AAG

AAG Energy Holdings Limited
亞美能源控股有限公司
(Incorporated in the Cayman Islands with limited liability)
(Stock Code: 2686)

ANNUAL RESULTS ANNOUNCEMENT FOR THE YEAR ENDED 31 DECEMBER 2017

Key Highlights:

- **2017 revenue (including subsidy and VAT refund) increased by 31.2%, while profit for the year and EBITDA increased by 71.9% and 59.1%, respectively**
- **The Board of Directors recommends a final full year dividend of HK$0.0248/share for approval by shareholders of the Company at the upcoming Annual General Meeting.**
- **Gross production increased 16% YoY and exceeded 614.0 MMCM target for 2017**
  - — 2017 gross production reached 629.9 MMCM, 13% YoY increase for Panzhuang and 67% YoY increase for Mabi
  - — By December 2017, daily production reached 1.9 MMCM per day, an 18% YoY increase
- **Substantial decrease in drilling and completion costs**
  - — Total Capex of RMB487.3 million compared with RMB602.0 million, a 19% saving
  - — The 45 SLH wells for Panzhuang had an average drilling cost of RMB2.9 million compared with a 2016 average of RMB3.8 million, a 25% YoY decrease
  - — The average costs of 67 wells for drilling and completion for Mabi in 2017 are approximately 30% and 25% lower respectively compared to similar type well's historical average cost
- **Panzhuang gas sales with exceptional utilization rate of 98% in 2017 and realized a higher ASP of RMB1.31/cm in 2017 compared to RMB1.20/cm in 2016**
- **Mabi entered into exploration phase sales agreement with PetroChina with effect from 1 July 2017 with an ASP of RMB1.14/cm and commenced recognizing revenues and expenses**
- **HSE demonstrated strong performance with expanding operations in 2017**

Dear shareholders,

On behalf of the board (the "**Board**") of directors (the "**Directors**") of AAG Energy Holdings Limited ("**AAG**" or the "**Company**", together with its subsidiaries, collectively the "**Group**"), we hereby present the annual results of the Company for the year ended 31 December 2017.

FINANCIAL SUMMARY

	Year ended 31 December	
	2017	2016
	RMB'000	*RMB'000*
Revenue	**541,598**	411,278
Other income	**193,913**	149,276
Profit from operations	**322,122**	197,140
EBITDA	**432,541**	271,753
Adjusted EBITDA	**465,202**	332,908
Profit for the year	**183,198**	106,635
Basic earnings per share (RMB)	**0.055**	0.032
Diluted earnings per share (RMB)	**0.055**	0.032

	As at 31 December	
	2017	2016
	RMB'000	*RMB'000*
Property, plant and equipment	**3,504,437**	3,188,674
Cash and bank balances	**2,274,633**	2,375,347
Total assets	**6,132,689**	5,938,474
Total equity	**4,950,345**	4,836,934

BUSINESS REVIEW

We are pleased to announce the Group continues to deliver strong production growth compared with 2016. The Group's 2017 gross gas production increased by 16.4% to 629.9 million cubic meters ("**MMCM**") (22.3 billion cubic feet ("**bcf**")) (comprising Panzhuang's gross production of 571.6 MMCM (20.2 bcf) and Mabi's gross production of 58.3 MMCM (2.1 bcf)) compared with 2016.

During 2017, AAG realized a higher average selling price ("**ASP**") of RMB1.30/cubic meter ("**cm**") comprising an ASP of RMB1.31/cm and RMB1.14/cm for Panzhuang and Mabi, respectively (compared to RMB1.20/cm for Panzhuang for 2016). This increase in ASP for Panzhuang was driven by government policy of "coal-to-gas conversion" and increased demand for gas in the winter months.

In July 2017, we entered into the exploration phase sales contract with PetroChina Company Limited ("**PetroChina**") and Mabi began to recognize revenues and expenses in the second half of 2017 ("**2H2017**").

The combination of rapid drilling and completion with continuous optimization of well design and implementation, and more new wells ramped up production in Panzhuang and Mabi which led to increased production output in 2017.

Revenue (including subsidy and VAT refund) in 2017 increased by 31.2% to RMB735.5 million compared with 2016. Profit from operations in 2017 increased by 63.4% to RMB322.1 million. Profit for the year in 2017 increased by 71.9% to RMB183.2 million. EBITDA in 2017 increased by 59.1% to RMB432.5 million.

The total annual incurred Capex was RMB487.3 million, compared to the budget of RMB602.0 million. The average drilling cost for 1 single lateral horizontal ("**SLH**") well in Panzhuang was reduced by approximately RMB0.9 million per well from 2016. For Mabi, the average drilling cost for 1 pad drill well ("**PDW**") was about RMB0.8 million by the end of 2017, representing only 75% of similar type well's historical average cost. Looking forward, AAG remains committed to driving costs down and keeping a healthy margin.

PROPOSED DIVIDEND

The Board recommends a final full year dividend of HK$0.0248/share for the year ended 31 December 2017 in view of the strong operational and financial performance combined with stringent cost control. The Company's continuing strong cash position, increased cash flow from operations and unused borrowing facilities enable the payment of the Company's first dividends.

The outlook for the Company's business remains strong and supports its ability to sustain this dividend in the future.

OPERATIONS REVIEW

We continued focusing on the Health, Safety and Environment ("**HSE**") performance with expanding operation activities. AAG has achieved 5 million man-hours (3 years and 111 days) without Lost Time Injury on 25 December 2017.

We have achieved significant progress towards certain key operational objectives for its two key assets operated by the Group's two subsidiaries: Panzhuang concession operated by Sino-American Energy, Inc. ("**SAEI**") and Mabi concession operated by Asian American Gas, Inc. ("**AAGI**").

- **Panzhuang Concession**

  AAG's Panzhuang concession in partnership with China United Coalbed Methane Corporation Ltd. ("**CUCBM**") continues to be the highest producing coalbed methane ("**CBM**") natural gas project in China, and was designated as the leading CBM production sharing contract in China under the Thirteenth Five-Year Development and Utilization Plan for Coalbed Methane ("**Energy Plan**") released by the National Energy Administration (國家能源局, "**NEA**") and the National Development and Reform Commission (國家發展和改革委員會, "**NDRC**").

- **Panzhuang production update**

  Total annual production from Panzhuang reached 571.6 MMCM (20.2 bcf), surpassing our 2017 production target of 557.2 MMCM (19.7 bcf) with an 13% increase year on year ("**YoY**"). Panzhuang's average daily production in 2017 was 1.57 MMCM per day ("**MMCMD**"), an 13.4% increase YoY. The sales utilization rate in Panzhuang has remained very high at 98% during 2017. Panzhuang's gross sales volume in 2017 increased by 13% to 559.7 MMCM (19.8 bcf), compared with the full year 2016 gross sales volume of 495.5MMCM (17.5 bcf). Further details on production and well count of Panzhuang are set out below in Table 1.

- **Panzhuang drilling and surface facilities**

  In 2017, AAG drilled and completed 55 wells (comprising 45 SLHs and 10 PDWs). For the full year 2017, the 45 SLH wells were completed in just 16.9 days on average with an average drilling cost of RMB2.9 million per SLH well compared with a 2016 average of RMB3.8 million per SLH well, with wells drilled in 22 days. Our original 2017 drilling plan of 29 wells for Panzhuang was completed by the third quarter of 2017. Savings from drilling operation and improved operation efficiency allowed us to increase the number of wells drilled in 2017.

  We added 2 additional surface compressors at the central station which will allow us to expand gas sales market at a higher pressure, thereby giving us a higher price for gas in the future. The 2017 average daily production was 1.57 MMCMD. With such a high daily production average, Panzhuang will remain the most productive CBM concession in China for years to come. At the end of 2017, there were a total of 147 wells contributing to production. Of these 147 wells, there are 19 PDWs, 49 multi-lateral wells ("**MLD**"), and 79 SLH wells.

  The current processing capacity of our Panzhuang surface facilities is about 2.45 MMCMD, with 5 gas gathering stations, 18 wellhead compressors, 55.4 km of trunk links and 90 km of single well pipelines completed. We are in the process of upgrading our central gathering station and adding a new 35KV transformer station, which will further improve surface compression capacity to increase gas production and sales.

- **Mabi Concession**

  AAG's Mabi concession in partnership with PetroChina is the leading development stage CBM gas project in China designated under the Energy Plan. In 2017, Mabi focused on improving pilot performance, initiating cost control and preparing for the commercial development after Overall Development Plan approval is received.

- **Mabi gas sales contract signed — revenue recognition started**

  As stated in the 2017 Interim Report published on 24 August 2017 ("**2017 Interim Report**"), on 1 July 2017, AAG entered into an exploration phase gas sales agreement with PetroChina, which sets out the terms of exploration phase gas sales of Mabi concession during the exploration period. In summary, this pilot sales agreement allows Mabi to sell up to 500 thousand cubic meters per day ("**MCMD**") of gas to the PetroChina West East pipeline 1. Similar to our Panzhuang concession, Mabi pilot sales also qualifies for the RMB0.30/cm subsidy and the Value Added Tax ("**VAT**") refund. We are very excited with this development since we have commenced revenue recognition for Mabi with effect from 2H2017, and we have commenced recovering our cost and delivering value to our shareholders.

  The sales utilization rate in Mabi increased to 92% after the additional power grid project finished in the first half of 2017 ("**1H2017**"). Mabi's gross pilot sales volume in 2017 increased by 151% to 53.6 MMCM (1.9 bcf). Further details on production and well count of Mabi are set out below in Table 1.

- **Mabi pilot program update**

  AAG's Mabi concession showed promising success in 2017. Mabi's 2017 gross pilot production increased to 58.3 MMCM (2.1 bcf) compared with 35.0 MMCM (1.2 bcf) in 2016. The 2017 average daily production for Mabi was 160.0 MCMD, a 68% increase compared to 95.5 MCMD in 2016.

  We have drilled 67 wells and hydraulic fractured 56 wells in 2017. The average cost of these 67 wells for drilling and completion are approximately 30% and 25% lower respectively compared to similar type well's historical average cost. By the end of 2017, there are 127 wells at various stages of pilot production in Mabi. A combination of low cost PDW with well casing and hydraulic fracture completion will allow for one well to access multiple coal seams with the lowest investment. Based on the recent success of Mabi pilot production improvement and development optimization, the Mabi concession is ready for scaled commercial development.

- **Mabi ODP progress**

  All Overall Development Plan Phase I ("**ODP I**") associated sub-approvals have been secured. The ODP I report had been further revised based on the improved well performance and market condition, and passed final review by our project partner China National Petroleum Corporation ("**CNPC**"). According to the announcement published by the State Council in early 2017, to simplify the regulatory approval procedures and facilitate the CBM commercialization process, Sino-foreign CBM ODPs will no longer require approval from NDRC, but instead will be replaced by a project filing process. We expect this filing process to be in place in 1H2018 which will allow Mabi to start the scaled development of ODP I in the middle of 2018.

Table 1 — Operation matrix of Panzhuang ("PZ") and Mabi ("MB") concessions	**2017 Total**	2016 Total	% Change
Total gross production (MMCM)	**629.84**	541.08	16.40%
Total average daily production (MMCMD)	**1.72**	1.48	16.88%
Panzhuang (PZ) gross production (MMCM)	**571.56**	506.13	12.93%
PZ MLD	**340.87**	447.95	-23.91%
PZ SLH	**205.67**	45.67	350.34%
PZ PDW	**25.02**	12.50	100.18%
Total PZ producing wells**	**147**	97	51.55%
PZ MLD	**49**	49	0.00%
PZ SLH	**79**	34	132.35%
PZ PDW	**19**	14	35.71%
PZ wells drilled	**55**	30	83.33%
PZ wells fracked	**6**	6	28.57%
Mabi (MB) gross production (MMCM)	**58.28**	34.95	66.77%
MB MLD	**0.11**	0.19	-40.78%
MB SLH	**23.76**	3.08	671.29%
MB PDW	**34.42**	31.69	8.61%
Total Mabi producing wells*	**127**	121	79.34%
MB MLD	**1**	2	-50.00%
MB SLH	**10**	12	-16.67%
MB PDW	**116**	107	8.41%
MB wells drilled	**67**	8	737.50%
MB wells fracked	**56**	31	80.65%

* Operations update as of 31 December 2017, 08:00 CST

** well count is calculated from pumping start date

EXPLORATION AND RESERVE UPDATE

As stated in 2017 Interim Report, the exploration focus has been gradually moving towards field development preparation. The Group is pleased that both the Panzhuang and the Mabi concession have both gone through major exploration and appraisal programs and achieved reasonable resources assessment.

Based on reports issued by Netherland Sewell & Associates Inc. ("**NSAI**"), an independent reserve certification company, the Group's net 1P and 2P natural gas reserves as at 2017 year end ("**2017YE**") are 153.0 bcf and 617.6 bcf respectively, which represents an 43% increase over the net 1P of 107.2 bcf at 2016YE, and a 12% decrease from the net 2P of 697.8 bcf at 2016 year end ("**2016YE**").

The Panzhuang concession contributed a net 1P of 111.4 bcf and a net 2P of 190.9 bcf. Both net 1P and 2P increased from 2016YE (when taking into account gas production volume in 2017) due to good performance of existing wells and the accelerated drilling program in 2017. This shows our commitment to developing Panzhuang above its original designed capacity of 17.5 bcf per year. The increased 2P reserves will further contribute to future production in Panzhuang.

The Mabi concession contributed a net 1P of 41.6 bcf, or an 329% increase over the net 1P of 9.7 bcf at 2016YE which benefited from existing wells' performance, new wells coming online and implementation of exploration phase gas sales contract in Mabi in 2017. An optimized Long Range Plan ("**LRP**") with high-graded development strategy was developed in 2017 for delivering stronger economics based on an assessment of the Mabi gas field. This resulted in a small reduction in Mabi's net 2P reserves (15%). The original plan of developing possible reserve will not be developed based on the revised LRP. This results in decreased possible reserves. The portion of reduced net possible reserves are reclassified as contingent resources pending on economics and technology viability.

The following table sets forth our reserve data as of 31 December 2017 compared with 2016:

Table 2

Reserve Data**	**2017 Gross** (bcf)	**Net**(*)(**) (bcf)	**2016 Net**(*)(**) (bcf)
Total			
Proved (1P)	190.6	153.0	107.2
Proved + probable (2P)	858.8	617.6	697.8
Proved + probable + possible (3P)	1,159.9	822.2	1,525
Panzhuang			
Proved (1P)	142.5	111.4	97.5
Proved + probable (2P)	245.6	190.9	197.3
Proved + probable + possible (3P)	305.5	236.5	264.8
Mabi			
Proved (1P)	48.1	41.6	9.7
Proved + probable (2P)	613.2	426.8	500.5
Proved + probable + possible (3P)	854.4	585.6	1,260.2

Notes:

* Net gas reserves are our share of the gas reserves according to the terms of each production sharing contract and after adjustment for fuel and shrinkage.

** Our reserve estimates and the future net revenue have been prepared by NSAI in accordance with generally accepted petroleum engineering and evaluation principles set forth in the Standards Pertaining to the Estimating and Auditing of Oil and Gas Reserves Information promulgated by the Society of Petroleum Engineers. NSAI used standard engineering and geosciences methods or a combination of methods, including performance analysis, volumetric analysis, and analogy, that it considered to be appropriate and necessary to classify, categorize, and estimate volumes in accordance with the 2007 PRMS (the Petroleum Resources Management System published by the Society of Petroleum Engineers, American Association of Petroleum Geologists, World Petroleum Council, and Society of Petroleum Evaluation Engineers in March 2007) definitions and guidelines. These reserve amounts are estimates only and should not be construed as exact quantities.

NEW OPPORTUNITIES

The Group has been actively pursuing new oil & gas opportunities for future growth, mainly covering attractive oil & gas assets inside and outside China. In 2017, AAG's M&A team screened numerous deals and progressed several deals to advanced stage of negotiations. We believe AAG is well positioned for further expansion in the near term, and are very excited about prospects in 2018.

OUTLOOK AND GUIDANCE FOR 2018

China's total gas demand was up 16% YoY to 241 billion cubic meters ("**bcm**") for the full year 2017, according to SIA Energy, an independent China-focused oil and gas consulting firm, owing to the coal-to-gas conversion program which substantially increased gas demand in 2017 as the PRC Government encourages coal users to switch to gas. Domestic gas supply, on the other hand, only increased 10% to 150 bcm, which shows the strong supply and demand imbalance. It is the Company's belief that gas use promotion policy and environmental protection will become resilient growth drivers in the medium and long term.

As published in the 13th Five Year Plan, the PRC government is committed to establishing the right incentives and market drivers for increasing gas demand by 2020, and CBM is an important part of this plan. The NEA and the NDRC took great strides from 2015 — 2017 in gas reform initiatives, including: pushing third party access to pipelines, rolling out programmes incentivizing coal to gas switching, enhancing infrastructure interconnectivity, and streamlining the hierarchy of gas transmission and distribution businesses. The NEA will take further steps in 2018 to incentivize gas production and market reform. These measures will support AAG's growth aspirations beyond the leading independent producer of CBM in China.

For 2018, the Group will continue making investments in Panzhuang and Mabi as follows:

- **Panzhuang:**

  The full year plan includes drilling 49 SLH and 12 PDW production wells, work overs on existing wells, and minor hydraulic refracture works. Surface facilities investments will include the continuation of the central station upgrade, further power station construction, and related trunk line construction for future development.

  The Group's full year gross production expectation for Panzhuang is 626.0 MMCM (22.1 bcf) subject to anticipated project execution and related government approvals.

- **Mabi:**

  In Mabi, the Group will focus on execution of the ODP I implementation plan once ODP I plan receives approval. This will include both drilling new wells in core areas, infill drilling in existing development areas, and starting new gas gathering station construction. The drilling and completion technology will build off the success in recent years of low cost PDWs.

  The full year plan includes drilling approximately 198 new PDWs and hydraulic fracturing approximately 72 wells. Much work will go into surface facilities such as trunk lines, gas gathering stations, well pad preparation, and forestry and land approval.

  The Group's full year gross production expectation for Mabi is 97.3 MMCM (3.4 bcf) subject to anticipated project execution and related government approvals.

Based on the above development plan for Panzhuang and Mabi, the total capital expenditure will be approximately RMB890 million (comprising RMB320 million for Panzhuang and RMB570 million for Mabi) which will be funded by internal cashflows, a portion of proceeds from the IPO and/or the unutilized portion of the reserve-based lending facility. Mabi's capital expenditure of RMB570 million is based on the assumption that the Group will be responsible to fund 100% of Mabi's capital expenditure for 2018. However, the Group expects that PetroChina will fund 30% of Mabi's capital expenditure for 2018 and onwards once Mabi's ODP I filing is completed (which is expected to be completed in 2018), and the Group's share of Mabi's capital expenditure for 2018 will drop from RMB570 million to RMB410 million. The Group will re-assess the capital expenditure plan for 2018 and disclose any changes in the 2018 interim results if any adjustments are necessary.

The Group is confident that we will continue to control costs and maximize profits. As a high productivity and low-cost upstream gas producer with a strong balance sheet, we are well positioned to further expand our production in Panzhuang and commercial development in Mabi to satisfy China's growing energy demand. At the same time, the Group will continue to pursue new oil & gas business opportunities within China and in other regional markets to expand our business, serve adjacent communities with clean energy, and realize further return to our shareholders.

FINANCIAL RESULTS

The Board is pleased to announce the audited consolidated financial results of the Group for the year ended 31 December 2017 together with the comparative figures for the previous year as follows:

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

		Year ended 31 December	
		2017	2016
	Note	***RMB'000***	*RMB'000*
Revenue	*4*	**541,598**	411,278
Other income	*5*	**193,913**	149,276
Other losses, net		**(83)**	(913)
Operating expenses			
Depreciation and amortisation		**(110,419)**	(74,613)
Employee benefit expenses		**(142,130)**	(164,142)
Materials, services and logistics		**(134,686)**	(100,203)
Others		**(26,071)**	(23,543)
Total operating expenses		**(413,306)**	(362,501)
Profit from operations		**322,122**	197,140
Interest income	*6*	**6,306**	10,699
Finance costs	*6*	**(12,977)**	(18,578)
Exchange losses	*6*	**(4,510)**	(10,281)
Finance costs, net		**(11,181)**	(18,160)
Profit before income tax		**310,941**	178,980
Income tax expense	*7*	**(127,743)**	(72,345)
Profit attributable to owners of the Company for the year		**183,198**	106,635
Other comprehensive income:			
Items that may be reclassified subsequently to profit or loss			
Currency translation differences		**(90,363)**	90,613
Total comprehensive income attributable to owners of the Company for the year		**92,835**	197,248
Earnings per share (RMB)			
— Basic	*11*	**0.055**	0.032
— Diluted	*11*	**0.055**	0.032

CONSOLIDATED BALANCE SHEET

	Note	As at 31 December 2017 RMB'000	2016 RMB'000
ASSETS			
Non-current assets			
Property, plant and equipment		**3,504,437**	3,188,674
Land use rights		**11,982**	12,265
Intangible assets		**39,832**	33,907
Other non-current assets		**1,434**	4,116
		3,557,685	3,238,962
Current assets			
Inventories		**2,444**	1,760
Trade and other receivables	*8*	**297,927**	319,850
Current income tax prepaid		**–**	2,555
Restricted bank deposits		**37,663**	31,583
Cash and cash equivalents		**2,236,970**	2,343,764
		2,575,004	2,699,512
Total assets		**6,132,689**	5,938,474
EQUITY			
Equity attributable to owners of the Company			
Share capital		**2,041**	2,034
Capital surplus		**4,769,340**	4,839,134
Retained earnings/(Accumulated deficits)		**178,964**	(4,234)
Total equity		**4,950,345**	4,836,934
LIABILITIES			
Non-current liabilities			
Asset retirement obligations		**14,609**	13,176
Borrowings	*9*	**513,593**	496,376
Deferred income tax liabilities		**232,080**	148,213
		760,282	657,765
Current liabilities			
Trade and other payables	*10*	**396,953**	443,775
Current income tax liabilities		**25,109**	–
		422,062	443,775
Total liabilities		**1,182,344**	1,101,540
Total equity and liabilities		**6,132,689**	5,938,474

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

1. GENERAL INFORMATION

AAG Energy Holdings Limited (the "**Company**") and its subsidiaries (together, the "**Group**") are principally engaged in exploration, development and production of coalbed methane ("**CBM**") in the People's Republic of China (the "**PRC**"). The Company is an exempted company incorporated in the Cayman Islands with limited liability on 23 December 2014. The address of the Company's registered office is P.O.Box 31119, Grand Pavilion, Hibiscus Way, 802 West Bay Road, Grand Cayman, KY1-1205, Cayman Islands.

The Group conducts its business through two production sharing contracts ("**PSC**") entered into with China United Coalbed Methane Corporation Ltd. ("**CUCBM**") and PetroChina Company Limited ("**PetroChina**") for the Panzhuang and Mabi concessions respectively in Shanxi Province of the PRC.

The Overall Development Plan ("**ODP**") of the Panzhuang concession was approved by the National Development and Reform Commission of the PRC on 28 November 2011, which allowed the Panzhuang concession to enter into the commercial development phase. On 1 November 2016, Panzhuang concession entered into production phase after the Joint Management Committee ("**JMC**") approved and announced based on the terms of Panzhuang PSC. Asian American Gas Inc. ("**AAGI**") and PetroChina entered into exploration phase sales contract with effect from 1 July 2017. As at 31 December 2017, Mabi concession was still in exploration phase.

The Company's initial public offering ("**IPO**") of its shares on the Main Board of the Stock Exchange of Hong Kong Limited was completed on 23 June 2015.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The principal accounting policies applied in the preparation of these consolidated financial statements are set out below. These policies have been consistently applied to all the years presented, unless otherwise stated.

Basis of preparation

The consolidated financial statements of the Group have been prepared in accordance with all applicable Hong Kong Financial Reporting Standards ("**HKFRS**") and requirements of the Hong Kong Companies ordinance Cap.622. The consolidated financial statements have been prepared under the historical cost convention.

The consolidated financial statements are presented in Renminbi ("**RMB**") unless otherwise stated.

The preparation of the financial statements in conformity with HKFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgement in the process of applying the Group's accounting policies.

Changes in accounting policy and disclosures

(a) New and amended standards adopted by the Group

The Group has applied the following standards and amendments for the first time for their annual reporting period commencing 1 January 2017:

- *Recognition of Deferred Tax Assets for Unrealised Losses — Amendments to HKAS 12*; and

- *Disclosure initiative — amendments to HKAS 7*.

The amendments to HKAS 7 require disclosure of changes in liabilities arising from financing activities.

(b) New standards and interpretations not yet adopted

Certain new accounting standards and interpretations have been published that are not mandatory for 31 December 2017 reporting periods and have not been early adopted by the Group. The Group's assessment of the impact of these new standards and interpretations is set out below.

(i) HKFRS 9 Financial instruments

Nature of change

HKFRS 9 addresses the classification, measurement and derecognition of financial assets and financial liabilities, introduces new rules for hedge accounting and a new impairment model for financial assets.

Impact

HKFRS 9 retains but simplifies the mixed measurement model and establishes three primary measurement categories for financial assets: amortised cost, fair value through other comprehensive income ("**FVOCI**") and fair value through profit or loss. The basis of classification depends on the entity's business model and the contractual cash flow characteristics of the financial assets. Investments in equity instruments are required to be measured at fair value through profit or loss with the irrevocable option at inception to present changes in fair value in OCI not recycling. The Group does not expect the new guidance to have an impact on the classification and measurement of its financial assets since the Group does not have any debt instruments and equity investments.

There will be no impact on the Group's accounting for financial liabilities, as the new requirements only affect the accounting for financial liabilities that are designated at fair value through profit or loss and the Group does not have any such liabilities. The derecognition rules have been transferred from HKAS 39 Financial Instruments: Recognition and Measurement and have not been changed.

The new impairment model requires the recognition of impairment provisions based on expected credit losses rather than only incurred credit losses as is the case under HKAS 39. It applies to financial assets classified at amortised cost, debt instruments measured at FVOCI, contract assets under HKFRS 15 Revenue from Contracts with Customers, lease receivables, loan commitments and certain financial guarantee contracts. The Group has assessed the new impairment model and is expecting no significant impact.

Date of adoption by Group

The Group will adopt the new standard on 1 January 2018.

(ii) HKFRS 15 Revenue from contracts with customers

Nature of change

The HKICPA has issued a new standard for the recognition of revenue. This will replace HKAS 18 which covers contracts for goods and services and HKAS 11 which covers construction contracts and the related literature.

The new standard is based on the principle that revenue is recognised when control of a good or service transfers to a customer.

The standard permits either a full retrospective or a modified retrospective approach for the adoption.

Impact

Management has assessed the effects of applying the new standard on the Group's financial statements and has identified no significant impact.

Date of adoption by group

The Group will adopt the new standard on 1 January 2018.

(iii) HKFRS 16 Leases

Nature of change

HKFRS 16 was issued in January 2016. It will result in almost all leases being recognised on the balance sheet, as the distinction between operating and finance leases is removed. Under the new standard, an asset (the right to use the leased item) and a financial liability to pay rentals are recognised. The only exceptions are short-term and low-value leases.

The accounting for lessors will not change significantly.

Impact

The standard will affect primarily the accounting for the Group's operating leases. As at the reporting date, the Group has non-cancellable operating lease commitments of RMB7,552,000. The Group estimates that approximately 0.32% of these relate to payments for short-term and low value leases which will be recognised on a straight-line basis as an expense in profit or loss.

However, the Group has not yet assessed what other adjustments, if any, are necessary for example because of the change in the definition of the lease term and the different treatment of variable lease payments and of extension and termination options. It is therefore not yet possible to estimate the amount of right-of-use assets and lease liabilities that will have to be recognised on adoption of the new standard and how this may affect the Group's profit or loss and classification of cash flows going forward.

Mandatory application date/Date of adoption by Group

Mandatory for financial years commencing on or after 1 January 2019. At this stage, the Group does not intend to adopt the standard before its effective date. The Group intends to apply the simplified transition approach and will not restate comparative amounts for the year prior to first adoption.

There are no other standards that are not yet effective and that would be expected to have a material impact on the entity in the current or future reporting periods and on foreseeable future transactions.

3. SEGMENT INFORMATION

The chief operating decision-maker ("**CODM**") has been identified as the directors and chief executive of the Company who review the Group's internal reporting in order to assess performance and allocate resources. The CODM has determined the operating segments based on these reports.

The Group's operating segments are defined by PSCs, which is the basis by which the CODM makes decisions about resources to be allocated and assesses their performance. The financial information of the two PSCs have been separated to present segment information to be reviewed by the CODM.

The measurement of results and assets of the operating segments are the same as those described in the summary of significant accounting policies. The CODM evaluates the performance of the operating segments of the PSCs based on profit before income tax, depreciation and amortisation, interest income, finance costs and exchange losses ("**EBITDA**").

The segment information provided to the CODM for the reportable segments for the year ended 31 December 2017 is as follows:

	Panzhuang concession *RMB'000*	**Mabi concession** *RMB'000*	**Total** *RMB'000*
For the year ended 31 December 2017			
Revenue from external customers	**512,886**	**28,712**	**541,598**
EBITDA	**552,844**	**(26,889)**	**525,955**
Other income	**180,170**	**13,743**	**193,913**
Operating expenses	**(231,281)**	**(84,760)**	**(316,041)**
Depreciation and amortisation	**(90,993)**	**(15,375)**	**(106,368)**
Interest income	**4,613**	**211**	**4,824**
Finance costs	**(2,065)**	**(123)**	**(2,188)**
Exchange (losses)/gains	**(9,726)**	**17,074**	**7,348**
Income tax expense	**(127,736)**	**–**	**(127,736)**
For the year ended 31 December 2016			
Revenue from external customers	411,278	–	411,278
EBITDA	441,628	(45,075)	396,553
Other income	149,276	–	149,276
Operating expenses	(184,449)	(50,135)	(234,584)
Depreciation and amortisation	(65,906)	(5,589)	(71,495)
Interest income	8,933	113	9,046
Finance costs	(2,654)	(61)	(2,715)
Exchange (losses)/gains	(13,262)	3,782	(9,480)
Income tax expense	(72,345)	–	(72,345)

	Panzhuang concession *RMB'000*	**Mabi concession** *RMB'000*	**Total** *RMB'000*
As at 31 December 2017			
Total assets	**2,141,264**	**2,282,764**	**4,424,028**
Total liabilities	**507,976**	**145,908**	**653,884**
Additions to non-current assets (other than deferred tax assets)	**163,208**	**157,108**	**320,316**
As at 31 December 2016			
Total assets	2,344,636	1,991,940	4,336,576
Total liabilities	400,879	189,622	590,501
Additions to non-current assets (other than deferred tax assets)	234,448	336,837	571,285

A reconciliation of EBITDA to total profit before income tax is provided as follows:

	Year ended 31 December	
	2017	2016
	RMB'000	*RMB'000*
Total EBITDA for reportable segments	**525,955**	396,553
Headquarter overheads	**(93,414)**	(124,800)
Depreciation and amortisation	**(110,419)**	(74,613)
Interest income	**6,306**	10,699
Finance costs	**(12,977)**	(18,578)
Exchange losses	**(4,510)**	(10,281)
Profit before income tax	**310,941**	178,980

Reportable segments' assets are reconciled to total assets as follows:

	As at 31 December	
	2017	2016
	RMB'000	*RMB'000*
Total segment assets	**4,424,028**	4,336,576
Unallocated		
Unallocated cash and cash equivalents	**1,703,240**	1,594,604
Others	**5,421**	7,294
Total assets per balance sheet	**6,132,689**	5,938,474

Reportable segments' liabilities are reconciled to total liabilities as follows:

	As at 31 December	
	2017	2016
	RMB'000	*RMB'000*
Total segment liabilities	**653,884**	590,501
Unallocated		
Unallocated long term borrowings	**513,593**	496,376
Others	**14,867**	14,663
Total liabilities per balance sheet	**1,182,344**	1,101,540

4. REVENUE

For the years ended 31 December 2017 and 2016, all the Group's revenue is derived from the sale of the Group's share of CBM sold to customers in the PRC.

5. OTHER INCOME

	Year ended 31 December	
	2017	2016
	RMB'000	*RMB'000*
VAT refund (a)	**50,063**	29,456
Government subsidy (b)	**143,850**	119,820
	193,913	149,276

(a) VAT refund is granted by the PRC government according to "The Notice on Tax Policy Issued by The Ministry of Finance and The State Administration of Taxation on Speeding Up The Drainage of Coalbed Methane" (《財政部國家稅務總局關於加快煤層氣抽採有關稅收政策問題的通知》). CUCBM and PetroChina applies for the VAT refund for Panzhuang and Mabi concession, respectively. The Group recognises its entitlement based on the Group's share of CBM sold and when there is reasonable assurance that the amount will be received.

(b) Government subsidy is granted by the PRC government according to "The Implementation Opinions of Subsidies Granted by The Ministry of Finance on The Development and Utilisation of Coalbed Methane" (《財政部關於煤層氣(瓦斯)開發利用補貼的實施意見》) at RMB0.3/cm of the CBM sold. CUCBM and PetroChina applies for the subsidy for Panzhuang and Mabi concession, respectively. The Group recognises its entitlement based on the Group's share of CBM sold and when there is reasonable assurance that the amount will be received.

6. FINANCE COSTS, NET

	Year ended 31 December	
	2017	2016
	RMB'000	RMB'000
Interest expense of bank borrowings	**(39,176)**	(33,369)
Bank loan commitment fee	**(12,577)**	(18,236)
Accretion expenses of asset retirement obligations	**(400)**	(342)
Subtotal	**(52,153)**	(51,947)
Less: amounts capitalised on qualifying assets	**39,176**	33,369
Finance costs	**(12,977)**	(18,578)
Interest income	**6,306**	10,699
Exchange losses	**(4,510)**	(10,281)
Finance costs, net	**(11,181)**	(18,160)

7. INCOME TAX EXPENSE

	Year ended 31 December	
	2017	2016
	RMB'000	*RMB'000*
Current income tax	**(43,876)**	(290)
Deferred income tax	**(83,867)**	(72,055)
	(127,743)	(72,345)

The Company was incorporated in the Cayman Islands as an exempt company with limited liability and, accordingly, is exempted from payment of local income tax.

No provision for Hong Kong profits tax has been provided as the Group did not derive any assessable profits in Hong Kong during the year.

AAGI and AAG Energy (China) Limited, which were incorporated in the British Virgin Islands under the International Business Companies Acts of the British Virgin Islands, are exempted from payment of local income tax.

SAEI, which was incorporated in Samoa under the International Business Companies Acts of the Samoa, is exempted from payment of local income tax.

Corporate income tax in the PRC is calculated based on the taxable profit of branches established in the PRC. According to the PRC Corporate Income Tax Law promulgated by the PRC government, the tax rate applicable for the PRC branches of the Group's subsidiaries is 25%.

The tax on the Group's profit before income tax differs from the theoretical amount that would arise using the statutory tax rate as follows:

	Year ended 31 December	
	2017	2016
	RMB'000	*RMB'000*
Profit before income tax	**310,941**	178,980
Tax expense calculated at applicable statutory tax rates	**(146,350)**	(22,859)
Utilization of previously/(current period) deductible temporary differences for which no deferred tax asset was recognised	**22,848**	(47,229)
Expenses not deductible for taxation purposes	**(1,812)**	(1,967)
Others	**(2,429)**	(290)
Income tax expense	**(127,743)**	(72,345)

8. TRADE AND OTHER RECEIVABLES

	As at 31 December	
	2017	2016
	RMB'000	*RMB'000*
Trade receivables (a)		
— CUCBM (i)	**10,769**	32,948
— PetroChina (ii)	**10,503**	–
— External customers (iii)	**80,008**	20,061
Notes receivable (b)	**32,600**	119,567
Government grants receivables (c)		
— Government	**70,084**	43,102
— CUCBM	**20,938**	42,620
— PetroChina	**4,432**	–
Due from CUCBM for cash calls and accrued expenses (d)	**54,642**	40,631
Prepaid expenses, deposits and others	**21,148**	28,118
	305,124	327,047
Less: provision for impairment	**(7,197)**	(7,197)
	297,927	319,850

(a) Trade receivables

(i) The ageing analysis of trade receivables — due from CUCBM:

	As at 31 December	
	2017	2016
	RMB'000	*RMB'000*
Within 3 months	**10,769**	32,948

Note: Trade receivables due from CUCBM represent the cash collected from external customers attributable to Sino-American Energy, Inc. ("**SAEI**") and deposited into CUCBM's bank account on behalf of the Group, which is jointly managed by CUCBM and the SAEI.

(ii) The ageing analysis of trade receivables — due from PetroChina:

	As at 31 December	
	2017	2016
	RMB'000	*RMB'000*
Within 3 months	**10,503**	–

(iii) The ageing analysis of trade receivables — due from external customers

	As at 31 December	
	2017	2016
	RMB'000	*RMB'000*
Within 3 months	**46,242**	12,864
3 months to 6 months	**20,510**	–
6 months to 1 year	**6,059**	–
Over 3 years	**7,197**	7,197
	80,008	20,061
Provision	**(7,197)**	(7,197)
	72,811	12,864

	As at 31 December	
	2017	2016
Past due but not impaired	***RMB'000***	*RMB'000*
Within 3 months	**46,242**	12,864
3 months to 6 months	**20,510**	–
6 months to 1 year	**6,059**	–
	72,811	12,864

These relate to a number of independent customers for whom there is no significant financial difficulty and based on past experience, the overdue amounts can be recovered.

The trade receivables are due upon billing.

(iv) Movement of bad debt provision:

	Year ended 31 December	
	2017	2016
	RMB'000	*RMB'000*
Beginning and end of the year	**7,197**	7,197

(b) Notes receivable are bank acceptance with maturity dates within six months.

(c) This represents the VAT refund and government subsidies for CBM receivable from the government through CUCBM and PetroChina.

(d) This represents CUCBM's share of the cash calls and accrued expenses for the development costs of Panzhuang concession yet to be received from CUCBM.

(e) As at 31 December 2017, the carrying amounts of trade and other receivables approximated their fair values.

(f) The carrying amounts of the Group's trade and other receivables (excluding prepayments) are denominated in the following currencies:

	As at 31 December	
	2017	2016
	RMB'000	*RMB'000*
RMB	**282,967**	298,378
HK$	**630**	723
US$	**–**	17
	283,597	299,118

9. BORROWINGS

	As at 31 December	
	2017	2016
	RMB'000	*RMB'000*
Bank loans, secured		
Between 2 and 5 years	**513,593**	496,376
	513,593	496,376
Annual interest rate	**LIBOR+4.15%**	LIBOR+4.15%
Annual effective interest rate	**7.15%**	6.79%

As at 31 December 2017 and 2016, the Group's borrowings were all denominated in US$, which were drawn down by SAEI. On 8 July 2015, SAEI as borrower entered into an up to US$250 million senior secured revolving credit facility with AAGI as guarantor, and with AAGI's shares in SAEI mortgaged as security, for a term of 69 months with a final maturity date of 31 March 2021 bearing interest at LIBOR plus a margin of 4.15% for the first 4 years and 4.65% for the remainder of the facility.

Movements in borrowings are analysed as follows:

	RMB'000
Year ended 31 December 2017	
Opening balance as at 1 January 2017	**496,376**
Addition	**39,687**
Amortisation of financing costs	**7,087**
Currency translation differences	**(29,557)**
Closing balance as at 31 December 2017	**513,593**
Year ended 31 December 2016	
Opening balance as at 1 January 2016	418,859
Addition	40,438
Amortisation of financing costs	6,956
Currency translation differences	30,123
Closing balance as at 31 December 2016	496,376

The Group has the following undrawn borrowing facilities:

	As at 31 December	
	2017	2016
	USD'000	*USD'000*
Expiring beyond 1 year	**118,000**	174,000

The US$250 million borrowing facility commenced reduction of the maximum borrowing facility amount on 1 July 2017 and will continue reducing every six months until the maximum borrowing facility reduces to zero. As of 1 January 2018, the maximum borrowing facility amount was reduced to US$175 million, and accordingly, the undrawn borrowing facility amount as at that date was reduced to US$93 million.

Under the terms of the borrowing facilities, the Group is required to comply with the following financial covenant: the ratio of net debt to net assets must be not more than 67%. The Group has complied with this covenant throughout the reporting period. As at 31 December 2017, the balance of cash and cash equivalents exceeds the balance of bank borrowings.

As at 31 December 2017, the fair value of borrowings approximated to RMB514 million (31 December 2016: RMB496 million). The fair value is within level 2 hierarchy.

10. TRADE AND OTHER PAYABLES

	As at 31 December	
	2017	2016
	RMB'000	*RMB'000*
Trade payables	**350,956**	393,198
Amounts due to related parties		
— CUCBM	**1,000**	1,000
— PetroChina	**9,243**	8,852
Social securities and other payables	**35,754**	40,725
	396,953	443,775

(a) The ageing analysis of trade payables were as follows:

At 31 December 2017, the ageing analysis of the trade payables based on invoice date were as follows:

	As at 31 December	
	2017	2016
	RMB'000	*RMB'000*
Within 6 months	**205,987**	322,202
6 months to 1 year	**59,960**	18,700
1 to 2 years	**56,339**	29,895
2 to 3 years	**12,205**	16,480
Over 3 years	**16,465**	5,921
	350,956	393,198

(b) As at 31 December 2017, the carrying amounts of trade and other payables approximated their fair values.

(c) The carrying amounts of the Group's trade and other payables are denominated in the following currencies:

	As at 31 December	
	2017	2016
	RMB'000	*RMB'000*
RMB	**383,438**	430,811
HK$	**3,182**	286
US$	**10,333**	12,678
	396,953	443,775

11. EARNINGS PER SHARE

(a) Basic

The basic earnings per share is calculated by dividing the profit attributable to owners of the Company by the weighted average number of ordinary shares in issue during the years ended 31 December 2017 and 2016.

	Year ended 31 December	
	2017	2016
Profit attributable to owners of the Company *(RMB'000)*	**183,198**	106,635
Weighted average number of ordinary basic shares in issue *(Thousands)*	**3,333,675**	3,326,780
Basic earnings per share *(RMB)*	**0.055**	0.032

(b) Diluted

Diluted earnings per share is calculated by adjusting the weighted average number of ordinary shares outstanding to assume conversion of all dilutive potential ordinary shares. The Company has share options and RSUs outstanding which are potentially dilutive. The assumed proceeds from conversion of these options and RSUs shall be regarded as having been received from the issue of ordinary shares at the average market price of ordinary shares during the period. The difference between the number of shares that would have been issued assuming the exercise of the share options and RSUs and the number of shares that could have been issued at the average market price of the ordinary shares during the period with the same total assumed proceeds is the number of shares issued for no consideration. The resulting number of shares issued for no consideration is included in the weighted average number of ordinary shares as the denominator for calculating diluted earnings per share.

	Year ended 31 December	
	2017	2016
Profit attributable to owners of the Company *(RMB'000)*	**183,198**	106,635
Weighted average number of ordinary shares in issue *(Thousands)*	**3,333,675**	3,326,780
Adjustments for assumed conversion of share options and RSUs *(Thousands)*	**8,570**	13,538
Weighted average number of ordinary shares for diluted earnings per share *(Thousands)*	**3,342,245**	3,340,318
Diluted earnings per share *(RMB)*	**0.055**	0.032

12. DIVIDENDS

A final dividend in respect of the year ended 31 December 2017 of HK$0.0248 per share will be proposed at the annual general meeting on 8 May 2018. These financial statements do not reflect this dividend payable.

REVIEW OF OPERATING RESULTS

	Year Ended 31 December	
	2017	2016
	RMB'000	*RMB'000*
Revenue	**541,598**	411,278
— Panzhuang	**512,886**	411,278
— Mabi	**28,712**	–
Subsidy income	**143,850**	119,820
— Panzhuang	**134,320**	119,820
— Mabi	**9,530**	–
VAT refund	**50,063**	29,456
— Panzhuang	**45,850**	29,456
— Mabi	**4,213**	–
Other losses, net	**(83)**	(913)
Operating expenses	***(413,306)***	*(362,501)*
Depreciation and amortization	**(110,419)**	(74,613)
Employee benefit expenses	**(142,130)**	(164,142)
Materials, services and logistics	**(134,686)**	(100,203)
Others	**(26,071)**	(23,543)
Panzhuang	***(231,281)***	*(184,449)*
Depreciation and amortization	**(90,993)**	(65,906)
Employee benefit expenses	**(49,389)**	(46,316)
Materials, services and logistics	**(79,959)**	(60,978)
Others	**(10,940)**	(11,249)
Mabi	***(84,760)***	*(50,135)*
Depreciation and amortization	**(15,375)**	(5,589)
Employee benefit expenses	**(35,110)**	(24,896)
Materials, services and logistics	**(25,787)**	(13,249)
Others	**(8,488)**	(6,401)
Headquarters	***(97,265)***	*(127,917)*
Depreciation and amortization	**(4,051)**	(3,118)
Employee benefit expenses	**(57,631)**	(92,930)
Materials, services and logistics	**(28,940)**	(25,976)
Others	**(6,643)**	(5,893)
EBITDA	**432,541**	271,753
— Panzhuang	**552,844**	441,628
— Mabi	**(26,889)**	(45,075)
Profit from operations	**322,122**	197,140
Interest income	**6,306**	10,699
Finance costs	**(12,977)**	(18,578)
Exchange losses	**(4,510)**	(10,281)
Finance costs — net	**(11,181)**	(18,160)
Profit before income tax	**310,941**	178,980
Income tax expense	**(127,743)**	(72,345)
Profit for the year	**183,198**	106,635

Revenue. Our revenue increased by RMB130.3 million, or 31.7%, from RMB411.3 million in 2016 to RMB541.6 million in 2017. This increase was mainly generated by Panzhuang due to an increase in net sales volume as a result of increased production and an increase in the ASP to RMB1.31/cm for 2017. Panzhuang's gross production increased by 13% from 506.1 cubic meters (17.9 bcf) in 2016 to 571.6 cubic meters (20.2 bcf) in 2017, with a constant utilization rate of 98% for both 2016 and 2017. Panzhuang's ASP for 2017 increased to RMB1.31/cm compared to RMB1.20/cm for 2016 due to increased demand from the government's policy to switch from coal to gas and market conditions during the winter months. In addition, with the signing of the Mabi exploration phase sales contract with effect from 1 July 2017, Mabi began to recognize revenue and related operating expenses starting from 1 July 2017.

Set out below are the production, sales, ASP and revenue of the Group.

	Year ended 31 December	
	2017	2016
Gross production volume (bcf)[1]	**22.3**	19.1
Panzhuang	***20.2***	*17.9*
Mabi	***2.1***	*1.2*
Gross production volume (mmcm)[1]	**629.9**	541.1
Panzhuang	***571.6***	*506.1*
Mabi	***58.3***	*35.0*
Gross sales volume (bcf)[2]	**21.7**	18.3
Panzhuang	***19.8***	*17.5*
Mabi	***1.9***	*0.8*
Gross sales volume (mmcm)[2]	**613.3**	516.9
Panzhuang	***559.7***	*495.5*
Mabi	***53.6***	*21.4*
Net sales volume (bcf)[3]	**15.3**	12.7
Panzhuang	**13.8**	*12.1*
Mabi	***1.5***	*0.6*
Net sales volume (mmcm)[3]	**433.0**	359.8
Panzhuang	***390.5***	*343.2*
Mabi	***42.5***	*16.6*
ASP		
RMB per cubic meter	**1.30**	1.20
Panzhuang	***1.31***	*1.20*
Mabi	***1.14***	*1.20*
US$ per mcf	**5.44**	5.13
Panzhuang	***5.52***	*5.13*
Mabi	***4.78***	*5.09*
Revenue (in RMB in thousands)[4]	**541,598**	411,278
Panzhuang	***512,886***	*411,278*
Mabi	***28,712***	*N/A*

Note:

1. Gross production volume is the total amount of CBM produced.

2. Gross sales volume is gross production volume less utilization loss.

3. Net sales volume is the portion of gross sales volume allocated to us under the production sharing contract and after deduction of amount sold to pay applicable VAT and local taxes.

4. After Mabi signed the exploration phase sales contract with effect from 1 July 2017, Mabi commenced revenue recognition in the Profit and Loss Statement in 2H2017. In 2016 and 1H2017, Mabi's sales was recognized by offsetting Capex/Property, Plant and Equipment per IFRS requirements.

Subsidy income. Our subsidy income is RMB119.8 million and RMB143.8 million in 2016 and 2017, respectively. Our subsidy income increased by RMB24.0 million or 20.0%, mainly due to the increased sales volume for Panzhuang. In addition, Mabi's sales volume began contributing to subsidy income.

VAT refund. Our VAT refund is RMB29.5 million and RMB50.1 million in 2016 and 2017, respectively. Our VAT refund increased by RMB20.6 million or 69.8% in 2017 mainly due to increase in ASP for Panzhuang in 2017 and an one-off adjustment in 2016 for local government's share of VAT refund with effect from 2014. In addition, Mabi began to recognize VAT refund after the signing of the exploration phase sales contract with effect from 1 July 2017.

Other losses, net. Our other losses decreased by RMB829,960 from RMB913,431 in 2016 to RMB83,471 in 2017 due to less disposition of scrap materials at a loss.

Operating expenses. Our operating expenses increased by RMB50.8 million or 14.0%, from RMB362.5 million in 2016 to RMB413.3 million in 2017 primarily due to increases in depreciation and amortization as a result of increased production wells and increases in materials, services and logistics expenses mainly due to more wells put into production and legal consulting service expenses, offset by less employee benefit expenses due to decreased share-based compensation expenses in 2017. In addition, Mabi began recognizing operating expenses in the 2H2017 as a result of entering into the exploration phase sales contract.

- *Depreciation and amortization*. Our depreciation and amortization increased by RMB35.8 million or 48.0%, from RMB74.6 million in 2016 to RMB110.4 million in 2017 due to more wells and wellhead compressors put into production as production increased in Panzhuang. In addition, Mabi began recognizing more depreciation and amortization expenses with effect from 1 July 2017 as a result of entering into the exploration phase sales contract.

- *Employee benefit expenses*. Our employee benefit expenses decreased by RMB22.0 million or 13.4%, from RMB164.1 million in 2016 to RMB142.1 million in 2017, largely due to decrease in non-cash share-based compensation expenses by RMB27.8 million and a reduction of severance and consulting fees paid to our ex-Co-CEO, but partially offset by increased employees' benefit expenses for Mabi with effect from 1 July 2017 as a result of entering into the exploration phase sales contract.

- *Materials, services and logistics*. Our materials, services and logistics expenses increased by RMB34.5 million or 34.4%, from RMB100.2 million in 2016 to RMB134.7 million in 2017, primarily due to increased electricity and other operating costs at Panzhuang associated with more wells put into production, and non-operation-related expenses for business development and legal consulting service. In addition, Mabi began recognizing more of these expenses with effect from 1 July 2017 as a result of entering into the exploration phase sales contract.

Others. Our other expenses are RMB23.5 million and RMB26.1 million in 2016 and 2017, respectively.

EBITDA. Our EBITDA increased by RMB160.7 million or 59.1%, from RMB271.8 million in 2016 to RMB432.5 million in 2017. This increase was primarily due to Panzhuang's increase in net sales volume as a result of a 13% increase in gross production, increase in ASP from RMB1.20/cm in 2016 to RMB1.31/cm in 2017, increase in subsidy income and VAT refund, decrease in headquarter's employee benefit expenses as a result of decreased non-cash share-based compensation expenses and a reduction of severance and consulting fees paid to our ex-Co-CEO, offset by increase in Panzhuang's material, services and logistic costs due to more wells put into production and non-operation-related expenses related to business development and legal consulting service in 2017. In addition, Mabi began recognizing revenue and related expenses with effect from 1 July 2017 as a result of entering into the exploration phase sales contract. In summary, higher production volume and realized ASP, combined with stringent cost controls resulted in an increase in EBITDA outperforming increase in revenues. Included in EBITDA of RMB271.8 million in 2016 are non-cash share-based compensation expenses of RMB48.3 million, non-operation-related business development/feasibility studies expenses of RMB8.3 million and severance payment of RMB4.6 million for departure of one of our Co-CEOs. Included in the EBITDA of RMB432.5 million in 2017 are non-cash share-based compensation expenses of RMB20.5 million, non-operations-related expenses for business development and legal consulting service of RMB10.4 million and one-off consulting fee of RMB1.7 million paid to our ex-Co-CEO. Panzhuang's EBITDA increased by RMB111.2 million or 25.2%, from RMB441.6 million in 2016 to RMB552.8 million in 2017. Panzhuang's EBITDA in 2017 increased primarily due to increases in production volume and ASP combined with an increase in subsidy income and VAT refund, which was partially offset by higher materials and electricity expenses as a result of additional wells. Mabi's negative EBITDA decreased by RMB18.2 million or 40.4%, from negative RMB45.1 million in 2016 to negative RMB26.9 million in 2017 because Mabi began to recognize revenue and related expenses with effect from 1 July 2017 as a result of entering into the exploration phase sales contract.

Profit from operations. As a result of the foregoing, our profit from operations increased by RMB125.0 million or 63.4%, from RMB197.1 million in 2016 to RMB322.1 million in 2017.

Interest income. Our interest income decreased by RMB4.4 million or 41.1%, from RMB10.7 million in 2016 to RMB6.3 million in 2017 primarily due to decreased cash and fixed deposit balances.

Finance costs. Our finance costs decreased by RMB5.6 million or 30.1%, from RMB18.6 million in 2016 to RMB13.0 million in 2017 largely due to decreased commitment fees resulting from reduction in the maximum reserve-based lending loan amount.

Exchange losses. Our foreign exchange translation losses decreased by RMB5.8 million or 56.3%, from RMB10.3 million in 2016 to RMB4.5 million in 2017 primarily due to exchange gain resulting from the impact of the appreciation of the Renminbi on the drawn portion of the new US$250 million reserve-based facility ("**New US$250 million RBL**"), which reduced the foreign exchange translation losses between HK$ and US$ for our cash balance in HK$.

Profit before income tax. Our profit before income tax increased by RMB131.9 million or 73.7% from RMB179.0 million in 2016 to RMB310.9 million in 2017 mainly due to the factors affecting EBITDA and decrease in foreign exchange translation losses and finance costs, but partially offset by increase in depreciation and amortization expense and reduction in interest income.

Income tax expense. Our income tax expense increased by RMB55.4 million, or 76.6%, from RMB72.3 million in 2016 to RMB127.7 million in 2017, mainly due to increase in taxable profit for Panzhuang in 2017. Income tax expense arises from Panzhuang's operations. Mabi had no income tax expense given it had no taxable profit.

Profit for the year. Our profit for the year increased by RMB76.6 million, or 71.9%, from RMB106.6 million in 2016 to RMB183.2 million in 2017, primarily due to the factors affecting profit before income tax stated above but partially offset by the increase in income tax expense.

EBITDA AND ADJUSTED EBITDA

We provide a reconciliation of EBITDA and adjusted EBITDA to profit for the year, our most directly comparable financial performance calculated and presented in accordance with HKFRS. EBITDA refers to earnings before interest income, finance costs, exchange gains/losses, income tax and depreciation and amortization. Adjusted EBITDA refers to EBITDA adjusted to exclude non-cash expenses, non-recurring items or non-operations-related expenses to show EBITDA from the Group's core operations.

We have included EBITDA and adjusted EBITDA as we believe they are financial measures commonly used in the oil and gas industry. We believe that EBITDA and adjusted EBITDA are used as supplemental financial measures by our management and by investors, research analysts, bankers and others to assess our operating performance, cash flow and return on capital as compared to those of other companies in our industry, and our ability to take on financing. However, EBITDA and adjusted EBITDA should not be considered in isolation or construed as alternatives to profit from operations or any other measure of performance or as an indicator of our operating performance or profitability. EBITDA and adjusted EBITDA fail to account for income tax, exchange gains/losses, interest income, finance costs and depreciation and amortization.

The following table presents a reconciliation of EBITDA and adjusted EBITDA to profit for the year:

	Year ended 31 December	
	2017	2016
	RMB'000	*RMB'000*
Reconciliation of profit for the year to EBITDA:		
Profit for the year	**183,198**	106,635
Income tax expense	**127,743**	72,345
Interest income	**(6,306)**	(10,699)
Finance costs	**12,977**	18,578
Exchange losses	**4,510**	10,281
Depreciation and amortization	**110,419**	74,613
EBITDA	**432,541**	271,753
Non-cash share-based compensation expenses	**20,515**	48,270
Non-operations-related business development and legal service expenses	**10,437**	8,272
Severance payment and consulting fees paid to our ex-Co-CEO	**1,709**	4,613
Adjusted EBITDA	**465,202**	332,908

Our EBITDA increased by RMB160.7 million or 59.1%, from RMB271.8 million in 2016 to RMB432.5 million in 2017. This increase was primarily due to Panzhuang's increase in net sales volume as a result of a 13% increase in gross production, increase in ASP from RMB1.20/cm in 2016 to RMB1.31/cm in 2017, increase in subsidy income and VAT refund, decrease in headquarter's employee benefit expenses as a result of decreased non-cash share-based compensation expenses and a reduction of severance payment and consulting fees paid to our ex-Co-CEO, offset by increase in Panzhuang's material, services and logistic costs due to more wells put into production and non-operation-related expenses related to business development and legal consulting service in 2017. In addition, Mabi began recognizing revenue and related expenses with effect from 1 July 2017 as a result of entering into the exploration phase sales contract. In summary, higher production volume and realized ASP, combined with stringent cost controls resulted in increase in EBITDA outperforming increase in revenues.

Our adjusted EBITDA increased by RMB132.3 million, or 39.7%, from RMB332.9 million in 2016 to RMB465.2 million in 2017. This increase was due to the reasons explained above for the increase in EBITDA adjusted for decreased non-cash share-based compensation expenses and severance payment/consulting fees paid to our ex-Co-CEO in 2017 and increased non-operations-related expenses for business development and legal consulting service included in 2017.

LIQUIDITY AND CAPITAL RESOURCES

We had cash and bank balances of RMB2,274.6 million as at 31 December 2017 (RMB2,375.3 million as at 31 December 2016).

On 8 July 2015, SAEI entered into a New US$250 million RBL with The Hongkong and Shanghai Banking Corporation Limited, Standard Chartered Bank (Hong Kong) Limited, Bank of Communication Ltd, Offshore Banking Unit and Societe Generale, Singapore Branch and on 16 July 2015, SAEI successfully drew down US$70 million from the New US$250 million RBL to prepay and replace the original US$100 million reserve-based facility.

The New US$250 million RBL commenced reduction of the maximum borrowing facility amount on 1 July 2017 and will continue reducing every six months until the maximum borrowing facility reduces to zero. As of 31 December 2017, the maximum borrowing facility amount was reduced to US$200 million. As at 31 December 2017, the unutilised portion of the New US$250 million RBL is US$118 million. On 1 January 2018, the maximum borrowing facility amount was further reduced to US$175 million, and accordingly the undrawn borrowing facility amount as at that date was further reduced to US$93 million.

As of 31 December 2016 and 2017, we had long-term borrowings of RMB496.4 million and RMB513.6 million, respectively, all of which were non-current secured U.S. dollar bank borrowings representing the drawn portion of the New US$250 million RBL as of 31 December 2016 and 2017, respectively.

Cash Flows

The table below sets forth our cash flows for each of the years indicated.

	Year ended 31 December	
	2017	2016
	RMB'000	*RMB'000*
Net cash generated from operating activities	**438,301**	257,418
Net cash used in investing activities	**(455,556)**	(337,742)
Net cash generated from financing activities	**26,392**	12,874
Net increase/(decrease) in cash and cash equivalents	**9,137**	(67,450)
Cash and cash equivalents at beginning of the year	**2,343,764**	2,309,810
Exchange (losses)/gains on cash and cash equivalents	**(115,931)**	101,404
Cash and cash equivalents at end of the year	**2,236,970**	2,343,764

Operating Activities

Net cash generated from operating activities was RMB438.3 million in 2017 largely due to profit before income tax of RMB310.9 million, depreciation and amortization of RMB110.4 million, a decrease in trade and other receivables of RMB22.3 million, non-cash share-based compensation of RMB20.5 million, finance costs of RMB13.0 million mainly for commitment fee, an increase in trade and other payables of RMB12.7 million, and unrealized exchange losses of RMB4.5 million. These were offset by RMB32.9 million of interest paid and RMB16.2 million income tax paid.

Net cash generated from operating activities was RMB257.4 million in 2016 largely due to profit before income tax of RMB179.0 million, depreciation and amortization of RMB74.6 million, non-cash share-based compensation of RMB48.3 million, finance costs of RMB18.6 million and unrealized exchange losses of RMB12.6 million, and increase in trade and other payables of RMB7.8 million. These were offset by an increase in trade and other receivables of RMB40.9 million, RMB26.3 million of interest paid, interest income of RMB10.7 million and RMB5.3 million income tax paid.

Investing Activities

Net cash used in investing activities was RMB455.6 million in 2017 and comprised mainly of purchases of property, plant and equipment of RMB456.3 million, increase in restricted bank deposits of RMB6.1 million, offset by interest received of RMB6.5 million. The purchase of property, plant and equipment primarily comprised of payment for more wells drilled, additional well head compressors and construction of gas gathering stations and power facilities.

Net cash used in investing activities was RMB337.7 million in 2016 is mainly for the purchase of property, plant and equipment of RMB570.1 million, increase in restricted bank deposits of RMB23.6 million, offset by decrease in term deposits with an initial term of over three months of RMB246.0 million and interest received of RMB9.5 million. The purchase of property, plant and equipment primarily comprised of payment for more wells drilled, additional boosters and compressors, and construction of gas gathering stations and power facilities.

Financing Activities

Net cash generated from financing activities was RMB26.4 million in 2017 largely due to RMB39.7 million of cash received from drawing down a portion of the New US$250 million RBL, offset by finance costs of RMB13.4 million largely due to payment for commitment fees paid for unutilized portion of the New US$250 million RBL.

Net cash generated from financing activities was RMB12.9 million in 2016 largely due to RMB40.4 million of cash received from drawing down a portion of the New US$250 million RBL, offset by finance costs of RMB19.9 million largely due to payment for commitment fees paid for unutilized portion of the New US$250 million RBL and payment of RMB7.7 million of IPO-related expenses.

Cash and Bank Balances

We had cash and bank balances of RMB2,375.3 million and RMB2,274.6 million as of 31 December 2016 and 2017, respectively. Our cash and bank balances consist of cash on hand, cash at banks, and restricted bank deposits. The decrease in our cash position is largely due to purchases of property, plant and equipment. As at 31 December 2016 and 2017, we had approximately 67.2% and 75.1% of our cash and bank balances held in HK$ or US$.

FINANCIAL RISK FACTORS

Our activities expose us to a variety of financial risks: credit risk, market risk (including foreign exchange risk and cash flow interest rate risk), liquidity risk and concentration risk. Our overall risk management program focuses on the unpredictability of financial markets and seeks to minimise potential adverse effects on our financial performance.

Credit Risk

As the majority of the cash at bank balances are placed with state-owned and international banks and financial institutions in the PRC and Hong Kong, and there has been no recent history of default in relation to these banks and financial institutions, the corresponding credit risk is relatively low. Therefore, our credit risk arises primarily from trade and other receivables. We have controls in place to assess the credit quality of our customers. We have concentration risk on trade receivables. Only limited allowance for uncollectible receivables was made in the past as our sales were only made to the customers with good credit history. The utilisation of credit limits is regularly monitored.

Foreign exchange risk

We are exposed to foreign exchange risk arising from various currency exposures, primarily with respect to US$. Foreign exchange risk arises when future commercial transactions or recognised assets or liabilities are denominated in a currency other than the entity's functional currency.

Prior to 30 April 2016, we were exposed to non-cash foreign exchange risk arising from retranslation of US$ denominated inter-company loans. To manage the foreign exchange risk, management decided to execute a debt restructuring on 30 April 2016 by converting the inter-company loans into perpetual loans through entering into perpetual loan agreements between respective group companies such that the perpetual loans do not bear interest and the lenders can not request repayment. Upon completion of this debt restructuring, any foreign exchange differences arising from retranslation of these US$ denominated perpetual loans are recognised in equity in the consolidated financial statements.

We manage our foreign exchange risk by closely monitoring the movement of the foreign currency rates, and by monitoring the amount of the US$ loan utilised from the US$250 million revolving credit facility, which is our only US$ borrowings from third parties.

As at 31 December 2017, if RMB had weakened/strengthened by 1% against the US$ with all other variables held constant, profit before income tax for the year would have been RMB902,000 (31 December 2016: RMB3,909,000) lower/higher, respectively, mainly as a result of foreign exchange gains/losses on translation of US$ denominated payables held by our entities with their functional currency as RMB.

Cash flow interest rate risk

Our income and operating cash flows are substantially independent of the changes in market rates. Our floating-rate bank borrowings expose us to cash flow interest rate risk. A detailed analysis of our bank borrowings, together with their respective interest rates and maturity dates are included in Note 9.

SIGNIFICANT INVESTMENT HELD

The Group did not hold any significant investments for the year ended 31 December 2017.

ACQUISITION AND DISPOSAL OF SUBSIDIARIES

The Group had no material acquisition or disposal of subsidiaries or associated companies for the year ended 31 December 2017.

SIGNIFICANT CHANGES/EVENTS AFTER THE END OF FINANCIAL YEAR

There are no other significant changes in the Group's financial position or from the information disclosed under the management discussion and analysis in this annual results announcement for the year ended 31 December 2017 or significant events occurred after the end of financial year.

EMPLOYEES

As at 31 December 2017, the Company had 643 employees, with 68 based in Beijing, 570 based in Shanxi and 5 based in Hong Kong, respectively. There have been no material changes to the information disclosed in the Company's prospectus dated 11 June 2015 (the "**Prospectus**") in respect the remuneration of employees, remuneration policies and staff development.

PRE-IPO SHARE OPTION SCHEME

The Company adopted the pre-IPO share option scheme of the Company (the "**Pre-IPO Share Option Scheme**") on 31 March 2015, a summary of principal terms (such as the purpose, the participants and the consideration for accepting and exercising any options, among others) of which is set out in the section headed "Statutory and General Information — Pre-IPO Share Option Scheme" in Appendix V to the Prospectus.

Outstanding Options

For the year ended 31 December 2017, 7,540,993 options have lapsed. 60,000 options have been exercised. As at 31 December 2017, there were a total of 223,014,280 options outstanding. If all the outstanding options are exercised, there would be a dilution effect on the share capital of the Company as at 31 December 2017 of approximately 6.68%. Save as disclosed above, no further options have been or would be granted by the Company after the date on which the Shares were listed on the Stock Exchange and from which dealing therein commenced (the "**Listing Date**") pursuant to the Pre-IPO Share Option Scheme.

POST-IPO RSU SCHEME

The Company adopted the post-IPO restricted share unit scheme of the Company (the "**Post-IPO RSU Scheme**") on 5 June 2015, which took effect on the Listing Date, a summary of principal terms (such as the purpose, the participants, among others) of which is set out in the section headed "Statutory and General Information — Post-IPO RSU Scheme" in Appendix V to the Prospectus.

On 18 December 2015, the Company offered to grant an aggregate of 41,234,696 restricted share units ("**RSUs**") to certain connected grantees and non-connected grantees of the Group in accordance with the Post-IPO RSU Scheme. On 31 January 2016, an aggregate of 19,865,199 RSUs were accepted by the connected grantees and an aggregate of 21,199,297 RSUs were accepted by the non-connected grantees, respectively.

On 24 March 2017, the Board of the Company approved the conditional grant of an aggregate of 26,333,182 RSUs to certain connected grantees and non-connected grantees of the Group in accordance with the Post-IPO RSU Scheme, subject to the approval by the independent shareholders of the Company and the acceptance by the grantees where applicable. On 9 May 2017, the grant of RSUs to the connected grantees was approved by the independent shareholders at the extraordinary general meeting. On 31 May 2017, an aggregate of 26,333,182 RSUs were accepted by the relevant grantees.

OUTSTANDING RSUs

For the year ended 31 December 2017, 2,622,115 RSUs have lapsed. 9,880,788 RSUs have vested. As at 31 December 2017, there were a total of 53,984,475 RSUs outstanding. If all outstanding RSUs are vested, there would be a dilution effect on the share capital of the Company as at 31 December 2017 of approximately 1.62%.

USE OF NET PROCEEDS FROM LISTING

The net proceeds from the listing of the Company (after deducting underwriting fee and relevant expenses) amounted to approximately RMB1,506.9 million. As of 31 December 2017, RMB273.1 million of the proceeds had been utilized. The net proceeds were and will be used for the same purpose as set out in the section headed "Future Plans and Use of Proceeds — Use of Proceeds" in the Prospectus.

FINAL DIVIDEND

The Board has recommended the payment of a final dividend of HK$0.0248 per share for the year ended 31 December 2017, subject to the approval of the Shareholders at the AGM to be held on 8 May 2018. The proposed dividends are expected to be payable on 20 June 2018 to the Shareholders whose names appear on the register of members of the Company as of 16 May 2018.

ANNUAL GENERAL MEETING AND CLOSURE OF THE REGISTER OF MEMBERS

The annual general meeting of the Company (the "**AGM**") is tentatively scheduled to be held on Tuesday, 8 May 2018. The notice of the AGM will be published and issued to shareholders in due course. The register of members of the Company will be closed from 3 May 2018 to 8 May 2018, both days inclusive, in order to determine the identity of the shareholders who are entitled to attend and vote at the AGM, during which period no transfers of Shares will be registered. To be eligible to attend the AGM, all properly completed transfer forms accompanied by the relevant share certificates must be lodged for registration with the Company's branch share registrar in Hong Kong, Computershare Hong Kong Investor Services Limited, at Shops 1712–1716, 17th Floor, Hopewell Centre, 183 Queen's Road East, Wanchai, Hong Kong not later than 4:30 p.m. on 2 May 2018.

The record date for qualifying to receive the proposed final dividend is 16 May 2018. In order to determine the right of shareholders entitled to receive the proposed final dividend, which is subject to the approval by shareholders in the forthcoming AGM, the register of members of the Company will also be closed from 14 May 2018 to 16 May 2018, both days inclusive, during which period the registration of transfer of shares will be suspended. All transfer of shares, accompanied by the relevant share certificates, must be lodged with the Company's branch share registrar and transfer office in Hong Kong, Computershare Hong Kong Investor Services Limited, at Shops 1712–1716, 17th Floor, Hopewell Centre, 183 Queen's Road East, Wanchai, Hong Kong for registration no later than 4:30 p.m. on 11 May 2018.

CORPORATE GOVERNANCE

The Company is committed to maintaining high standards of corporate governance to safeguard the interests of shareholders and to enhance corporate value and accountability. The Company has adopted the Corporate Governance Code (the "**CG Code**") contained in Appendix 14 to the Rules Governing the Listing of Securities (the "**Listing Rules**") on The Stock Exchange of Hong Kong Limited (the "**Stock Exchange**") as its own code of corporate governance. The Company has complied with all applicable code provisions under the CG Code during the year ended 31 December 2017. The Company will continue to review and monitor its corporate governance practices to ensure compliance with the CG Code.

MODEL CODE FOR SECURITIES TRANSACTIONS

The Company has adopted the "Model Code for Securities Transactions by Directors of Listed Issuers" (the "**Model Code**") as set out in Appendix 10 of the Listing Rules as its own code of conduct regarding directors' securities transactions. Having made specific enquiries of all Directors, each of the Directors has confirmed that they have complied with the required standards as set out in the Model Code for the year ended 31 December 2017.

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

Neither the Company nor its subsidiaries has purchased, sold or redeemed any of the Company's listed securities for the year ended 31 December 2017.

AUDIT COMMITTEE AND REVIEW OF FINANCIAL STATEMENTS

The Board has established an audit committee (the "**Audit Committee**") which comprises two independent non-executive Directors and a non-executive Director, namely Mr. Stephen Cheuk Kin Law (chairman), Mr. Robert Ralph Parks and Mr. Gordon Sun Kan Shaw.

The Audit Committee has, together with the Board and external auditor of the Company, reviewed the accounting standards and practices adopted by the Group and the audited annual results for the year ended 31 December 2017. The Audit Committee has also reviewed the effectiveness of the risk management and internal control systems of the Company and considers the risk management and internal control systems to be effective and adequate.

PUBLICATION OF THE ANNUAL RESULTS AND 2017 ANNUAL REPORT ON THE WEBSITES OF THE STOCK EXCHANGE AND THE COMPANY

This annual results announcement is published on the websites of the Stock Exchange (www.hkexnews.hk) and the Company (www.aagenergy.com), and the annual report for the year ended 31 December 2017 containing all the information required by the Listing Rules will be dispatched to the shareholders of the Company and published on the respective websites of the Stock Exchange and the Company in due course.

By order of the Board
AAG Energy Holdings Limited
Stephen Xiangdong Zou
Chairman

Hong Kong, 23 March 2018

As of the date of this announcement, the executive Director is Stephen Xiangdong Zou; the non-executive Directors are Peter Randall Kagan, Gordon Sun Kan Shaw, Zhen Wei, Lei Jin, Guiyong Cui, Saurabh Narayan Agarwal and Fei Nie; and the independent non-executive Directors are Yaowen Wu, Robert Ralph Parks, Stephen Cheuk Kin Law and Fredrick J. Barrett.