Interim Report 2005/2006

Daqing Petroleum and Chemical Group Limited

(Incorporated in the Cayman Islands with limited liability)

(Stock Code: 362)

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Corporate Information

Board of Directors
Executive Directors
Ms. Chan Yuk Foebe
Mr. Peng Zhanrong
Mr. Chiau Che Kong
(appointed on 14 December 2005)
Mr. Wang Hailou
(resigned on 12 January 2006)
Mr. Chu Ki
(resigned on 14 December 2005)

Independent Non-executive Directors
Mr. Ma Wing Yun Bryan
Mr. Meng Fanxi
Mr. Yau Chung Hong

Company Secretary
Mr. Tsang Chiu Hung

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Head Office and Principal Place of Business in Hong Kong
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Authorised Representatives
Ms. Chan Yuk Foebe
Mr. Chiau Che Kong

Auditors
RSM Nelson Wheeler
Certified Public Accountants
7th Floor, Allied Kajima Building
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Hong Kong

Legal Advisers to the Company
Simmons & Simmons
35th Floor
Cheung Kong Center
2 Queen's Road Central
Hong Kong

Principal Bankers
Hang Seng Bank Limited
83 Des Voeux Road Central
Central
Hong Kong

Standard Chartered Bank
Shop A25-A27, Ground Floor
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Hong Kong

The Bank of China
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PRC

Principal Share Registrar and Transfer Office
Bank of Bermuda (Cayman) Limited
P. O. Box 513 G.T.
2nd Floor, Strathvale House
North Church Street
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Grand Cayman
Cayman Islands
British West Indies

Hong Kong Branch Share Registrar and Transfer Office
Tengis Limited
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28 Queen's Road East
Hong Kong

Stock Code: 362

Financial Highlights

	Six months ended 31 December		
	2005	2004	Change
	HK$'000	HK$'000	
TURNOVER	**343,953**	300,628	14.4%
NET PROFIT FROM ORDINARY ACTIVITIES ATTRIBUTABLE TO SHAREHOLDERS	**40,700**	40,318	0.9%
BASIC EARNINGS PER SHARE	**HK2.5 cents**	HK3.2 cents	(21.9%)
INTERIM DIVIDEND PER SHARE	–	–	–

The Board of Directors ("Board" or "Directors") of Daqing Petroleum and Chemical Group Limited (the "Company") is pleased to announce the unaudited condensed consolidated interim financial statements ("Interim Financial Statements") of the Company and its subsidiaries (collectively the "Group") for the six months ended 31 December 2005 ("Period"). The results had been reviewed by the Company's audit committee ("Audit Committee").

Condensed Consolidated Income Statement

	Note	Unaudited six months ended 31 December 2005 HK$'000	2004 HK$'000
TURNOVER	3	**343,953**	300,628
Cost of sales		**(266,684)**	(226,373)
Gross profit		**77,269**	74,255
Other revenue		**2,614**	4,603
Selling and distribution costs		**(5,642)**	(4,057)
Administrative expenses		**(16,277)**	(13,241)
Other operating expenses		**(291)**	(483)
Non-recurring litigation fee and legal fee for set up of a subsidiary	5	**–**	(4,234)
PROFIT FROM OPERATING ACTIVITIES	5	**57,673**	56,843
Finance costs		**(205)**	(526)
PROFIT BEFORE TAX		**57,468**	56,317
Tax	6	**(3,898)**	(8,652)
PROFIT FOR THE PERIOD		**53,570**	47,665
ATTRIBUTABLE TO:			
Equity holders of the Company		**40,700**	40,318
Minority interests		**12,870**	7,347
		53,570	47,665
EARNINGS PER SHARE	7		
– Basic		**HK2.5 cents**	HK3.2 cents
– Diluted		**N/A**	N/A

Condensed Consolidated Balance Sheet

	Note	Unaudited 31 December 2005 HK$'000	Restated Audited 30 June 2005 HK$'000
ASSETS			
Non-current assets			
Fixed assets	8	**275,772**	155,769
Land use rights		**57,526**	29,592
Other assets	9	**12,887**	13,061
Intangible assets	10	**10,094**	10,094
Deferred development costs	11	**4,953**	4,953
Deposits paid for the establishment of a proposed joint venture	12	**5,140**	5,140
Amount paid for the acquisition of fixed assets and land use rights	13	**–**	73,551
		366,372	292,160
Current assets			
Inventories		**86,380**	125,901
Trade receivables	14	**134,497**	176,836
Prepayments, deposits and other receivables		**37,714**	24,450
Cash and cash equivalents		**343,997**	143,057
		602,588	470,244
Total assets		**968,960**	762,404

	Note	Unaudited 31 December 2005 HK$'000	Restated Audited 30 June 2005 HK$'000
EQUITY			
Capital and reserves attributable to equity holders of the Company			
Issued capital	16	**16,644**	14,496
Other reserves		**284,055**	190,215
Retained profits		**427,393**	386,693
		728,092	591,404
Minority interests		**99,229**	86,359
Total equity		**827,321**	677,763
LIABILITIES			
Current liabilities			
Short term borrowing		**–**	26,000
Trade payables	15	**20,464**	8,198
Other payables and accruals		**75,116**	10,196
Tax payable		**46,059**	40,247
Total liabilities		**141,639**	84,641
Total equity and liabilities		**968,960**	762,404
Net current assets		**460,949**	385,603
Total assets less current liabilities		**827,321**	677,763

Condensed Consolidated Statement Of Changes In Equity – Unaudited

	For the six months ended 31 December 2005							
	Attributable to equity holders of the Company							
	Share premium account HK$'000	Capital reserve HK$'000	Fixed asset revaluation reserve HK$'000	Exchange reserve HK$'000	Retained profits HK$'000	Sub-total HK$'000	Minority interests HK$'000	Total HK$'000
At 1 July 2005, as previously reported as equity	183,407	106	9,817	436	390,923	584,689	–	584,689
At 1 July 2005, as previously reported as minority interests	–	–	–	–	–	–	86,359	86,359
Effect of adopting Hong Kong Accounting Standard 17	–	–	(3,551)	–	(4,230)	(7,781)	–	(7,781)
At 1 July 2005, as restated	183,407	106	6,266	436	386,693	576,908	86,359	663,267
Issue of shares	93,840	–	–	–	–	93,840	–	93,840
Profit for the period	–	–	–	–	40,700	40,700	12,870	53,570
At 31 December 2005	277,247	106	6,266	436	427,393	711,448	99,229	810,677

	For the six months ended 31 December 2004							
	Attributable to equity holders of the Company							
	Share premium account HK$'000	Capital reserve HK$'000	Fixed asset revaluation reserve HK$'000	Exchange reserve HK$'000	Retained profits HK$'000	Sub-total HK$'000	Minority interests HK$'000	Total HK$'000
At 1 July 2004, as previously reported as equity	47,341	106	5,958	–	305,173	358,578	–	358,578
At 1 July 2004, as previously reported as minority interests	–	–	–	–	–	–	28,284	28,284
Effect of adopting Hong Kong Accounting Standard 17	–	–	(5,958)	–	(4,242)	(10,200)	(1,133)	(11,333)
At 1 July 2004, as restated	47,341	106	–	–	300,931	348,378	27,151	375,529
Rights issue	140,128	–	–	–	–	140,128	–	140,128
Rights issue expenses	(4,062)	–	–	–	–	(4,062)	–	(4,062)
Capital contributed by minority interests	–	–	–	–	–	–	38,233	38,233
Profit for the period	–	–	–	–	40,318	40,318	7,347	47,665
At 31 December 2004, as restated	183,407	106	–	–	341,249	524,762	72,731	597,493

Condensed Consolidated Cash Flow Statement

	Unaudited six months ended 31 December	
	2005	2004
	HK$'000	HK$'000
NET CASH INFLOW FROM OPERATING ACTIVITIES	**205,163**	28,344
NET CASH OUTFLOW FROM INVESTING ACTIVITIES	**(74,212)**	(89,580)
NET CASH INFLOW FROM FINANCING ACTIVITIES	**69,989**	140,898
NET INCREASE IN CASH AND CASH EQUIVALENTS	**200,940**	79,662
CASH AND CASH EQUIVALENTS AT THE BEGINNING OF PERIOD	**143,057**	83,636
CASH AND CASH EQUIVALENTS AT THE END OF PERIOD	**343,997**	163,298
ANALYSIS OF BALANCES OF CASH AND CASH EQUIVALENTS		
Cash and bank balances	**343,997**	163,298

Notes to Condensed Consolidated Financial Statements

1. Basis of Preparation and Accounting Policies

These unaudited condensed consolidated financial statements have been prepared in accordance with Hong Kong Accounting Standard ("HKAS") 34 "Interim Financial Reporting" issued by the Hong Kong Institute of Certified Public Accountants.

These condensed consolidated financial statements should be read in conjunction with 2005 annual financial statements.

The accounting policies and methods of computation used in the preparation of these condensed consolidated financial statements are consistent with those used in the annual financial statements for the year ended 30 June 2005 except that the Group has changed certain of its accounting policies following its adoption of new/ revised Hong Kong Financial Reporting Standards and Hong Kong Accounting Standards ("HKFRS") which are effective for accounting periods commencing on or after 1 January 2005.

The changes to the accounting policies of the Group under the new HKFRS do not have a material impact as a whole and particulars of these changes are set out in note 2 below.

2. Changes in Accounting Policies

In 2005, the Group adopted the following new/revised standards of HKFRS:

HKAS 1	Presentation of Financial Statements
HKAS 2	Inventories
HKAS 7	Cash Flow Statements
HKAS 8	Accounting Policies, Changes in Accounting Estimates and Errors
HKAS 10	Events after the Balance Sheet Date
HKAS 16	Property, Plant and Equipment
HKAS 17	Leases
HKAS 21	The Effects of Changes in Foreign Exchange Rates
HKAS 23	Borrowing Costs
HKAS 24	Related Party Disclosures
HKAS 27	Consolidated and Separate Financial Statements
HKAS 32	Financial Instruments: Disclosures and Presentation
HKAS 33	Earnings per Share
HKAS 36	Impairment of Assets
HKAS 38	Intangible Assets
HKAS 39	Financial Instruments: Recognition and Measurement
HKAS – Int 12	Scope of HKAS – Int 12 consolidation – Special Purpose Entities
HKFRS 2	Share-based Payments

2. Changes in Accounting Policies (Cont'd)

HKAS 1 has affected the presentation of minority interests and other disclosures.

The adoption of HKAS 17 has resulted in a change in the accounting policy relating to the leasehold land. Leasehold land and buildings were previously carried at cost or valuation less accumulated depreciation. In accordance with the provisions of HKAS 17, a lease of land and building should be split into a lease of land and a lease of building in proportion to the relative fair values of the leasehold interests in the land element and the building element of the lease at the inception of the lease. Land use rights are expensed in the income statement on a straight-line basis over the period of the lease. HKAS 17 has been applied retrospectively.

The adoption of HKFRS 2 has resulted in a change in the accounting policy for share-based payments. Until 30 June 2005, the provision of share options to employees did not result in an expense in the income statement. Effective on 1 July 2005, the Group expenses the cost of share options in the income statement. As a transitional provision, the cost of share options granted after 7 November 2002 and had not yet vested on 30 June 2005 was expensed retrospectively in the income statement of the respective periods. Because there were no unvested share options at 1 July 2005 and no share options have been granted during the Period, the adoption of HKFRS 2 has had no impact on the Group's results for the current or prior accounting periods.

The adoption of other new/revised HKFRS did not result in substantial changes to the Group's accounting policies.

3. Turnover

Turnover represents the net invoiced value of goods sold, after allowances for returns and trade discounts, and after eliminations of all significant intra-Group transactions during the Period.

4. Segment Information

Segment information is presented by way of two segment formats: (i) on a primary segment reporting basis, by business segment; and (ii) on a secondary segment reporting basis, by geographical segment.

(i) Business segments

The following table presents revenue and results information for the Group's business segments:

	Manufacture and sale of											
	Lubricants		Anti-corrosive coatings		Additives		Vinyl acetate		Polyvinyl-chloride		Consolidated	
	2005 HK$'000	2004 HK$'000	2005 HK$'000	2004 HK$'000	2005 HK$'000	2004 HK$'000	2005 HK$'000	2004 HK$'000	2005 HK$'000	2004 HK$'000	2005 HK$'000	2004 HK$'000
Segment revenue:												
Sales to external customers	122,263	175,442	77,472	107,486	1,219	1,974	91,280	15,726	51,719	–	343,953	300,628
Segment results	13,509	31,872	12,544	25,004	169	518	28,502	2,454	5,785	–	60,509	59,848
Unallocated revenue											1,611	4,603
Unallocated expenses											(4,447)	(7,608)
Profit from operating activities											57,673	56,843
Finance costs											(205)	(526)
Profit before tax											57,468	56,317
Tax											(3,898)	(8,652)
Profit for the period											53,570	47,665
Attributable to:												
Equity holders of the Company											40,700	40,318
Minority interests											12,870	7,347
											53,570	47,665

4. Segment Information (Cont'd)

(ii) Geographical segments

All of the Group's revenue, results, assets and liabilities are derived from customers in the People's Republic of China (the "PRC" or "China") and accordingly, no further detailed analysis of the Group's geographical segments is presented.

5. Profit from Operating Activities

The Group's profit from operating activities is arrived at after charging/(crediting):

	Six months ended 31 December	
	2005	2004
	HK$'000	HK$'000
Cost of inventories sold	**266,684**	226,373
Depreciation	**2,520**	1,568
Amortisation of land use rights	**319**	77
Amortisation of other assets	**174**	173
Loss on disposal of an investment property	**–**	70
Interest income	**(863)**	(63)
Net rental income	**–**	(20)

6. Tax

	Six months ended 31 December	
	2005	2004
	HK$'000	HK$'000
Current Period provision:		
Hong Kong	**–**	–
Elsewhere in the PRC	**3,898**	8,652
Tax charge for the Period	**3,898**	8,652

6. Tax (Cont'd)

No provision for Hong Kong profits tax has been made as the Group did not generate any assessable profits arising in Hong Kong during the Period (2004: Nil). Taxes on profits assessable elsewhere have been calculated at the rates of tax prevailing in the jurisdictions in which the Group operates, based on existing legislation, interpretations and practices in respect thereof.

According to the Income Tax Law of the PRC, Daqing Black Bird Chemical Co., Ltd. ("Daqing Black Bird"), a subsidiary of the Company, is subject to an income tax rate of 15%, being the preferential tax rate applicable to Daqing Black Bird operating in one of the high and new technology industrial development zones of the PRC.

Mudanjiang Dongbei Chemical Engineering Company Limited ("Mudanjiang Dongbei Chemical"), a subsidiary of the Company, was exempt from the income tax of the PRC for two years starting from the first profitable year of its operations, i.e., from 1 January 2004 to 31 December 2005. Mudanjiang Dongbei Chemical is also entitled to a 50% relief from the income tax of the PRC for the following three years, i.e., from 1 January 2006 to 31 December 2008. Upon expiry of the tax relief period, Mudanjiang Dongbei Chemical will be subject to an income tax rate of 33%.

Mundanjiang Dongbei Gaoxin Chemical Company Limited ("Mudanjiang Dongbei Gaoxin"), a subsidiary of the Company, was exempted from the income tax of the PRC for two years starting from the first profitable year of its operations, i.e., from 1 January 2005 to 31 December 2006. Mudanjiang Dongbei Gaoxin is also entitled to a 50% relief from the income tax of the PRC for the following three years, i.e., from 1 January 2007 to 31 December 2009. Upon expiry of the tax relief period, Mudanjiang Dongbei Gaoxin will be subject to an income tax rate of 33%.

The provision for income tax of the other subsidiaries operating in the PRC have been calculated at the rate of 33%, based on existing legislation, interpretations and practices in respect thereof.

A reconciliation of the tax expense applicable to profit/(loss) before tax using the statutory rates for the countries in which the Company and its subsidiaries are domiciled to the tax expense at the effective tax rates, and a reconciliation of the applicable rates (i.e., the statutory tax rates) to the effective tax rates, are as follows:

	Hong Kong		The PRC		Total	
	2005 HK$'000	2005 %	2005 HK$'000	2005 %	2005 HK$'000	2005 %
Profit/(loss) before tax	(4,214)		61,682		57,468	
Tax at the statutory tax rate	(737)	17.5	20,355	33.0	19,618	34.1
Preferential statutory tax rate offered	–	–	(4,678)	(7.6)	(4,678)	(8.1)
Income tax exempted	–	–	(11,779)	(19.1)	(11,779)	(20.5)
Income not subject to tax	(2)	–	–	–	(2)	–
Expenses not deductible for tax	739	(17.5)	–	–	739	1.3
Tax charge at the Group's effective tax rate	–	–	3,898	6.3	3,898	6.8

6. Tax (Cont'd)

	Hong Kong		The PRC		Total	
	2004	2004	2004	2004	2004	2004
	HK$'000	%	HK$'000	%	HK$'000	%
Profit/(loss) before tax	(7,610)		63,927		56,317	
Tax at the statutory tax rate	(1,332)	17.5	21,096	33.0	19,764	35.1
Preferential statutory tax rate offered	–	–	(12,522)	(19.6)	(12,522)	(22.2)
Lower tax rate for tax relief granted	–	–	78	0.1	78	0.1
Income not subject to tax	(1)	–	–	–	(1)	–
Expenses not deductible for tax	1,333	(17.5)	–	–	1,333	2.4
Tax charge at the Group's effective tax rate	–	–	8,652	13.5	8,652	15.4

Deferred tax has not been provided as the Group did not have any significant unprovided deferred tax liabilities during the Period (2004: Nil).

7. Earning Per Share

The calculation of basic earnings per share is based on the Group's net profit from ordinary activities attributable to shareholders for the Period of approximately HK$40,700,000 (2004: HK$40,318,000), and the weighted average of 1,659,740,217 (2004: 1,255,006,957) ordinary shares in issue during the Period.

No diluted earnings per share was presented for the Period as there were no potential ordinary shares in issue during the Period.

8. Capital Expenditure

During the Period, the additions to fixed assets including the construction in progress in the PRC were approximately HK$120.0 million (2004: HK$89.6 million).

9. Other Assets

	Six months ended 31 December 2005 HK$'000	Year ended 30 June 2005 HK$'000
Net book value at the beginning of the period/year	**13,061**	13,407
Amortisation provided for the period/year	**174**	346
Net book value at the end of the period/year	**12,887**	13,061

The Group is in the process of obtaining land use rights certificates together with the related building ownership certificates for certain of its leasehold land and buildings situated in Daqing, Heilongjiang Province, the PRC.

In the opinion of the Directors, the Group has obtained the right to use the land and the related improvements legally. Once the Group obtains all of the relevant certificates, the Group will have the right to assign, lease or mortgage the land and its improvements.

10. Intangible Assets

	Six months ended 31 December 2005 HK$'000	Year ended 30 June 2005 HK$'000
Net book value at the beginning of the period/year	**10,094**	–
Additions	**–**	10,094
Amortisation provided for the period/year	**–**	–
Net book value at the end of the period/year	**10,094**	10,094

11. Deferred Development Costs

In the opinion of the Directors, no amortisation was provided for the Period as the products are still at the development stage and are not yet available for use to the Group.

12. Deposits Paid for the Establishment of a Proposed Joint Venture

	31 December 2005 HK$'000	30 June 2005 HK$'000
Huludao BoHai Shipping Black Bird Painting Co., Ltd. ("Huludao Subsidiary")	**5,140**	5,140

On 20 January 2003, the Group entered into an agreement with an independent third party to establish the Huludao Subsidiary, a Sino-foreign equity joint venture in the PRC (the "Huludao Agreement"). Pursuant to the Huludao Agreement, the Group would have a 65% equity interest in the Huludao Subsidiary. The principal activities of the Huludao Subsidiary are the manufacture and sale of anti-corrosive coatings. The proposed total investment in the Huludao Subsidiary is RMB20,000,000 (equivalent to approximately HK$18,692,000), of which RMB8,000,000 (equivalent to approximately HK$7,477,000) is the proposed registered capital. As at 31 December 2005, the Group had paid HK$5,140,000 as a partial contribution for its commitment, totalling HK$12,149,000, of the proposed total investment of the Huludao Subsidiary. The remaining contribution required from the Group to fulfil the proposed total investment in the Huludao Subsidiary of approximately HK$7,009,000 is disclosed as a capital commitment in note 20(b) to the Interim Financial Statements.

13. Amount Paid for the Acquisition of Fixed Assets and Land Use Rights

	31 December 2005 HK$'000	30 June 2005 HK$'000
Acquisition cost	**–**	73,551

As at 31 December 2005, the Group had a commitment, which was authorised by the directors of the Company but not contracted for, to make a payment of RMB20,000,000 (equivalent to approximately HK$18,692,000) as development funds to an account designated by the 牡丹江市經濟委員會(Mudanjiang City Economic Committee) for use in technological improvements and environmental protection in respect of the operation of the Mudanjiang Dongbei Gaoxin.

14. Trade Receivables

The Group normally allows credit terms to established customers ranging from 30 to 150 days.

An aged analysis of the trade receivables as at the balance sheet date, based on the invoice date, is as follows:

	31 December 2005 HK$'000	30 June 2005 HK$'000
Within 30 days	**73,271**	80,811
31 – 60 days	**37,876**	61,930
61 – 90 days	**16,867**	21,846
91 – 120 days	**6,483**	12,247
121 – 365 days	**–**	2
	134,497	176,836

Included in the Group's trade receivables as at 31 December 2005 is an amount due from the joint venture partner of the proposed Sino-foreign equity joint venture of approximately HK$8,600,000 (30 June 2005: HK$10,764,000), which is repayable on credit terms similar to those offered to other customers of the Group.

15. Trade Payables

The Group normally obtains credit terms ranging from 30 to 120 days from its suppliers.

An aged analysis of the trade payables as at the balance sheet date, based on the invoice date, is as follows:

	31 December 2005 HK$'000	30 June 2005 HK$'000
Within 30 days	**19,133**	8,173
31 – 60 days	**1,234**	–
61 – 90 days	**97**	–
Over 90 days	**–**	25
	20,464	8,198

16. Share Capital

Shares

	31 December 2005 HK$'000	30 June 2005 HK$'000
Authorised:		
2,000,000,000 ordinary shares of HK$0.01 each	**20,000**	20,000
Issued and fully paid:		
1,664,410,000 (30 June 2005: 1,449,600,000) ordinary shares of HK$0.01 each	**16,644**	14,496

16. Share Capital (Cont'd)

A summary of the movements in the issued share capital of the Company during the Period is as follows:

	Note	Number of ordinary shares issued '000	Par value HK$'000
At 1 July 2004		966,400	9,664
Rights issue		483,200	4,832
At 30 June 2005		1,449,600	14,496
Issue of new shares to a substantial shareholder	(a)	214,810	2,148
At 31 December 2005		1,664,410	16,644

Note:

(a) On 22 June 2005, Master Oriental Limited, a substantial shareholder of the Company, placed 214,810,000 ordinary shares of HK$0.01 each in the Company to independent third parties at a price of HK$0.455 each. Master Oriental Limited then subscribed for a total of 214,810,000 new shares of HK$0.01 each in the Company at HK$0.455 per share. The subscription was completed on 4 July 2005 and proceeds of approximately HK$96,000,000 net of expense were raised by the Company. The excess of the cash consideration received over the nominal value of the shares issued, in the amount of approximately HK$93,840,000, net of expenses, was credited to the share premium account.

(b) Subsequent to the Period end, on 10 January 2006 and 8 February 2006, the Company had granted a total of 94,100,000 new share options of which 27,540,000 were granted to two executive directors; 49,920,000 were granted to employees and 16,640,000 were granted to a business associate.

As at the date of this report, 80,330,000 of above-mentioned share options had been exercised at the subscription price on the range of HK$0.363 to HK$0.455 per share, including of which 13,770,000 of share options was exercised by Mr. Peng Zhanrong, executive director of the Company, at HK$0.363 each. The proceeds from allotment of shares received by the Company was approximately HK$33,752,000.

On 8 February 2006, Mr Chiau Che Kong, executive director of the Company, exercised 6,000,000 share options at the subscription price of HK$0.47 each and the total proceeds received by the Company was HK$2,820,000.

17. Share Option Schemes

Share options are granted to directors, executives and employees under the Share Option Scheme which became effective on 18 November 2002 for a period of 10 years. The exercise period of the share options granted is determinable by the directors and in any event not later than 10 years from the date of grant of share options, subject to the provisions for early termination thereof.

The following share options were outstanding during the Period:

	Number of share options								Price of Company's shares***	
Category or name of participant	At 1 July 2005	Granted during the Period	Exercised during the Period	Lapsed during the Period	At 31 December 2005	Date of grant of share options *	Exercise period of share options	Exercise price of share options** HK$	At grant date of options HK$	At exercise date of options HK$
Mr. Chiau Che Kong	6,000,000	-	-	-	6,000,000	1 April 2004	7 April 2004 to 6 April 2007	0.47	0.475	N/A
Other employee	7,000,000	-	-	-	7,000,000	1 April 2004	7 April 2004 to 6 April 2007	0.47	0.475	N/A
Total	13,000,000	-	-	-	13,000,000					

* The vesting period of the share options is from the date of the grant until the commencement of the exercise period.

** The exercise price of the share options is subject to adjustment in the case of a rights or bonus issue, or other similar changes in the Company's share capital.

*** The price of the Company's shares disclosed as at the date of the grant of the share options is the average closing price as quoted on the Stock Exchange of Hong Kong Limited for the five trading days immediately preceding to the date of the grant of the share options.

18. Related Party Transactions

There is no significant related party transaction during the Period (2004: Nil).

19. Contingent Liabilities

The Group did not have any significant contingent liabilities as at the balance sheet date (30 June 2005: Nil).

20. Commitments

(a) Commitments under operating leases

The Group leases certain leasehold land and buildings under operating lease arrangements. The original lease terms for these leasehold land and buildings range from one to ten years.

At 31 December 2005, the Group had total future minimum lease payments under non-cancellable operating leases for leasehold land and buildings falling due as follows:

	31 December 2005 HK$'000	30 June 2005 HK$'000
Within one year	**1,200**	1,358
In the second to fifth years, inclusive	**4,486**	4,486
Beyond five years	**2,056**	2,617
	7,742	8,461

The Company did not have any operating lease arrangements as at 31 December 2005 (30 June 2005: Nil).

(b) Capital commitments

At the balance sheet date, the Group had the following outstanding capital commitments:

	31 December 2005 HK$'000	30 June 2005 HK$'000
Contracted, but not provided for:		
(a) Leasehold buildings and plant under construction	**3,738**	79,159
(b) Contribution to PRC joint ventures (note 12)	**7,009**	7,009
(c) Development costs	**–**	1,963
	10,747	88,131

INTERIM DIVIDEND

The Directors have resolved that no interim dividend will be declared in respect of the Period (2004: Nil).

MANAGEMENT DISCUSSION AND ANALYSIS

Business Review

During the Period, the high international crude oil price and the lack of global oil refining facilities have resulted in acute shortage and dramatic escalations of the price of primary petrochemical related product ingredients around the world which was rarely seen in the past several decades. The management has promptly responded to the rapidly changing market environment, but was only able to transfer a small part of the significant cost increment to market due to the extremely fierce competition within the industry.

As a result, the Group recorded a turnover of HK$343.9 million for the Period, representing an increase of 14.4% over the corresponding period of the previous year, while the profit attributable to shareholders was HK$40.7 million, representing an increase of 0.9% over the corresponding period of the previous year.

During the Period, amid the formidable external operating environment, lubricants and coating segment achieved turnovers of HK$122.3 million and HK$77.5 million, respectively, representing a decrease of 30.3% and 27.9% over the corresponding period of the previous year. Operating profits were HK$13.5 million and HK$12.5 million, respectively during the period, representing a decrease of 57.6% and 49.8% over the corresponding period of the previous year. As primary lubricant and coating ingredient prices generally lag behind crude oil prices and still surging recently, it is expected that the lubricants and coating segment will experience tougher situation in the second half year. The Group will radically reform the lubricants and coating segment with a series of measures and appropriate modification in areas including aggressive promotion of brand and marketing, enhancement of quality and service standard and optimization of ancillary facilities to increase its competitiveness and enlarge its market share.

Facing increasing competition in petrochemical related products market, the Group is proactively improving the production technology of petrochemical related products in order to reduce costs, as well as devoting more efforts in the development of coal related chemical sector. Due to the continuous high pricing of crude oils, coal related chemical production line is able to maintain its cost competitiveness.

The Group commenced the development of coal related chemical sector since 2004, with vinyl acetate being its first coal related chemical project. After operating for over one year, the production and sales of vinyl acetate has stabilised and generated remarkable profits for the Group. During the Period, turnover was HK$91.3 million, representing a significant increase of 93.5% (based on monthly proportional adjustment: two months in last year and six months in this year) over the corresponding period of the previous year. Operating profit was HK$28.5 million, representing a significant increase of 287.2% (based on monthly proportional adjustment: two months in last year and six months in this year) over the corresponding period of the previous year.

The Group continued to step up the development of coal related chemical sector with PVC as its second coal related chemical project. The Group successfully acquired assets including the land, plants and production facilities of Madanjiang PVC Factory through a tender in May 2005. On 27 September 2005, the Group formally took over the assets and related operations of Mudanjiang PVC Factory. After operating for almost six months, the PVC production and sales segment is now on track and started to contribute profits to the Group. During the Period, the PVC segment recorded a turnover of HK$51.7 million and an operating profit of HK$5.8 million, respectively. Within the short period of six months after taking over the PVC Factory, the Group successfully increased the effectiveness of this production line by reducing the consumption proportion of raw materials.

Net Proceeds Raised by Placement of existing shares and Subscription of new shares

The net proceeds raised by the placement of existing shares and subscription of new shares of the Company by a substantial shareholder was about HK$96,000,000, of which HK$56,000,000 was utilized by the Group at the date of this report with HK$40,000,000 still being unused. During the Period, approximately HK$30,000,000 was injected into Mudanjiang Dongbei Gaoxin (of which approximately HK$10,000,000 for upgrading and refurbishment of the production facilities of the PVC business and approximately HK$20,000,000 for working capital of the PVC business); and about HK$26,000,000 was used as working capital of the Group.

Liquidity and Financial Ratios

As at 31 December 2005, the Group had total assets of approximately HK$969.0 million (30 June 2005: HK$762.4 million) which were financed by current liabilities of approximately HK$141.6 million (30 June 2005: HK$84.6 million), nil non-current liabilities (30 June 2005: Nil), minority interests of approximately HK$99.2 million (30 June 2005: HK$86.4 million) and shareholders equity of approximately HK$728.1 million (30 June 2005: HK$591.4 million).

At 31 December 2005, the current assets of the Group amounted to approximately HK$602.6 million (30 June 2005: HK$470.2 million) comprising inventories of approximately HK$86.4 million (30 June 2005: HK$125.9 million), trade receivables of approximately HK$134.5 million (30 June 2005: HK$176.8 million), prepayment, deposits and other receivables of approximately HK$37.7 million (30 June 2005: HK$24.5 million), cash and cash equivalents of approximately HK$344.0 million (30 June 2005: HK$143.1 million).

At 31 December 2005, the Group's current ratio (current assets/current liabilities), quick ratio ((current assets – inventory)/(current liabilities)), gearing ratio (total debts/total assets) and debts to equity ratio (total debts/shareholders' equity) of the Group were approximately 4.2 (30 June 2005: 5.6), 3.6 (30 June 2005: 4.1), 14.6% (30 June 2005: 11.1%) and 19.4% (30 June 2005: 14.3%), respectively. These changes reflected an improvement in the Group's structure of assets and liabilities.

As at 31 December 2005, the Group did not have any significant contingent liabilities.

Foreign Exchange Exposure

Although most of the operations were carried out in the PRC in which transactions were denominated in RMB, the Directors consider that the Group has no significant exposure to foreign exchange fluctuations in view of the stability of the RMB in recent years. The Directors also consider that there will be sufficient cash resources denominated in Hong Kong dollars for the repayment of borrowings and future dividends. During the Period under review, the Group did not use any financial instrument for hedging purposes and the Group did not have any hedging instrument outstanding as at 31 December 2005.

Number and Remuneration of Employees

At 31 December 2005, the Group had 840 full time employees in the PRC and Hong Kong. The Group recognizes the importance of human resources to its success. Remuneration is maintained at competitive levels with discretionary bonuses payable on a merit basis and in line with industry practice. Other staff benefits provided by the Group include mandatory provident fund, insurance schemes and performance related commissions.

During the Period under review, no share options were granted to any staff. At 31 December 2005, a total of 13,000,000 share options are outstanding with exercisable periods up to 6 April 2007 with exercise prices HK$0.47 per share.

Prospects

The Directors believe that moving towards coal related chemical sector is the right direction of the Group to achieve the goal of fast development and sustainable growth. The rapid growth in revenue from sales of our vinyl acetate, which adopts calcium carbide methodology (電石法化工工藝方法), has proven that our improved production technology in coal related chemical sector has cost advantage over our competitors which adopt acetylene methodology (乙炔法化工工藝方法) during sustained high crude oil price.

The Group's second move to the coal related chemical sector is the production of polyvinyl-chloride ("PVC"), which also adopts the calcium carbide methodology. The Directors believe that our expertise in the calcium carbide methodology will provide a strong base for enhancing the efficiency of PVC production. In addition, the upgrade of the existing production plant and equipment of PVC aiming to produce high grade PVC raw materials is running on schedule. The construction work of production plant and installation of machinery for producing high grade PVC raw materials is expected to commence later in the year.

Prospects (Cont'd)

With the global supply of petroleum remains in shortage, China continues to increase import annually given the lack of local production, the prices of petrochemical raw materials fluctuate significantly. On the other hand, China is extremely rich in coal reserve and the price of coal is relatively stable comparing to the price of crude oil. Directors believes that the coal related chemical sector will become better and better.

Looking ahead, the Group will endeavor to explore more opportunities in the coal related chemical field. The Group is constantly seeking for both upstream and downstream potential merger and acquisitions opportunities in the coal related chemical sector. The Group is well prepared to increase investments to develop a chain of coal related chemical production platforms in northeastern region of the PRC.

DISCLOSURE OF ADDITIONAL INFORMATION

Directors' Interests or Short Positions in Shares and Underlying Shares

As at 31 December 2005, none of the directors and chief executive of the Company had any interests or short positions in the shares or underlying shares or, as the case may be, the percentage in the equity interest and debentures of the Company or its associated corporations (within the meaning of the Securities and Futures Ordinance (Chapter 571 of the Laws of Hong Kong) (the "SFO")) which were 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 and short positions which he was taken or deemed to have under such provisions of the SFO), or which were required, pursuant to section 352 of the SFO, to be entered in the register maintained by the Company referred to therein, or which were required, pursuant to the Model Code for Securities Transactions by Directors of Listed Companies contained in the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited ("Listing Rules"), to be notified to the Company and the Stock Exchange.

DIRECTORS' RIGHTS TO ACQUIRE SHARES OR DEBENTURES

Apart from as disclosed in the share option schemes disclosures in note 17 to the Interim Financial Statements, at no time during the Period were rights to acquire benefits by means of the acquisition of shares in or debentures of the Company granted to any director or their respective spouse or children under 18 years of age, or were any such rights exercised by them; or was the Company or any of its subsidiaries a party to any arrangement to enable the directors to acquire such rights in any other body corporate.

INTERESTS OF SHAREHOLDERS DISCLOSABLE UNDER THE SFO

As far as the directors of the Company are aware, as at 31 December 2005, the following persons, other than a director or chief executive of the Company, had an interest or a short position in the shares and underlying shares in the Company as recorded in the register required to be kept under section 336 of the SFO:

Name of shareholder	Number of ordinary shares	Nature of interest	Approximate percentage of interest
Master Oriental Limited ("Master Oriental")	Long position 263,340,000 (note 1)	Corporate interests	15.82% (note 1)
Heng Tai Consumables Group Limited ("Heng Tai")	Long position 263,340,000 (note 1)	Corporate interests	15.82% (note 1)
Chan Yuen Tung	Long position 197,055,488 (note 2)	Beneficial owner	11.84%

Notes:

1. Master Oriental, a company incorporated in Hong Kong, is a wholly-owned subsidiary of Heng Tai, a company incorporated in the Cayman Islands whose shares are listed on the Stock Exchange. In accordance with the SFO, Heng Tai is deemed to be interested in the shares held by Master Oriental in the Company. On 22 June 2005, Heng Tai and the Company jointly announced that, pursuant to a placing agreement and a top-up subscription agreement, Master Oriental would sell 214,810,000 existing shares of the Company (the "Placing") and subscribe for 214,810,000 new shares of the Company (the "Subscription"), respectively. Upon completion of the placing and the subscription Master Oriental held 15.82% in the issued share capital of the Company.

2. To the best knowledge of the directors, Mr. Chan Yuen Tung is not a connected person of the Company and is not connected with any of the directors, chief executive and substantial shareholders of the Company or any of its subsidiaries or their respective associates (as defined in the Listing Rules).

Save as disclosed above, as at 31 December 2005, no other person had an interest or a short position in the shares and underlying shares in the Company as recorded in the register required to be kept under section 336 of the SFO.

SUFFICIENCY OF PUBLIC FLOAT

Based on the information that is publicly available to the Company and within the knowledge of the directors as at the date of this report, there is sufficient public float of more than 25% of the Company's shares in the market as required under the Listing Rules.

PURCHASE, REDEMPTION OR SALE OF LISTED SECURITIES OF THE COMPANY

Neither the Company, nor any of its subsidiaries purchased, redeemed or sold any of the Company's listed securities during the Period.

PRE-EMPTIVE RIGHTS

There are no provisions for pre-emptive rights under the Company's articles of association or the Companies Law (Law 3 of 1961, as consolidated and revised) of the Cayman Islands, being the jurisdiction in which the Company was incorporated, which would oblige the Company to offer new shares on a pro rata basis to the existing shareholders.

MODEL CODE FOR SECURITIES TRANSACTIONS

The Company has adopted the Model Code for Securities Transactions by Directors of Listed Issuer as set out in Appendix 10 of the Listing Rules (the "Model Code") as its own code of conduct regarding Directors' securities trading. Having made specific enquiry of all Directors of the Company, all of them confirmed that they have complied with the required standard of dealings as set out in the Model Code during the Period.

CORPORATE GOVERNANCE

Code on Corporate Governance Practices

In the opinion of the directors, the Company has during the Period complied with the Code on Corporate Governance Practices as set out in Appendix 14 of the Listing Rules, except for the following aspects:

1. Under code provision A.2.1, the roles of chairman and chief executive officer should be separate and should not be performed by the same individual. Currently, both roles are being performed by Ms. Chan Yuk Foebe, the Chairman. In the opinion of directors, given the scale of operation and the size of the Group, the present arrangement is beneficial to the Company and the shareholders as a whole.

2. Certain independent non-executive directors are not appointed for a specific term but are subject to rotation and re-election at the annual general meeting in accordance with the Company's articles and association.

AUDIT COMMITTEE

The Company set up an audit committee (the "Audit Committee") on 8 April 2001, with written terms of reference, for the purposes of reviewing and providing supervision over the Group's financial reporting process and internal control systems. The Audit Committee comprises the three independent non-executive directors of the Company, namely, Mr. Ma Wing Yun Bryan, Mr. Meng Fanxi and Mr. Yau Chung Hong. The Audit committee has reviewed with the management the accounting principles and practices adopted by the Group and discussed auditing, internal control and financial reporting matters including the review of the unaudited interim results of the Company for the six months ended 31 December 2005.

REMUNERATION COMMITTEE

A remuneration committee (the "Remuneration Committee") was established on 1 July, 2005 with specific written terms of reference which deal clearly with its authority and duties. The Remuneration Committee, currently comprises Ms. Chan Yuk Foebe (Chairman of the Board), Mr. Ma Wing Yun Bryan and Mr. Yau Chung Hong (both are independent non-executive directors), is responsible for advising the Board on the remuneration policy and framework for all remuneration of the Company's directors and senior management, as well as reviewing and determining the remuneration packages of directors and senior management with reference to the Company's objectives from time to time.

By order of the Board
Chan Yuk Foebe
Chairman

Hong Kong, 23 March 2006