

The directors (the "Directors") of CNOOC Limited (the "Company") are pleased to present their report together with the audited financial statements for the year ended 31 December 2002.

Principal Activities and Operating Results

The principal activity of the Company is investment holding of its subsidiaries (which together with the Company shall be known as the "Group"), which are principally engaged in the exploration, development, production and sales of crude oil and natural gas.

Summary of Financial Information

Please refer to the financial statements for a summary of the assets and liabilities of the Group as at 31 December 2002 on page 45 and the operating results for the year then ended on page 44.

Loans

Please refer to note 27 to the financial statements on pages 74 to 75 for details of the long-term bank loans of the Group for the year ended 31 December 2002.

Property, Plant and Equipment, net

Please refer to note 19 to the financial statements on pages 68 to 69 for movements in property, plant and equipment, net of the Group for the year ended 31 December 2002.

Reserves

Please refer to the statement of changes in equity on page 46 and note 33 of the financial statements on page 83 for movements in the reserves of the Group and the Company, respectively, for the year ended 31 December 2002.

Subsidiaries and Associated Company

Particulars of the Company's subsidiaries and associated company as at 31 December 2002 are set out in notes 20 and 21 to the financial statements on pages 69 to 72.

Dividends

The Directors recommend the payment of a final dividend of HK\$0.15 per share for the year ended 31 December 2002 and a special cash dividend of HK\$0.15 per share.

Retirement Benefits

Please refer to note 34 to the financial statements on page 84 for details of the retirement benefits of the Group for the year ended 31 December 2002.

Major Suppliers and Customers

Purchases from the largest supplier of the Group for the year ended 31 December 2002 represented approximately 15% of the Group's total purchases. The total purchases attributable to the five largest suppliers of the Group accounted for approximately 34% of the total purchases of the Group for the year then ended.

Sales to the largest customer for the year ended 31 December 2002 represented approximately 29% of the Group's total sales. The total sales attributable to the five largest customers of the Group accounted for approximately 50% of the total sales of the Group for the year then ended.

None of the Directors or their respective associates (as defined in the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the "Listing Rules")) or any shareholder of the Company (which to the knowledge of the Directors owns more than 5% of the Company's share capital) had any interests in the five largest suppliers or customers of the Group for the year ended 31 December 2002.

Connected Transactions

The Independent Non-executive Directors confirmed that the following connected transactions for the year ended 31 December 2002 to which the Group was a party and the agreements governing those transactions were entered into by the Group:

1. in the ordinary and usual course of its business;

2. either (a) on normal commercial terms, or (b) where there was no available comparison, on terms no less favourable than those available to independent third parties; and
3. on terms that were fair and reasonable so far as the shareholders of the Company were concerned.

The Independent Non-executive Directors further confirmed that:

1. the aggregate annual volume of transactions under the materials, utilities and ancillary services supply agreements has not exceeded 10% of the audited consolidated total revenues of the Group in the immediate preceding financial year;
2. the aggregate annual volume of transactions in relation to technical services has not exceeded RMB5,300 million;
3. the aggregate annual volume of transactions in relation to research and development services for particular projects has not exceeded RMB160 million;
4. the aggregate annual volume of transactions in relation to sales of crude oil, condensate oil and liquefied petroleum gas has not exceeded 38% of the audited consolidated total revenues of the Group in the immediate preceding financial year;
5. the amount paid under the general research and development services agreement has not exceeded RMB110 million; and
6. the aggregate amounts paid under the lease and management agreements have not exceeded RMB55 million.

The auditors of the Group have reviewed the transactions referred to in the above paragraph 1 to paragraph 6 and confirmed to the Directors that:

1. the transactions have received the approval of the Directors;

2. the transactions were in accordance with the pricing policies as stated in the Company's financial statements; and
3. the transactions were entered into in accordance with the terms of the agreements governing the transactions.

Please refer to note 30 to the financial statements on pages 76 to 78 for a summary of the related party transactions which include the Group's connected transactions.

Share Capital

Please refer to note 32 to the financial statements on pages 80 to 82 for details of movements in the Company's share capital for the year ended 31 December 2002.

Share Option Schemes

On 4 February 2001, the Company adopted a pre-global offering share option scheme (the "Pre-Global Offering Share Option Scheme"). Pursuant to the Pre-Global Offering Share Option Scheme:

1. options for an aggregate of 4,620,000 shares have been granted;
2. the subscription price per share is HK\$5.95; and
3. the period during which an option may be exercised is as follows:
 - (a) 50% of the shares underlying the option shall vest 18 months after the date of the grant; and
 - (b) 50% of the shares underlying the option shall vest 30 months after the date of the grant.

The exercise period for options granted under the Pre-Global Offering Share Option Scheme shall end not later than 10 years from 12 March 2001.

On 4 February 2001, the Company adopted a share option scheme (the "2001 Share Option Scheme") for the purposes of recognising the contribution that certain individuals had made to the Company and attracting and retaining the best available personnel to the Company. Pursuant to the 2001 Share Option Scheme:

1. options for an aggregate of 8,820,000 shares have been granted;
2. the subscription price per share is HK\$6.16; and
3. the period during which an option may be exercised is as follows:
 - (a) one-third of the shares underlying the option shall vest on the first anniversary of the date of the grant;
 - (b) one-third of the shares underlying the option shall vest on the second anniversary of the date of the grant; and
 - (c) one-third of the shares underlying the option shall vest on the third anniversary of the date of the grant.

The exercise period for options granted under the 2001 Share Option Scheme shall end not later than 10 years from 27 August 2001.

In view of the amendments to the relevant provisions of the Listing Rules regarding the requirements of share option schemes of a Hong Kong listed company effective on 1 September 2001, no further options will be granted under the 2001 Share Option Scheme.

In June 2002, the Company adopted a new share option scheme (the "2002 Share Option Scheme").

Under the 2002 Share Option Scheme, the Directors of the Company may, at their discretion, invite employees, including executive directors, of the Company or any of its subsidiaries, to take up options to subscribe for shares. The maximum aggregate number of shares (including those that could be subscribed for under the Pre-Global

Offering Share Option Scheme and the 2001 Share Option Scheme) which may be granted shall not exceed 10% of the total issued share capital of the Company. The maximum number of shares which may be granted under the 2002 Share Option Scheme to any individual in any 12 month period up to the next grant shall not exceed 1% of the total issued share capital of the Company from time to time.

According to the 2002 Share Option Scheme, the consideration payable by a participant for the grant of an option will be HK\$1.00. The subscription price of a share payable by a participant upon the exercise of an option will be determined by the Directors at their discretion at the date of grant, except that such price may not be set below a minimum price which is the highest of:

1. the nominal value of a share;
2. the average closing price of the shares on the HKSE as stated in the HKSE's quotation sheets for the five trading days immediately preceding the date of grant of the option; and
3. the closing price of the shares on the HKSE as stated in the HKSE's quotation sheets on the date of grant of the option.

The period during which an option may be exercised is as follows:

1. one-third of the shares underlying the option shall vest on the first anniversary of the date of the grant;
2. one-third of the shares underlying the option shall vest on the second anniversary of the date of the grant; and
3. one-third of the shares underlying the option shall vest on the third anniversary of the date of the grant.

The exercise period for options granted under the 2002 Share Option Scheme shall end not later than 10 years from the date on which the option is granted.

As at 31 December 2002, the directors and employees of the Group had the following personal interests in options to subscribe for shares in the Company granted under the share option schemes of the Company:

Name of Grantee	No. of shares involved in the options outstanding at the beginning of the year	No. of shares involved in the options outstanding at year end	Date of Grant	Closing price per share immediately before the date on which the options were granted	Exercise Price (HK\$)
Directors:					
Wei Liucheng	500,000	500,000	12 March 2001	—	5.95
	500,000	500,000	27 Aug 2001	7.30	6.16
Fu Chengyu	350,000	350,000	12 March 2001	—	5.95
	350,000	350,000	27 Aug 2001	7.30	6.16
Jiang Longsheng	280,000	280,000	12 March 2001	—	5.95
	230,000	230,000	27 Aug 2001	7.30	6.16
Zhou Shouwei	280,000	280,000	12 March 2001	—	5.95
	350,000	350,000	27 Aug 2001	7.30	6.16
Luo Han	280,000	280,000	12 March 2001	—	5.95
	230,000	230,000	27 Aug 2001	7.30	6.16
Employees:					
Other Employees	2,930,000	2,930,000	12 March 2001	—	5.95
	7,160,000	7,160,000	27 Aug 2001	7.30	6.16

As at 31 December 2002, no options granted under the Pre-Global Offering Share Option Scheme and the 2001 Share Option Scheme have been exercised.

The weighted average fair value of the options granted under the Pre-Global Offering Share Option Scheme and the 2001 Share Option Scheme at the grant dates was RMB3.10. This was estimated using the Black-Scholes option pricing model under the following assumptions: risk-free interest rates of 5.25%, expected volatility of 44%, an expected life of five years and an expected dividend yield of 2.0%

The assumptions on which the option pricing model is based represent the subjective estimations of the Directors as to the circumstances existing at the time the options were granted.

Purchase, Sale or Redemption of Shares

For the year ended 31 December 2002, neither the Company nor its subsidiaries has purchased, sold or redeemed any of the Company's listed shares.

Substantial Shareholders of the Company

The Company has been notified of the following interests in the Company's issued shares as of 31 December 2002 amounting to 10% or more of the ordinary shares in issue:

	Ordinary Shares held		Percentage of Total Issued Shares
	Directly	Indirectly	
(i) China National Offshore Oil Corporation ("CNOOC")	-	5,800,000,000	70.61%
(ii) Overseas Oil & Gas Corporation, Limited ("OOGC")	-	5,800,000,000	70.61%
(iii) CNOOC (BVI) Limited ("CNOOC (BVI)")	5,800,000,000	-	70.61%

Note: In light of the fact that CNOOC and OOGC, directly or indirectly, control one-third or more of the voting rights in the shareholders' meetings of CNOOC (BVI), in accordance with the Securities (Disclosure of Interests) Ordinance, the interests of CNOOC (BVI) are deemed to be, and have therefore been included in, the interests of CNOOC and OOGC.

Apart from the foregoing, as at 31 December 2002, no person or corporation had any interest in the share capital of the Company as recorded in the registers required to be kept under section 16(1) of the Securities (Disclosure of Interests) Ordinance as having an interest in 10% or more of the issued share capital of the Company.

Directors and Senior Management of the Company

Please refer to pages 28 to 31 for information concerning the Directors and senior management of the Company.

Directors' Interests in the Equity Securities of the Company

As at 31 December 2002, the interests of the Directors and chief executive of the Company in the equity securities of the Company and its associated company as required to be recorded in the register maintained under section 29 of the Securities (Disclosure of Interests) Ordinance were as follows:

Director	Company	Personal Interest
Chak Kwong So	CNOOC Limited	30,000 Ordinary Shares

Directors' Interests in Contracts

Each of the Executive Directors has entered into a service contract with the Company for a term of three years effective from 28 February 2001.

Apart from the foregoing, no director proposed for re-election at the forthcoming annual general meeting has an unexpired service contract with the Company which is not determinable by the Company within one year without payment of compensation (other than normal statutory obligations).

No contract of significance to which the Company or any of its subsidiaries was a party and in which a director of the Company had a material interest, whether directly or indirectly, subsisted at the end of the year or at any time during the year.

Emoluments of the Directors and the Five Highest Paid Individuals

Please refer to notes 13 and 14 to the financial statements on pages 63 to 64 for details of the emoluments of the Directors and the five highest paid individuals of the Company.

Material Legal Proceedings

As at 31 December 2002, the Company was not involved in any material litigation or arbitration and no material litigation or claims was pending or threatened or made against the Company as far as the Company is aware of.

Compliance with the Code of Best Practice

The Company has complied with the Code of Best Practice as set out by the HKSE in Appendix 14 to the Listing Rules throughout the year ended 31 December 2002, except that the Non-executive Directors were not appointed for a specific term, but are subject to retirement by rotation and re-election at the Company's annual general meeting in accordance with the Company's articles of association.

Auditors

Ernst & Young was appointed as the auditors of the Company for the year ended 31 December 2002 and has audited the accompanying financial statements. A resolution to re-appoint Ernst & Young as auditors of the Company will be proposed at the forthcoming annual general meeting.

By Order of the Board

WEI Liucheng

Chairman

Hong Kong, 27 March 2003