



山東墨龍石油機械股份有限公司

Shandong Molong Petroleum Machinery Company Limited

(a joint stock limited company incorporated in the People's Republic of China)

(Stock Code: 8261)

**Third Quarterly Results Report
For the nine months ended 30 September 2004**

Characteristics of the Growth Enterprise Market (“GEM”) of The Stock Exchange of Hong Kong Limited (The “Stock Exchange”)

GEM has been established as a market designed to accommodate companies to which a high investment risk may be attached. In particular, companies may list on GEM with neither a track record of profitability nor any obligation to forecast future profitability. Furthermore, there may be risks arising out of the emerging nature of companies listed on GEM and the business sectors or countries in which the companies operate. Prospective investors should be aware of the potential risks of investing in such companies and should make the decision to invest only after due and careful consideration. The greater risk profile and other characteristics of GEM mean that it is a market more suited to professional and other sophisticated investors.

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This report, for which the directors (“Directors”) of Shandong Molong Petroleum Machinery Company Limited (the “Company”) collectively and individually accept full responsibility, includes particulars given in compliance with the Rules Governing the Listing of Securities on the GEM of the Stock Exchange (“GEM Listing Rules”) for the purpose of giving information with regard to the Company. The Directors, having made all reasonable enquiries, confirm that, to the best of their knowledge and belief: (1) the information contained in this report is accurate and complete in all material respects and not misleading; (2) there are no other matters the omission of which would make any statement in this report misleading; and (3) all opinions expressed in this report have been arrived at after due and careful consideration and are founded on bases and assumptions that are fair and reasonable.

HIGHLIGHTS

- Achieved a turnover of approximately RMB352,001,000 for the nine months ended 30 September 2004, representing an approximately 71.8% increase in turnover as compared with the turnover for the corresponding period in 2003.
- Accomplished a net profit of approximately RMB44,703,000 for the nine months ended 30 September 2004, representing an approximately 68.4% increase in net profit as compared with the net profit for the corresponding period in 2003.
- Earnings per share of the Group was approximately RMB9.2 cents for the nine months ended 30 September 2004.
- The Directors do not recommend the payment of an interim dividend for the three months ended 30 September 2004.

THIRD QUARTERLY RESULTS (UNAUDITED)

The board of directors of the Company is pleased to announce the unaudited results of the Company and its subsidiary (the “Group”) for the nine months ended 30 September 2004.

For the three months ended 30 September 2004, the unaudited turnover is approximately RMB136,295,000, representing a growth of approximately 112.2% in turnover as compared with that of the corresponding period in 2003.

Due to the growth in turnover, the unaudited net profit of the Group for the three months and the nine months ended 30 September 2004 are approximately RMB19,643,000 and RMB44,703,000 respectively, representing a growth of 110.5% and 68.4% as compared with the corresponding figures in 2003.

CONDENSED CONSOLIDATED PROFIT AND LOSS ACCOUNT (UNAUDITED)

For the three months and the nine months ended 30 September 2004

The unaudited results of the Group for the three months and the nine months ended 30 September 2004 together with the unaudited comparative figures for the corresponding period in 2003 are as follows:

	Note	Three months ended 30 September		Nine months ended 30 September	
		2004 RMB'000	2003 RMB'000	2004 RMB'000	2003 RMB'000
Turnover	(2)	136,295	64,223	352,001	204,863
Cost of sales		(112,079)	(46,348)	(280,057)	(152,529)
Gross profit		24,216	17,875	71,944	52,334
Other revenue and gains		1,142	3,423	9,771	11,671
Selling and distribution costs		(5,990)	(2,156)	(12,721)	(6,620)
Administrative expenses		(3,144)	(2,465)	(8,630)	(7,981)
Other operating expenses		(1,491)	(2,007)	(4,219)	(5,408)
Profit from operating activities		14,733	14,670	56,145	43,996
Finance costs		(1,250)	(1,372)	(3,823)	(3,865)
Profit before tax		13,483	13,298	52,322	40,131
Tax	(3)	7,060	(3,554)	(5,630)	(12,370)
Profit before minority interests		20,543	9,744	46,692	27,761
Minority interests		(900)	(413)	(1,989)	(1,209)
Net profit from ordinary activities attributable to shareholders		19,643	9,331	44,703	26,552
Earnings per share — basic (RMB cents)	(4)	3.6	2.3	9.2	6.5
Interim dividend paid per share (RMB cents)		N/A	N/A	2.0	N/A

Notes:

1. Basis of presentation

The unaudited results of the Group have been prepared in accordance with Statements of Standard Accounting Practice issued by the Hong Kong Society of Accountants, accounting principles generally accepted in Hong Kong and the GEM Listing Rules.

The Company was incorporated as a joint stock company with limited liability in the People's Republic of China (the "PRC") on 30 December 2001 and its H shares were listed on the GEM (the "Listing") on 15 April 2004. On 16 August 2004, the Company became a foreign invested joint stock limited company.

2. Turnover & segment information

Turnover represents the invoiced value of goods sold, and after allowances for goods returned and trade discounts. All significant intra-group transactions have been eliminated on consolidation.

The Group's operating business is with customers based in the PRC, the United States and other countries. Each of the Group's geographical segments represents customer destinations to which the Group sells products or provides services which are subject to risks and returns that are different from those of the other geographical segments. Save as disclosed below, no further business segment information is presented as over 90% of the Group's revenue and assets relate to the sale of petroleum machineries.

By products	Three months ended		Nine months ended	
	30 September		30 September	
	2004	2003	2004	2003
	RMB'000	RMB'000	RMB'000	RMB'000
Oil well pipes	71,229	24,173	180,194	94,354
Other petroleum extraction machinery accessories	40,916	24,830	105,289	59,727
Oil well sucker rods	12,556	10,612	47,700	32,900
Oil well pumps	11,594	4,608	18,818	17,882
	<u>136,295</u>	<u>64,223</u>	<u>352,001</u>	<u>204,863</u>
By geographical area	Three months ended		Nine months ended	
	30 September		30 September	
	2004	2003	2004	2003
	RMB'000	RMB'000	RMB'000	RMB'000
PRC	106,612	54,975	281,830	179,009
United States	10,608	9,248	42,850	25,844
Other countries	19,075	0	27,321	10
	<u>136,295</u>	<u>64,223</u>	<u>352,001</u>	<u>204,863</u>

3. Tax

	Three months ended		Nine months ended	
	30 September		30 September	
	2004	2003	2004	2003
	<i>RMB'000</i>	<i>RMB'000</i>	<i>RMB'000</i>	<i>RMB'000</i>
The charge comprises PRC income tax	<u>(7,060)</u>	<u>3,554</u>	<u>5,630</u>	<u>12,370</u>

The Group is located in the PRC and as a result are subject to PRC corporate income tax at a rate of 33% on their assessable profits.

The subsidiary of the Company, Shouguang Molong Machinery Company Limited (“Molong Machinery”), being a welfare enterprise, was exempted from 2003 corporate income tax of approximately RMB11,333,000.

No provision for Hong Kong profits tax has been made as the Group did not generate any assessable profits in Hong Kong.

The Group had no significant unprovided deferred tax as at 30 September 2004 and 2003.

4. Earnings per share

The calculation of the basic earnings per share is based on the profit attributable to shareholders of approximately RMB19,643,000 and RMB44,703,000 for the three months and the nine months ended 30 September 2004 (2003: RMB9,331,000 and RMB26,552,000) and on the weighted average number of approximately 488,265,000 (2003: 405,000,000) shares in issue during the period.

Diluted earnings per share is not presented for the three months and the nine months ended 30 September 2004 and 2003 as there were no potential dilutive securities in existence during the relevant periods.

5. Reserves

There were no movements in reserves of the Group for the three months ended 30 September 2004 and 2003.

6. Capital commitments

As at 30 September 2004, the Group had capital commitments amounting to RMB80,559,000.

7. Contingent liabilities

As at 30 September 2004, the Group did not have any significant contingent liabilities.

INTERIM DIVIDEND

The Directors do not recommend the payment of an interim dividend for the three months ended 30 September 2004 (2003: Nil).

Total dividend for the nine months ended 30 September 2004 amounted to RMB10,800,000 (2003: Nil).

BUSINESS AND FINANCIAL REVIEW

Business Review

The Group principally engages in the design, manufacture and sale of petroleum extraction machinery and related accessories, which can be grouped into 5 main product categories, namely, oil well pipes, oil well sucker rods, oil well pumps, oil well pumping machines and other petroleum extraction machinery accessories. These products, which are principally used for upstream petroleum extraction engineering, are essential equipment for the petroleum extraction industry. Most of the Group's products are sold to domestic oilfields within the PRC. However, with the Group's proactive strategies in expanding its international markets, the export ratios of its products are increasing gradually. Currently, the Group's major customers are oil fields in the PRC including Daqing Oil Field (大慶油田), Shengli Oil Field (勝利油田), Xinjiang Oil Field (新疆油田), Zhongyuan Oil Field (中原油田) and Liaohe Oil Field (遼河油田), all of them being oil fields of subsidiaries or branches of China Petroleum Corporation ("PetroChina") or China Petroleum & Chemical Corporation ("Sinopec"). Moreover, the Company's main products such as oil well sucker rods, oil well pipes and valves are also exported to the United States, the United Kingdom, Indonesia and Syria with Campex Co. of the United States and Petroleum Pipe Co. Ltd. of the United Kingdom being its overseas customers.

During the period under review, demand for petroleum extraction machinery has increased significantly. Compared with business objectives as stated in the prospectus of the Company dated 30 March 2004, the Group's production capacities has increased gradually as scheduled with some of the production projects having surpassed their targets. Current annual production capacity of 3.5 million metres of oil well sucker rods and 50,000 tonnes of oil well pipes, respectively, are able to cater for increasing market demands.

Leveraging on its leading position in the petroleum extraction machinery industry and coupled with its committed efforts in new product research and development for enhancing competitiveness, the Group continued to be successful in enlarging its market coverage in the PRC. At the same time, the Group's overseas market also experienced significant growth with substantial increase in sales to the United States and other new emerging markets being recorded during the period under review. Export sales of the Group's core products, such as valves, related accessories, oil well pipes and oil well sucker rods increased notably with its product quality being highly acclaimed by overseas customers of the Group. In order to keep the Group's domestic and overseas customers fully abreast of the latest market and product information, the contents of Group's official website were revamped. In addition, the Group successfully implemented the Enterprise Resources Planning ("ERP") system which facilitated internal communications as well as further enhanced the efficiency in resources deployment and quality of management.

In terms of product research and development, the Group has successfully developed production technology in special seamless oil well pipes, super-strength oil well sucker rods and casing. The projects of special seamless oil well pipes and super-strength oil well sucker rods, which were officially established and put into full production on 8 June 2004 and 10 July 2004 respectively, had already met expected production capacity. The success in producing special seamless oil well pipes and super-strength oil well sucker rods ahead of schedule not only further enhanced the Group's production capacity and profitability, but also laid a solid foundation for the Group's future business development.

Financial Review

The Group has achieved an encouraging result during the period under review. For the nine months ended 30 September 2004, the Group has accomplished revenue of approximately RMB352,001,000 (2003: RMB204,863,000) and a net profit of approximately RMB44,703,000 (2003: RMB26,552,000), representing a growth of 71.8% in revenue and an increase of 68.4% in net profit as compared to the corresponding period in the previous year.

For the three months ended 30 September 2004, the Group has accomplished revenue of approximately RMB136,295,000 (2003: RMB64,223,000) and a net profit of approximately RMB19,643,000 (2003: RMB9,331,000). This represents a growth of 112.2% in total revenue and an increase of 110.5% in net profit as compared to the same period in the previous year.

As at 30 September 2004, the Group had net current assets of RMB119,293,000. The Directors believe that the Group would have sufficient capital to meet its liabilities and commitments.

FUTURE PROSPECTS

Research and Development

The Group is committed to research and development of new products, with particular emphasis on further enhancing the quality of super-strength oil well sucker rods, special seamless oil well pipes and casing. The Directors believe that the Group's commitment on research and development of new products and improvement of existing products are crucial for maintaining the Group's competitive edge in the PRC and overseas markets. In addition, the Group will strengthen its research and development capability by recruiting more research personnel with a view to improve product quality and functionality and sustain its competitive advantages in technology in response to market trends. The Group also planned to adopt advanced production lines and new production facilities in preparation for future business expansion.

Through these research and development projects, the Group expects to develop more innovative products as well as to expand existing production lines and/or construct new production lines according to actual demand in order to upgrade production capacity, and to satisfy ever-growing market demands.

Expansion of Market Coverage

To further enlarge domestic market coverage and enter into international market, the Group intends to actively expand its sales force and intensify its marketing activities, including participation in international and national petroleum extraction machinery exhibitions and fairs, paying regular oil fields visits, assimilating customers' opinions and latest market development, and enhancing its relationships with existing customers in order to expand the Group's scope of market coverage in the PRC and overseas markets. Besides, the Group also intends to expand its sales network in strategic locations such as South East Asia and the Middle East. The Group believes that expansion of sales network in such locations would assist the Group to maintain closer contacts with overseas markets, increase product sales and enhance the Group's reputation in the international market.

Expansion of Production Capacity

In order to cater for the rising demand of the petroleum extraction machinery in the PRC, the Group will upgrade its production capacity by constructing new production facilities. Success in the production of super-strength oil well sucker rods in July 2004 will further broaden the Group's product ranges and revenue sources.

Looking into the future, with oil prices scaling new historical highs from time to time, demands for petroleum in the international and PRC markets remain high, which also leads to increase in inventory reserves. On the other hand, aging oilfields would accelerate functional obsolescence of petroleum extraction machinery which will lead to gradual increases in capital expenditure of global oil suppliers and serve as a driving force of demand for petroleum extraction machinery. The Directors expect that domestic and overseas demands for petroleum extraction machinery would sustain its growth momentum. The Group is confident of further progresses in its future business development by keeping abreast of market trends and maintaining competitiveness.

The Directors believe that, with its relentless efforts in developing new products, enhancing existing products as well as upgrading production capacity, the Group would capture the opportunities thus arisen, satisfy market demands and continue to enlarge market coverage successfully. At the same time, growth in profitability as a result of fortified management practices and more effective utilization of the Group's resources would generate satisfactory returns to our shareholders.

MATERIAL ACQUISITION/DISPOSAL AND SIGNIFICANT INVESTMENT

Saved as disclosed in the subsection headed "Further information about the business" in the section headed "Statutory and general information" in Appendix V to the prospectus dated 30 March 2004, the Group had no material acquisition, disposal and investment. At present the Group has no other future plan for material acquisitions or disposal of significant investments other than those set out in the section headed "Statement of business objectives" in the prospectus.

BANK FACILITIES AND PLEDGE OF ASSETS

The Group did not have banking facilities with financial institutions. As at 30 September 2004, the Group borrowed a sum of RMB74,000,000 short term loan which was secured by corporate guarantee and assets of the Group.

EMPLOYEES

A breakdown of the number of employees of the Group by function as at 30 September 2004 were set out below:

	Nine months ended	
	30 September	
	2004	2003
Research and development	47	40
Production	936	780
Quality control	78	70
Sales and marketing	52	45
Administration	156	142
	<u>1,269</u>	<u>1,077</u>
Total	<u>1,269</u>	<u>1,077</u>

The Group keeps a close watch on the levels of remuneration and benefits, rewarding staff according to merit. It also offers employees training and development opportunities to upgrade their abilities.

DISCLOSURE UNDER GEM LISTING RULES 17.15 TO 17.21

Under the Chapter 17.16 of GEM Listing Rules, a disclosure obligation arises, among other situations, where:

- (a) the relevant advances to an entity increases from that previously disclosed and any of the percentage ratios for the amount of the increase since the previous disclosure is 3% or more.

Advance to an entity

The total market capitalisation of the Company based on the average closing price of the H shares of the Company for the five business days from 23 September 2004 to 30 September 2004 was approximately HK\$354,239,000 (the "Market Capitalisation").

There is a trade receivable of an amount of approximately RMB63,082,000 and note receivable of an amount of approximately RMB2,336,000 owed from an independent party, China Petroleum Corporation ("PetroChina") as at 30 September 2004. Such receivables represented approximately 17.3% of the Market Capitalisation. Accordingly, a disclosure obligation under paragraph 17.16 of Chapter 17 for the Company arises.

There is a trade receivable of an amount of approximately RMB28,447,000 owed from an independent party, China Petroleum & Chemical Corporation ("Sinopec") as at 30 September 2004. Such receivables represented approximately 7.5% of the Market Capitalisation.

As confirmed by the Directors, the trade receivables and notes receivables referred to above were resulted from the sale of the Group's products to such customer in the ordinary course of business of the Group. The trade receivables and notes receivables were unsecured, interest free and had a credit terms of between 30 to 150 days.

DISCLOSURE OF DIRECTORS' AND SUPERVISORS' INTERESTS IN SHARES

As at 30 September 2004, the interest or short positions of the Directors or chief executives of the Company in the shares, debentures or underlying shares of the Company and its associated corporations (within the meaning of Part XV of the Securities, and Futures Ordinance (the "SFO")) which will be required to be notified to the Company and The Stock Exchange of Hong Kong Limited (the "Stock Exchange") pursuant to Divisions 7 and 8 of Part XV of the SFO (including interests or short positions which they are taken or deemed to have under such provisions of the SFO) or which will be required, pursuant to section 352 of the SFO, to be entered in the register referred to therein, or which will be required pursuant to rules 5.46 to 5.68 of the GEM Listing Rules, to be notified to the Company and the Stock Exchange, will be as follows:

Long positions in shares of the Company

Name	Type of Interest	Number of Shares (Note)	Percentage of domestic shares	Percentage of total registered share capital
Zhang En Rong	Personal	279,517,000	69.58%	51.76%
Lin Fu Long	Personal	34,216,000	8.52%	6.34%
Zhang Yun San	Personal	30,608,000	7.62%	5.67%
Xie Xin Cang	Personal	21,410,000	5.33%	3.96%

(Note: All represented domestic shares)

Other than as disclosed above, none of the Directors or chief executives of the Company had any interests or short position in the shares, underlying shares or debentures of the Company or any of its associated corporations (within the meaning of Part XV of the SFO), as recorded in the register required to be kept under section 352 of the SFO or as otherwise notified to the Company and the Stock Exchange pursuant to the required standard of dealings by Directors of the Company as referred to in Rule 5.46 to 5.68 of the GEM Listing Rules.

DIRECTORS' RIGHTS TO ACQUIRE H SHARES

During the nine months ended 30 September 2004, none of the Directors was granted any options to subscribe for H shares of the Company. As at 30 September 2004, none of the Directors nor their spouses or children under the age of 18 had any right to acquire H shares in the Company or had exercised any such right during the period.

SHARE OPTION SCHEME

The Company does not have share option scheme.

SUBSTANTIAL SHAREHOLDERS

As at 30 September 2004, the following persons (other than Directors or chief executives of the Company) had interests or short positions in the shares and underlying shares of the listed issuer as recorded in the register to be kept under section 336 of the SFO:

Long positions in shares

Name	Type of interests	Number of shares	Percentage of domestic shares	Percentage of H shares	Percentage of total registered capital
Zhang Xiu Lan (<i>Note 1</i>)	Interests of Spouse	279,517,000	69.58%	—	51.76%
Li Xiu Fen (<i>Note 2</i>)	Interests of Spouse	34,216,000	8.52%	—	6.34%
Zhang Xin Lan (<i>Note 3</i>)	Interests of Spouse	30,608,000	7.62%	—	5.67%
Li Bao Hui (<i>Note 4</i>)	Interests of Spouse	21,410,000	5.33%	—	3.96%
Martin Currie Investment Management Limited	Investment Manager	15,384,000	—	11.13%	2.85%
Martin Currie China Hedge Fund Limited	Investment Manager	12,264,000	—	8.87%	2.27%
Peter Cundill & Associates (Bermuda) Ltd.	Investment Manager	60,320,000	—	43.62%	11.17%
UBS AG	Person Having a Security Interest in Shares	12,264,000	—	8.87%	2.27%

Note 1: Zhang Xiu Lan is the wife of Zhang En Rong and is taken to be interested in the shares in 279,517,000 domestic shares held by Zhang En Rong under the SFO.

Note 2: Li Xiu Fen is the wife of Lin Fu Long and is taken to be interested in the shares in 34,216,000 domestic shares held by Lin Fu Long under the SFO.

Note 3: Zhang Xin Lan is the wife of Zhang Yun San and is taken to be interested in the shares in 30,608,000 domestic shares held by Zhang Yun San under the SFO.

Note 4: Li Bao Hui is the wife of Xie Xin Cang and is taken to be interested in the shares in 21,410,000 domestic shares held by Xie Xin Cang under the SFO.

Save as disclosed above, the Directors were not aware of any other person (other than Directors or chief executives of the Company) who had interests or short positions in the shares and underlying shares of the listed issuer as recorded in the register required to be kept under section 336 of the SFO.

COMPETING INTERESTS

None of the Directors or the management shareholders of the Company and their respective associates (as defined in the GEM Listing Rules) had any interest in a business which competes or may compete with the business of the Group.

SPONSOR'S INTEREST

As updated and notified by the Company's sponsor, Deloitte & Touche Corporate Finance Limited (the "Sponsor"), neither the Sponsor nor its Directors, employees or associates had any interest in the share capital of the Company as at 30 September 2004 pursuant to Note 3 to Rule 6.35 of the GEM Listing Rules.

Pursuant to an agreement dated 29 March 2004 entered into between the Company and the Sponsor, the Sponsor will receive a fee for acting as the Company's retained sponsor for the period from 15 April 2004 to 14 April 2006 or until the sponsor agreement is terminated in accordance with the terms and conditions set out therein.

AUDIT COMMITTEE

The Company established an audit committee on 20 March 2004 with written terms of reference in compliance with the requirements as set out in Rules 5.28 and 5.30 of the GEM Listing Rules. The primary duties of the audit committee are to review and to provide supervision over the financial reporting process and internal control system of the Group. The audit committee comprises the three independent non-executive Directors, Mr. Qin Xue Chang and Mr. Yan Yi Zhuang and Mr. Loke Yu alias Loke Hoi Lam. Mr. Qin Xue Chang is the chairman in the Audit Committee.

The Audit Committee has reviewed with the management the accounting principles and practices adopted by the Group and discussed internal controls and financial reporting matters, including a review of the unaudited results of the Group for the nine months ended 30 September 2004.

BOARD PRACTICES AND PROCEDURES

The Company has complied throughout the nine months ended 30 September 2004 with the requirements on board practices and procedures as set out in Rules 5.34 to 5.45 of the GEM Listing Rules.

CODE OF CONDUCT REGARDING SECURITIES TRANSACTIONS BY DIRECTORS

During the nine months ended 30 September 2004, the Company had adopted a code of conduct regarding securities transactions by directors on terms no less exacting than the required standard no dealings set out in Rules 5.48 to 5.67 of the GEM Listing Rules. The Company also had made specific enquiry of all directors and the Company was not aware of any non-compliance with the required standard of dealings and its code of conduct regarding securities transactions by directors.

PURCHASE, SALE OR REDEMPTION OF SECURITIES

Neither the Company nor its subsidiary has purchased, sold or redeemed any listed securities of the Company during the nine months ended 30 September 2004.

DIRECTORS

As at the date of this report, the executive Directors of the Company are Mr. Zhang En Yong, Mr. Zhang Yun San, Mr. Lin Fu Long, Mr. Xie Xin Cang, the non-executive Directors are Mr. Chen Jian Xiong, Mr. Wang Ping and the independent non-executive Directors are Mr. Qin Yue Chang, Mr. Yan Yi Zhuang, Mr. Loke Yu alias Loke Hoi Lam.

On behalf of the Board
Zhang En Rong
Chairman

2 November 2004, Shandong, the PRC