluations are performed on all customers requiring credit over a certain amount. These evaluations focus on the customer's past history of making payments when due and current ability to pay, and take into account information specific to the customer as well as pertaining to the economic environment in which the customer operates. The Group maintains different billing policies for different customers based on the negotiated terms with each of the customers. The Group will issue progress billing at different stages such as upon the signing of contracts and upon the delivery of products. The exact percentage of each part of payment varies from contract to contract. Trade receivables are due within 90 days from the date of billing. The Group negotiates with those debtors with overdue balances to agree a repayment schedule by both parties and regularly evaluates the credit quality of its debtors to assess the necessity to revise the credit term. Debtors with balances that are more than 24 months past due are requested to settle all outstanding balances before any further credit is granted.

The Group's exposure to credit risk is influenced mainly by the individual characteristics of each customer rather than the industry or country in which the customers operate and therefore significant concerns of credit risk primarily due to significant exposure to individual customers. At the end of the reporting period, 19% (2012: 22%) and 44% (2012: 46%) of the total trade receivables was due from the Group's largest debtor and the five largest debtors respectively.

The Group does not provide any other guarantees which would expose the Group or the Company to credit risk.

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.

Further quantitative disclosures in respect of the Group's exposure to credit risk arising from trade and other receivables are set out in note 21.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

34 FINANCIAL RISK MANAGEMENT AND FAIR VALUE (continued)

(b) LIQUIDITY RISK

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

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

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

The Group and the Company

	The Group		The Company	
	2013 RMB'000	2012 RMB'000	**2013 RMB'000**	2012 RMB'000
Within 1 year	**3,412,655**	1,442,952	**214,322**	–
More than 1 year but less than 2 years	**1,167,896**	647,333	**469,581**	–
More than 2 years but less than 5 years	**331,290**	121,602	**271,867**	–
Total contractual undiscounted cash outlow	**4,911,841**	2,211,887	**955,770**	–
Carrying value	**4,731,497**	1,983,019	**897,139**	–

Save as above, the Group's and the Company's other financial liabilities are required to be settled within one year or on demand and the total contractual undiscounted cash flows of these financial liabilities approximate to their carrying amounts on the statements of financial position.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

34 FINANCIAL RISK MANAGEMENT AND FAIR VALUE (continued)

(c) INTEREST RATE RISK

The Group's interest rate risk arises primarily from bank borrowings. 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 and floating rate debt obligations. Most of the interest-bearing borrowings of the Group as of 31 December 2013 are variable rate instruments.

(i) Interest rate profile

The following table details the interest rate profile of the Group's and the Company's interest-bearing liabilities at the end of the reporting period.

	The Group			
	2013		2012	
	Effective interest rate %	**Amount RMB'000**	Effective interest rate %	Amount RMB'000
Fixed rate borrowings:				
Interest-bearing borrowings	**1.05%–6.65%**	**1,252,036**	3.50%–6.50%	459,985
Variable rate borrowings:				
Interest-bearing borrowings	**1.17%–7.22%**	**3,479,461**	1.17%–6.72 %	1,523,034
Total borrowings:		**4,731,497**		1,983,019
Fixed rate borrowings as a percentage of total borrowings		**26%**		23%

	The Company			
	2013		2012	
	Effective interest rate %	**Amount RMB'000**	Effective interest rate %	Amount RMB'000
Variable rate borrowings:				
Interest-bearing borrowings	**4.10%**	**897,139**	–	–

34 FINANCIAL RISK MANAGEMENT AND FAIR VALUE (continued)

(c) INTEREST RATE RISK (continued)

(ii) Sensitivity analysis

At 31 December 2013, it is estimated that a general increase/decrease of 50 basis points in interest rates, with all other variables held constant, would have decreased/increased the Group's profit after tax by approximately RMB12,497,000 (2012: RMB3,176,000).

The sensitivity analysis above indicates the instantaneous change in the Group's profit after tax (and retained profits) that would arise assuming that the change in interest rates had occurred at the end of the reporting period, the impact on the Group's profit after tax (and retained profits) is estimated as an annualised impact on interest expense or income of such a change in interest rates. The analysis is performed on the same basis for 2012.

(d) CURRENCY RISK

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

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

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

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

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

34 FINANCIAL RISK MANAGEMENT AND FAIR VALUE (continued)

(d) CURRENCY RISK (continued)

The following table details the Group's exposure at the end of the reporting period 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

	2013 Exposure to foreign currencies (expressed in RMB'000)		
	USD	**EUR**	**RMB**
Cash and cash equivalents	**253,375**	**–**	**4,382**
Trade and other receivables	**2,046,656**	**21,047**	**76,726**
Interest-bearing borrowings	**(1,162,234)**	**–**	**–**
Trade and other payables	**(841,890)**	**–**	**(215,381)**
Overall net exposure	**295,907**	**21,047**	**(134,273)**

	2012 Exposure to foreign currencies (expressed in RMB'000)		
	USD	EUR	RMB
Cash and cash equivalents	330,432	12,635	35,242
Trade and other receivables	1,472,148	44,803	–
Interest-bearing borrowings	(943,962)	–	–
Trade and other payables	(848,806)	–	(389,882)
Overall net exposure	9,812	57,438	(354,640)

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

34 FINANCIAL RISK MANAGEMENT AND FAIR VALUE (continued)

(d) CURRENCY RISK (continued)

Sensitivity analysis

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

	The Group					
	2013			2012		
	Weakening/ (strengthening) of functional currency against these currencies	Increase/ (decrease) on profit after tax RMB'000	Increase/ (decrease) on retained profits RMB'000	Weakening/ (strengthening) of functional currency against these currencies	Increase/ (decrease) on profit after tax RMB'000	Increase/ (decrease) on retained profits RMB'000
USD	5%	9,094	9,094	5%	417	417
	(5)%	(9,094)	(9,094)	(5)%	(417)	(417)
EUR	5%	852	852	5%	2,325	2,325
	(5)%	(852)	(852)	(5)%	(2,325)	(2,325)
RMB	5%	(4,946)	(4,946)	5%	(13,331)	(13,331)
	(5)%	4,946	4,946	(5)%	13,331	13,331

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

The sensitivity analysis assumes that the change in foreign exchange rates had been applied to re-measure those financial instruments held by the Group which expose the Group to foreign currency risk at the end of the reporting period, 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 2012.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

34 FINANCIAL RISK MANAGEMENT AND FAIR VALUE (continued)

(e) FAIR VALUES

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

(i) *Cash and cash equivalents, bank deposits maturing over three months, pledged bank deposits, other financial assets, 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) *Amounts due from/to related companies*

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

(iv) *Other financial assets*

The fair value of other financial assets is estimated as being the present value of future cash flows, discounted at interest rates based on the expected/realised rates of return of the underlying principal-protected structural deposits.

34 FINANCIAL RISK MANAGEMENT AND FAIR VALUE (continued)

(e) FAIR VALUES (continued)

(v) Assets acquired through a business combination

The fair value of items of fixed assets is based on cost approach using historical costs and depreciated replacement cost when appropriate. Depreciated replacement cost reflects adjustments for physical deterioration as well as functional and economic obsolescence. The fair value of items of interests in leasehold land held for own use under operating lease is based on the open market approach using quoted market price for similar items when available less the estimated costs to sales. The fair value of the intangible assets is based on the income approach using the relief from royalty method to value the intangible assets. The income approach is based on the assumption that if an intangible asset has to be licensed from a third party owner, a royalty rate on turnover will be charged for the privilege of using the asset. By owning the asset, such royalties are avoided.

(vi) Fair value hierarchy and valuation process

The following table presents the fair value of the Group's other investment, other financial assets and assets acquired through a business combination measured at the end of the reporting period, categorised in to the three-level fair value hierarchy as defined in IFRS 13, Fair value measurement. The level into which a fair value measurement is classified is determined with reference to the observability and significance of the inputs used in the valuation technique as follows:

Level 1 valuations: Fair value measured using only Level 1 inputs i.e. unadjusted quoted prices in active markets for identical assets or liabilities at the measurement date.

Level 2 valuations: Fair value measured using Level 2 inputs i.e. observable inputs which fail to meet Level 1, and not using significant unobservable inputs. Unobservable inputs are inputs for which market data are not available.

Level 3 valuations: Fair value measured using significant unobservable inputs.

The Group has an established control framework with respect to the measurement of fair values. The management has overall responsibility for overseeing all significant fair value measurements, including Level 3 fair values and reports directly to the management.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

34 FINANCIAL RISK MANAGEMENT AND FAIR VALUE (continued)

(e) FAIR VALUES (continued)

(vi) Fair value hierarchy and valuation process (continued)

The management regularly reviews significant unobservable inputs and valuation adjustments. If third party information is used to measure fair values, then the management assesses the evidence obtained from the third parties to support the conclusion that such valuations meet the requirements of IFRS, including the level in the fair value hierarchy in which such valuations should be classified.

The fair value measurement of other financial assets and valuation of fair values of fixed assets, leasehold land held for own use under operating lease and intangible assets arising from business combination are categorised into Level 3 in the fair value hierarchy.

During the years ended 31 December 2012 and 2013, there were no transfer into or out of Level 3. The Group's policy is to recognise transfers between levels of fair value hierarchy as at the end of the reporting period in which they occur.

The movements during the period in the balance of these Level 3 fair value measurements are as follows:

	2013 RMB'000	2012 RMB'000
Other financial assets:		
At 1 January	**315,036**	678,000
Net payment/(proceeds) from purchases or sales	**488,464**	(362,964)
Net unrealised gains recognised in other comprehensive income during the period	**602**	–
At 31 December	**804,102**	315,036

The gain arising from the disposal of the other financial assets are presented in "net finance (expenses)/income" in the consolidated statement of profit or loss.

Given the short-term nature of other financial assets (with remaining maturity ranged from 7 days to 3 months), an increase/decrease in expected rates of return would not have a significant impact on the fair value and hence the Group's other comprehensive income.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

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

35 ACQUISITION OF SUBSIDIARIES

On 25 March 2013, the Group completed the acquisition of 55% equity interests in Bazhou Honghua Petroleum Applied Chemistry Co., Ltd. ("Bazhou Company") and its subsidiaries at a cash consideration of RMB51,900,000. Bazhou Company is principally engaged in manufacturing drilling fluid material and related drilling services. The Group expects that the acquisition will enhance the Group's technology level in oil-based drilling and enable the Group to access to the acquiree's technical talent, so as to raise the profitability in oil and gas engineering services segment.

Details of the fair value of net identifiable assets acquired are as follows:

	Fair value of net identifiable assets acquired as at the acquisition date RMB'000
Fixed assets	48,353
Construction in progress	41,911
Intangible assets	21,200
Trade and other receivables	37,886
Inventories	65,605
Cash and cash equivalents	3,801
Trade and other payables	(134,747)
Current tax payable	(10,981)
Deferred tax liabilities	(3,180)
Total net identifiable assets at fair value	69,848

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

35 ACQUISITION OF SUBSIDIARIES (continued)

	RMB'000
Goodwill arising from the acquisition	
Total consideration transferred	51,900
Non-controlling interests, based on their proportionate interest in the net identifiable assets of Bazhou Company	31,432
Fair value of net identifiable assets	(69,848)
Goodwill	13,484
Cash consideration	51,900
Cash and cash equivalent balances acquired	(3,801)
Net cash outflow arising from acquisition	48,099

The fair values are determined based on a valuation performed by an independent third party valuer.

Notes:

(i) The Group has chosen to measure the non-controlling interests ("NCI") in Bazhou Company at fair value for this acquisition. The fair value of the NCI of RMB31,432,000 is determined based on the valuation.

(ii) The consideration for this acquisition of RMB51,900,000 has been fully paid as at 31 December 2013.

(iii) The goodwill is attributable mainly to the skills and technical talent of Bazhou Company's work force, and the synergies expected to be achieved from integrating the Bazhou Company into the Group's existing oil and gas engineering services.

(iv) For the period from date of acquisition to 31 December 2013, Bazhou Company contributed a revenue of RMB69,716,000 and profit of RMB4,690,000 to the Group's results. If the acquisition had occurred on 1 January 2013, management estimates that consolidated revenue would have been RMB8,054,673,000 and consolidated profit for the year would have been RMB557,574,000. In determining these amounts, management have assumed that the fair value adjustments determined by the independent valuation that arose on the acquisition date would have been the same if the acquisition had occurred on 1 January 2013.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

36 COMMITMENTS

(a) CAPITAL COMMITMENTS

Capital commitments outstanding at 31 December 2013 not provided for in the financial statements were as follows:

	The Group	
	2013 RMB'000	2012 RMB'000
Contracted for	**640,927**	504,277
Authorised but not contracted for	**736,617**	307,721
	1,377,544	811,998

(b) OPERATING LEASE COMMITMENTS

At 31 December 2013, the total future minimum lease payments under non-cancellable operating leases are payable as follows:

	The Group	
	2013 RMB'000	2012 RMB'000
Within 1 year	**8,054**	5,339
After 1 year but within 5 years	**11,314**	5,567
After 5 years	**6,014**	7,320
	25,382	18,226

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.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

37 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 MATERIAL RELATED PARTIES OF THE GROUP:

Name of party	Relationship
Guanghan Hongtai Business Trading Co. Ltd (廣漢市宏泰商貿有限公司) ("Hongtai Company")	Hongtai Company is a party which spouses of certain directors and management have equity interest.
NCE Management, LLC ("NCE Management")	NCE Management is a party which certain management of Honghua America have equity interest.
Sichuan Shenyuan Drilling Rig Equipment Company (四川深遠石油鑽井工具有限公司) ("Sichuan Shenyuan Company")	Sichuan Shenyuan Company is a party which the spouse of the director has equity interest.
HH Egyptian Company	Joint venture
Honghua CIS Ltd.	Joint venture
Mr. Li Ming (黎明)	Director and management of a Group's subsidiary.
Kashi Tongbai Property Development Limited (喀什通百房地產開發有限公司) ("Kashi Company")	Kashi Company is a party which a director of a Group's subsidiary has equity interest.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

37 MATERIAL RELATED PARTY TRANSACTIONS (continued)

(b) PARTICULARS OF SIGNIFICANT TRANSACTIONS BETWEEN THE GROUP AND THE ABOVE RELATED PARTIES DURING THE RELEVANT PERIOD ARE AS FOLLOWS:

	The Group	
	2013	2012
	RMB'000	RMB'000
Purchases of parts and components		
Related companies	**31,443**	26,794
Sale of drilling rigs, parts and components		
Joint ventures	**5,341**	89,732

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

(c) AMOUNTS DUE FROM RELATED COMPANIES

	The Group	
	2013	2012
	RMB'000	RMB'000
Trade		
Joint ventures	**12,801**	51,588
Non-trade		
Related companies	**31,654**	2,174
Joint ventures	**337**	2,178
Immediate/ultimate holding company	**27**	30
	32,018	4,382
	44,819	55,970

The amounts due from related companies are unsecured, interest free and repayable on demand. No provision was made against the amounts due from related companies at 31 December 2013 (2012: RMB Nil).

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

37 MATERIAL RELATED PARTY TRANSACTIONS (continued)

(d) AMOUNTS DUE TO RELATED COMPANIES

	The Group	
	2013	2012
	RMB'000	RMB'000
Trade		
Related companies	**15,768**	5,523
Joint ventures	**11,697**	70
	27,465	5,593

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

(e) AMOUNTS DUE FROM CERTAIN SHAREHOLDERS

The amounts due from certain shareholders as at 31 December 2013 is an amount of RMB32,317,000 (2012: RMB32,317,000), being the amount indemnified by certain shareholders in relation to a legal claim, details of which are set in note 31(a).

(f) KEY MANAGEMENT PERSONNEL REMUNERATION

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

	The Group	
	2013	2012
	RMB'000	RMB'000
Basic salaries, allowances and other benefits in kind	**6,237**	6,442
Contributions to defined contribution retirement schemes	**259**	240
Discretionary bonus	**5,596**	12,982
Share-based payments	**20,016**	2,043
	32,108	21,707

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

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

38 IMMEDIATE AND ULTIMATE HOLDING COMPANY

The directors consider the immediate holding company and the ultimate holding company as at 31 December 2013 are Ally Giant Limited and Ample Chance International Limited respectively, which are incorporated in the British Virgin Islands. These entities do not produce financial statements available for public use.

39 CONTINGENT LIABILITIES

CONTINGENT LIABILITIES IN RESPECT OF LEGAL CLAIM

Lawsuits with a sales agency

A sales agency filed lawsuit against a subsidiary of the Company, alleged that it was owed commissions in excess of USD18,000,000 in relation to its services to the Group.

On 24 April 2013, the United Arab Emirates ("UAE") Federal Court of First Instance ordered the termination of the agency agreement and dismissed all claims from the sales agency. The sales agency filed an appeal to the UAE Federal Court of Appeal on the court's decision and hearing is yet to be made as at 31 December 2013.

Having consulted the Group's legal advisors, management considered that the Group had legal and factual merit to defend in the lawsuit. Accordingly, management determined that it was not probable that the outcome of the lawsuit will be unfavourable to the Group. No provision was made for the potential claim under this lawsuit.

NOTES TO THE FINANCIAL STATEMENTS

(Expressed in Renminbi unless otherwise indicated)

40 POSSIBLE IMPACT OF AMENDMENTS, NEW STANDARDS AND INTERPRETATIONS ISSUED BUT NOT YET EFFECTIVE FOR THE YEAR ENDED 31 DECEMBER 2013

Up to the date of issue of these financial statements, the IASB has issued a number of amendments and five new standards which are not yet effective for the year ended 31 December 2013 and which have not been adopted in these financial statements. These include the following which may be relevant to the Group.

	Effective for accounting periods beginning on or after
Amendments to IAS 32, Financial instruments: Presentation — Offsetting financial assets and financial liabilities	1 January 2014
IFRS 9, Financial instruments	Not yet established by IASB

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 with the exception of IFRS 9, is unlikely to have a significant impact on the Group's results of operations and financial position.

The mandatory effective date of IFRS 9 has not yet been established and IASB is working to expand IFRS 9 to add new requirements in respect of macro hedging. Accordingly, the impact of IFRS 9 may change as a consequence of further developments resulting from the IASB's project to replace IAS39. As a result, it is impractical to quantify the impact of IFRS 9 as at the date of these accounts.

FIVE-YEAR FINANCIAL HIGHLIGHTS

	2013 RMB'000	2012 RMB'000	2011 RMB'000	2010 RMB'000	2009 RMB'000 (restated)
Consolidated Income Statement					
Turnover	8,047,108	5,068,447	3,485,046	1,877,931	1,961,517
Cost of sales	(6,141,643)	(3,321,440)	(2,514,942)	(1,497,453)	(1,444,081)
Gross profit	1,905,465	1,747,007	970,104	380,478	517,436
Other revenue	176,469	63,333	27,444	29,900	7,085
Other net income/(loss)	7,435	2,084	60,012	(5,274)	9,234
Selling expenses	(524,053)	(553,623)	(385,532)	(180,642)	(179,980)
General and administrative expenses	(595,508)	(526,562)	(408,877)	(340,360)	(474,334)
Other operating expenses	(121,442)	(59,546)	(19,295)	(3,905)	(803)
Profit/(loss) from operations	848,366	672,693	243,856	(119,803)	(121,362)
Net finance (expenses)/income	(139,418)	29,259	(50,335)	(59,441)	(3,709)
Share of (loss)/profit from jointly controlled entities	(7,948)	(156)	293	2,801	(4,766)
Share of profit from an associate	–	7,662	5,398	–	–
Profit/(loss) before taxation	701,000	709,458	199,212	(176,443)	(129,837)
Income tax (expenses)/credit	(125,750)	(167,683)	(27,769)	4,372	7,126
Profit/(loss) for the year	575,250	541,775	171,443	(172,071)	(122,711)
Attributable to:					
Equity shareholders of the Company	537,617	529,458	167,984	(184,165)	(127,963)
Non-controlling interests	37,633	12,317	3,459	12,094	5,252
Figures per share					
Earnings/(loss) per share (RMB cents)					
— Basic	16.99	16.58	5.21	(5.71)	(3.97)
— Diluted	16.77	16.54	5.21	(5.71)	(3.97)
Dividend					
Dividends declared and paid	–	–	–	–	–
Dividends declared and paid per share	–	–	–	–	–
Dividend proposed after balance sheet date	151,983	150,102	104,700	–	–
Dividend proposed after balance sheet date per share	HKD 0.06	HKD 0.06	HKD 0.04	–	–

FIVE-YEAR FINANCIAL HIGHLIGHTS

	2013 RMB'000	2012 RMB'000	2011 RMB'000	2010 RMB'000	2009 RMB'000 (restated)
Consolidated Balance Sheet					
Total non-current assets	**4,548,371**	3,227,901	1,882,332	1,354,893	1,209,071
Total current assets	**9,680,684**	6,617,975	4,810,368	4,639,753	5,375,375
Total assets	**14,229,055**	9,845,876	6,692,700	5,994,646	6,584,446
Total current liabilities	**7,761,845**	4,517,478	2,119,137	1,729,051	2,062,235
Total non-current liabilities	**1,508,564**	739,671	398,705	194,804	262,804
Total liabilities	**9,270,409**	5,257,149	2,517,842	1,923,855	2,325,039
Total equity	**4,958,646**	4,588,727	4,174,858	4,070,791	4,259,407

Key financial ratios	2013	2012	2011	2010	2009 (restated)
Profitability					
Gross margin	**23.7%**	34.5%	27.8%	20.3%	26.4%
EBITDA margin	**13.4%**	16.3%	10.2%	(1.5%)	(2.2%)
Net margin	**6.7%**	10.4%	4.8%	(9.8%)	(6.5%)
Return					
Return on average equity	**11.7%**	12.4%	4.2%	(4.5%)	(3.0%)
Return on average assets	**4.5%**	6.4%	2.6%	(2.9%)	(1.8%)
Liquidity					
Current ratio	**1.25**	1.46	2.27	2.68	2.61
Quick ratio	**0.89**	0.86	1.54	1.61	1.69
Turnover					
Turnover of average trade and bills receivable	**107**	95	104	163	217
Turnover of average trade and bills payable	**120**	119	113	145	177
Turnover of average inventory	**165**	235	247	458	497
Gearing					
Total debts/Total assets	**33.3%**	20.1%	13.1%	10.4%	19.7%
Total liabilities/Total assets	**65.2%**	53.4%	37.6%	32.1%	35.3%
EBIT/Interest expenses	**3.98**	8.77	4.6	(2.5)	(1.9)

FIVE-YEAR FINANCIAL HIGHLIGHTS

Note:

Profitability		
Gross margin	=	Gross profit/Turnover
EBITDA	=	(Loss)/profit from operations + Share of (loss)/profit from jointly controlled entities + share of profit from an associate + Depreciation + Amortization
EBITDA margin	=	EBITDA/Turnover
Net margin	=	(Loss)/profit attributable to equity shareholders of the Company/Turnover
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/Turnover
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 + share of profit from an associate)/Interest expenses (including the interest expense capitalized into assets under construction)

DEFINITIONS

"Articles of Association"	the Articles of Association of the Company, approved at extraordinary shareholders' meetings of the Company on 21 January 2008, revised and approved at annual general meeting of the Company on 3 June 2009
"Board of Directors" or "Board"	the Board of Directors of the Company
"Companies Ordinance"	the Companies Ordinance (Chapter 622 of the Laws of Hong Kong) and the Companies (Winding Up and Miscellaneous Provisions) Ordinance (Chapter 32 of the Laws of Hong Kong), as the case may be
"Company" or "our Company" or "Honghua"	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 Limited, Ample Chance International Limited, Ally Smooth Investments Limited, Charm Moral International Limited, Beauty Clear Holdings Limited, Believe Power International Limited, Benefit Way International Limited, Wealth Afflux Limited, Mowbray Worldwide Limited, Ecotech Enterprises Corporation, Vast & Fast Corporation, Cavendish Global Corporation, Brondesbury Enterprises Limited, Dobson Global Inc, Darius Enterprises Limited, Zhang Mi (張弭), Ren Jie (任杰), Liu Zhi (劉智), Zheng Yong (鄭勇), Zuo Huixian (左輝先), Zhang Xu (張旭), Wang Jiangyang (王江陽), Chen Jun (陳俊), Fan Bing (范兵), Zhang Yanyong (張彥永), Ao Pei (敖沛), Tian Diyong (田弟勇), Shen Dingjian (沈定建), Liu Xuetian (劉學田) (deceased), Zhou Bing (周兵), Lv Lan (呂蘭), Tian Yu (田雨), Li Hanqiang (李漢強), Liu Yingguo (劉映國) and Liu Lulu (劉露璐). Contracts executed by the Controlling Shareholders after Liu Xuetian's death were executed by his legal successors

DEFINITIONS

"Director(s)"	member(s) of the Board of Directors of the Company
"During the Year"	for the year ended 31 December 2013
"Group" or "we" or "us" or "Honghua Group"	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
"HKD" or "HK dollars"	Hong Kong dollars, the lawful currency of Hong Kong
"Hong Kong" or "HK"	the Hong Kong Special Administrative Region of the PRC
"Honghua Company"	Sichuan Honghua Petroleum Equipment Co., Ltd. (四川宏華石油設備有限公司), formerly known as Chuanyou Guanghan Honghua Co., Ltd. (川油廣漢宏華有限公司), a limited liability company established in the PRC on 31 December 1997, and a wholly-owned subsidiary of Honghua Holdings Limited
"Honghua Oil & Gas Engineering"	Honghua Oil & Gas Engineering and Technology Services (Sichuan) Co., Ltd. (宏華油氣工程技術服務(四川)有限公司), a limited liability company established in the PRC and an indirect wholly-owned subsidiary of the Company
"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
"Last Year"	for the year ended 31 December 2012
"Listing Rules"	the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (as amended from time to time)
"PRC" or "China"	the People's Republic of China and, except where the context requires and only for the purpose of this Annual Report, references in this Annual Report to the PRC or China do not apply to Taiwan or Hong Kong and Macau Special Administrative Regions
"RMB" or "Renminbi"	Renminbi, the lawful currency of the PRC
"Russia"	The Russian Federation
"Securities and Futures Commission" or "SFC"	the Securities and Futures Commission of Hong Kong

DEFINITIONS

"SFO"	the Securities and Futures Ordinance (Chapter 571 of the Laws of Hong Kong)
"Share(s)"	ordinary shares issued by the Company, with a nominal value of HK$0.10 each
"Shareholder(s)"	holder(s) of our Share(s)
"Shenyuan Company"	Sichuan Deep & Fast Oil Drilling Tools Co., Ltd. (四川深遠石油鑽井工具有限公司), a limited liability company established in Chengdu, PRC
"Stock Exchange"	The Stock Exchange of Hong Kong Limited
"Substantial Shareholder(s)"	has the meaning ascribed to it under the Listing Rules
"UAE"	the United Arab Emirates
"United States", or "U.S."	the United States of America, including its territories and possessions
"US$" or "USD"	United States dollars, the lawful currency of the United States

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宏华集团有限公司
HONGHUA GROUP LIMITED