



山東墨龍石油機械股份有限公司
Shandong Molong Petroleum Machinery Company Limited*

(a Sino-foreign joint stock limited company incorporated in the People's Republic of China with limited liability)

(Stock Code: 568)

2007

INTERIM REPORT

The Stock Exchange takes no responsibility for the contents of this report, makes no representation as to its accuracy or completeness and expressly disclaims any liability whatsoever for any loss howsoever arising from or in reliance upon the whole or any part of the contents of this report.

This report, for which the 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 Stock Exchange of Hong Kong Limited (the "Listing Rules") for the purpose of giving information with regard to the Company. The directors of 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.

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HIGHLIGHTS

- Achieved a revenue of approximately RMB806,411,000 for the six months ended 30 June 2007 which represents a growth of approximately 81.9% as compared to RMB443,398,000 that of the same period last year.
- The net profit increased by approximately 79.5% to approximately RMB90,532,000 as compared to RMB50,424,000 that of the same period last year.
- Earnings per share of the Group were approximately RMB13.97 cents for the six months ended 30 June 2007. (*Refer to notes 7 and 17*)
- The board of directors of the Company does not recommend the payment of an interim dividend for the six months ended 30 June 2007.

The board of directors of the Company (the "Board") is pleased to announce the unaudited results of Shandong Molong Petroleum Machinery Company Limited and its subsidiaries (collectively, the "Group") for the six months ended 30 June 2007 (the "period under review").

UNAUDITED CONDENSED CONSOLIDATED PROFIT AND LOSS ACCOUNT

For the six months ended 30 June 2007

The unaudited results of the Group for the six months ended 30 June 2007 together with the unaudited comparative figures for the corresponding period in 2006 are as follows:

	Notes	Six months ended 30 June	
		2007	2006
		RMB'000	RMB'000
Revenue	(3)	806,411	443,398
Cost of sales		(640,854)	(334,778)
Gross profit		165,557	108,620
Other income and gains	(4)	14,062	8,999
Selling and distribution costs		(17,943)	(13,142)
Administrative expenses		(19,594)	(14,693)
Other operating expenses		(9,850)	(9,095)
Finance costs		(12,044)	(3,803)
Profit before tax	(5)	120,188	76,886
Tax	(6)	(29,196)	(25,374)
Profit for the period		90,992	51,512
Attributable to:			
Shareholders of the Company		90,532	50,424
Minority interests		460	1,088
		90,992	51,512
Dividends			
Interim dividend per share (RMB cents)		Nil	1.5
Earnings per share attributable to ordinary equity holders of the parent - basic (RMB cents)	(7), (17)	13.97	7.78

UNAUDITED CONDENSED CONSOLIDATED BALANCE SHEET

As at 30 June 2007

		As at 30 June 2007 RMB'000 (unaudited)	As at 31 December 2006 RMB'000 (audited)
	Notes		
NON-CURRENT ASSETS			
Property, plant and equipment		608,167	505,155
Investment properties		9,317	7,664
Prepaid land lease payments		21,199	19,709
Intangible assets		552	253
Available-for-sale equity investment		9,526	50
Deferred tax assets		6,053	8,942
		<hr/>	<hr/>
Total non-current assets		654,814	541,773
		<hr/>	<hr/>
CURRENT ASSETS			
4 Inventories	(8)	531,606	447,579
Trade receivables	(9)	358,830	169,878
Bills receivables		5,000	3,786
Prepayments, deposits and other receivables		100,344	37,808
Pledged deposits		243,298	219,254
Cash and bank balances		41,594	34,138
		<hr/>	<hr/>
Total current assets		1,280,672	912,443
		<hr/>	<hr/>

		As at 30 June 2007 RMB'000 (unaudited)	As at 31 December 2006 RMB'000 (audited)
	Notes		
CURRENT LIABILITIES			
Trade and bills payables	(10)	762,997	611,721
Other payables and accruals		79,591	59,024
Tax payable		25,836	18,740
Interest-bearing bank loans		281,586	135,000
Due to related parties		65,674	22,966
		<hr/> 1,215,684 <hr/>	<hr/> 847,451 <hr/>
NET CURRENT ASSETS		64,988	64,992
		<hr/>	<hr/>
TOTAL ASSETS LESS CURRENT LIABILITIES			
		719,802	606,765
		<hr/>	<hr/>
NON - CURRENT LIABILITIES			
Interest-bearing bank loans		100,000	70,000
		<hr/>	<hr/>
NET ASSETS		619,802	536,765
		<hr/> <hr/>	<hr/> <hr/>
EQUITY			
EQUITY ATTRIBUTABLE TO EQUITY HOLDERS OF THE PARENT			
Issued capital		64,800	64,800
Reserves		541,123	450,844
Proposed interim/final dividend		—	12,960
		<hr/>	<hr/>
		605,923	528,604
MINORITY INTERESTS		13,879	8,161
		<hr/>	<hr/>
TOTAL EQUITY		619,802	536,765
		<hr/> <hr/>	<hr/> <hr/>

UNAUDITED CONDENSED CONSOLIDATED CASH FLOW STATEMENT

For the six months ended 30 June 2007 and 2006

	Six months ended 30 June	
	2007	2006
	RMB'000	RMB'000
Net cash inflow from operating activities	90,741	28,302
Net cash outflow from investment activities	(141,000)	(128,517)
Net cash inflow from financing activities	168,080	84,438
	<hr/>	<hr/>
Net increase/ (decrease) in cash and cash equivalents	117,821	(15,777)
Cash and cash equivalents at the beginning of the period	35,215	110,166
	<hr/>	<hr/>
Cash and cash equivalents at the end of the period	153,036	94,389
	<hr/> <hr/>	<hr/> <hr/>
Analysis of balances of cash and cash equivalents		
Cash and bank balances	41,594	43,774
Time deposits with original maturity of less than three months when acquired, pledged as security for bills payable	111,442	50,615
	<hr/>	<hr/>
	153,036	94,389
	<hr/> <hr/>	<hr/> <hr/>

UNAUDITED CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

For the six months ended 30 June 2007 and 2006

	Attributable to equity holders of the parent										
	Issued Share capital	Capital reserve	Statutory reserve fund	Statutory welfare fund	Retained profits	Exchange fluctuation reserve	Subtotal of reserves	Proposed of interim dividend	Total	Minority interests	Total equity
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
At 1 January 2006	64,800	177,712	23,965	11,982	120,700	—	334,359	11,016	410,175	4,891	415,066
Profit for the period	—	—	—	—	50,424	—	50,424	—	50,424	1,088	51,512
Dividend paid	—	—	—	—	—	—	—	(11,016)	(11,016)	—	(11,016)
Proposed dividend for the period	—	—	—	—	(9,720)	—	(9,720)	9,720	—	—	—
At 30 June 2006	<u>64,800</u>	<u>177,712</u>	<u>23,965</u>	<u>11,982</u>	<u>161,404</u>	<u>—</u>	<u>375,063</u>	<u>9,720</u>	<u>449,583</u>	<u>5,979</u>	<u>455,562</u>
At 1 January 2007	64,800	177,712	41,132	11,982	220,269	(251)	450,844	12,960	528,604	8,161	536,765
Net profit for the period	—	—	—	—	90,532	—	90,532	—	90,532	460	90,992
Exchange fluctuation	—	—	—	—	—	(253)	(253)	—	(253)	—	(253)
Dividend paid	—	—	—	—	—	—	—	(12,960)	(12,960)	—	(12,960)
Absorbed minority interests	—	—	—	—	—	—	—	—	—	12,600	12,600
Paid to minority share holders	—	—	—	—	—	—	—	—	—	(7,342)	(7,342)
At 30 June 2007	<u>64,800</u>	<u>177,712</u>	<u>41,132</u>	<u>11,982</u>	<u>310,801</u>	<u>(504)</u>	<u>541,123</u>	<u>—</u>	<u>605,923</u>	<u>13,879</u>	<u>619,802</u>

NOTES TO THE UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Amounts expressed in Renminbi unless otherwise stated)

1. General Information and Basis of Preparation

The interim financial statements were unaudited. The interim financial statements have been reviewed by the audit committee of the Company.

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 Growth Enterprise Market of The Stock Exchange of Hong Kong Limited (the "Stock Exchange") (the "GEM") on 15 April 2004. On 9 July 2004, the Company became a Sino-foreign joint stock limited company. The company migrated from the GEM to the Main Board of the Stock Exchange on 7 February 2007.

The unaudited financial statements of the Group have been prepared in accordance with Hong Kong Financial Reporting Standards ("HKFRSs") (which also include Hong Kong Accounting Standards ("HKASs") and Interpretations) issued by the Hong Kong Institute of Certified Public Accountants, accounting principles generally accepted in Hong Kong and the requirements of Appendix 16 of the Listing Rules.

The principal accounting policies used in the preparation of the unaudited financial statements are consistent with those used in the preparation of the Group's annual financial statements for the year ended 31 December 2006.

The Group has adopted the following standards that have been issued and effective for the periods beginning on or after 1 January 2007. The adoption of such standards did not have material effect on these financial statements.

HKAS 1 (Amendment)	Capital Disclosures
HKFRS 7	Financial Instruments - Disclosures
HK (IFRIC) – Int 8	Scope of HKFRS 2
HK (IFRIC) – Int 9	Reassessment of Embedded Derivatives
HK (IFRIC) – Int 10	Interim Financial Reporting and Impairment

The Group has not early adopted the following standards that have been issued but not yet effective. The adoption of such standards will not result in substantial changes to the Group's accounting policies.

HKFRS 8	Operating Segments
HK (IFRIC) – Int 11	HKFRS 2 – Group and Treasury Share Transactions
HK (IFRIC) – Int 12	Service Concession Arrangements

2. Changes in accounting estimates

In order to reflect more reasonably the estimated useful life of the casing production line equipment, the Company has adopted a change in depreciation years of casing production line equipment. The change in this accounting estimate resulted in an increase of approximately RMB2,941,000 in the net profit for the six months ended 30 June 2007.

3. Revenue & Segment Information

Revenue 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, Europe 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 sales of petroleum machinery.

	For the six months ended 30 June 2007				
	United States	Europe	Other countries	Consolidated	
	PRC	United States	Europe	Other countries	Consolidated
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)	(Unaudited)
Segment revenue					
Sales to external customers	382,218	141,046	155,855	127,292	806,411
Other revenue	1,585	—	—	—	1,585
Total revenue	<u>383,803</u>	<u>141,046</u>	<u>155,855</u>	<u>127,292</u>	<u>807,996</u>
Segment results	<u>53,631</u>	<u>28,292</u>	<u>31,985</u>	<u>29,895</u>	143,803
Unallocated income					12,477
Unallocated expenses					(24,048)
Finance costs					<u>(12,044)</u>
Profit before tax					120,188
Tax					<u>(29,196)</u>
Profit for the period					<u>90,992</u>

	For the six months ended 30 June 2006				
	PRC	United States	Europe	Other countries	Consolidated
	RMB'000 (Unaudited)	RMB'000 (Unaudited)	RMB'000 (Unaudited)	RMB'000 (Unaudited)	RMB'000 (Unaudited)
Segment revenue					
Sales to external customers	290,852	78,861	50,057	23,628	443,398
Other revenue	3,915	—	—	—	3,915
	<hr/>	<hr/>	<hr/>	<hr/>	<hr/>
Total revenue	294,767	78,861	50,057	23,628	447,313
	<hr/>	<hr/>	<hr/>	<hr/>	<hr/>
Segment results	64,200	18,865	10,691	5,016	98,772
	<hr/>	<hr/>	<hr/>	<hr/>	<hr/>
Unallocated income					5,084
Unallocated expenses					(23,167)
Finance costs					(3,803)
					<hr/>
Profit before tax					76,886
Tax					(25,374)
					<hr/>
Profit for the period					51,512
					<hr/>

4. **Other Income and Gains**

	Six months ended 30 June	
	2007	2006
	RMB'000	RMB'000
	(Unaudited)	(Unaudited)
Sale of materials	1,119	3,915
Subcontract income	138	258
Bank interest income	2,634	1,632
Government subsidies	6,745	—
VAT refund	1,252	2,794
Gross rental income	328	172
Others	1,846	228
	<hr/>	<hr/>
	14,062	8,999
	<hr/>	<hr/>

5. Profit Before Tax

The Group's profit before tax is arrived at after charging/(crediting):

	Six months ended 30 June	
	2007	2006
	RMB'000	RMB'000
	(Unaudited)	(Unaudited)
Cost of inventories sold	640,854	334,778
Depreciation	23,197	7,557
Provision against inventories	1,206	1,836
Provision for doubtful debts	1,469	(410)
Research and development costs	10,149	5,780
	<u>687,865</u>	<u>353,541</u>

6. Tax

The Company is located in Mainland China and as a result is subject to the PRC corporate income tax at a rate of 33% on its assessable profits. No provision for Hong Kong profits tax has been made as the Group did not generate any assessable profits in Hong Kong during the period.

Weifang Molong Drilling Equipment Company Limited, the Company's subsidiary, was approved by the Ministry of Civil Affairs of Shandong Province (山東省民政廳) as a welfare enterprise (民政福利企業) and hence was entitled to a full exemption from corporate income tax for years 2006 and January to June of 2007 respectively according to the tax document Cai Shui Zi [1994] No. 1 Notice about the several preferential policies on corporate income tax (《關於企業所得稅若干優惠政策的通知》).

	Six months ended 30 June	
	2007	2006
	RMB'000	RMB'000
	(Unaudited)	(Unaudited)
Current - PRC tax charge for the period	32,085	25,845
Deferred	(2,889)	(471)
	<u>29,196</u>	<u>25,374</u>

7. Earnings Per Share

The calculation of the basic earnings per share is based on the profit attributable to shareholders of approximately RMB90,532,000 for the six months ended 30 June 2007 (2006: RMB50,424,000) and on the weighted average number of approximately 647,998,000 shares (2006: 647,998,000 shares) in issue.

Diluted earnings per share is not presented for the six months ended 30 June 2006 and 2007 as there were no potential dilutive securities in existence during the relevant periods.

8. **Inventories**

	30 June 2007 RMB'000 (unaudited)	31 December 2006 RMB'000 (audited)
Raw materials	180,691	118,855
Work in progress	214,767	205,967
Finished goods	136,148	122,757
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Total	531,606	447,579
	<hr/> <hr/>	<hr/> <hr/>

None of the above balance was carried at net realisable value.

9. **Trade Receivables**

An aged analysis of the trade receivables as at 31 December 2006 and 30 June 2007, based on invoice date, and net of provisions, is as follows:

	30 June 2007 RMB'000 (unaudited)	31 December 2006 RMB'000 (audited)
Trade receivables		
Within three months	339,168	155,018
Three to six months	17,519	14,145
Six months to one year	2,143	715
	<hr/>	<hr/>
Total	358,830	169,878
	<hr/> <hr/>	<hr/> <hr/>

10. Trade and Bills Payables

An aged analysis of trade and bills payables as at 31 December 2006 and 30 June 2007, based on invoice date, is as follows:

	30 June 2007 RMB'000 (unaudited)	31 December 2006 RMB'000 (audited)
Trade and bill payables		
Within three months	476,082	362,625
Three to six months	246,158	234,639
Six months to one year	33,131	6,843
More than one year	7,626	7,614
	<hr/>	<hr/>
Total	762,997	611,721
	<hr/> <hr/>	<hr/> <hr/>

As at 30 June 2007, the Group's bills payables of RMB578,238,000 (31 December 2006: RMB485,481,000) were secured by the pledge of certain time deposits amounting to RMB243,298,000 (31 December 2006: RMB219,254,000). The payable are non-interest-bearing and are normally settled on terms of six months.

11. Capital Commitments

	30 June 2007 RMB'000 (unaudited)	31 December 2006 RMB'000 (audited)
Contracted, but not provided for:		
Land and buildings	—	6,147
Plant and machinery	117,924	46,292
	<hr/>	<hr/>
	117,924	52,439
	<hr/> <hr/>	<hr/> <hr/>

12. **Contingent Liabilities**

As at 30 June 2007, the Group did not have any significant contingent liabilities.

13. **Gearing Ratio**

As at 30 June 2007, the Group's gearing ratio was approximately 68.0% (31 December 2006: 63.09%) which is calculated based on the Group's total liabilities of approximately RMB1,315,684,000 (31 December 2006: approximately RMB917,451,000) and total assets of approximately RMB1,935,486,000 (31 December 2006: approximately RMB1,454,216,000).

14. **Foreign Exchange Exposure**

The Group's exposure to exchange rate changes mainly came from certain receivables and the cash and cash equivalents denominated in functional currencies other than RMB.

15. **Related Party Transactions**

During the period, the Group had the following significant transactions with related parties:

The Group	Notes	Six months ended 30 June	
		2007	2006
		RMB'000	RMB'000
		(Unaudited)	(Unaudited)
Purchases of raw materials from other related parties	(i)	253,036	106,496
Sales of raw materials to other related parties	(ii)	13,681	4,183
Rental paid to a company in which a director of the Company is a shareholder	(iii)	162	67
Rental paid to other related parties	(iii)	70	42
Rental received from other related parties	(iv)	345	173
Subcontracting income received from other related parties	(v)	—	192
Subcontracting fees paid to other related parties	(v)	—	203
Purchases of equipment from other related parties	(vi)	—	3,490
		<u><u> </u></u>	<u><u> </u></u>

Notes:

- (i) The purchase of raw materials from other related parties represented purchase from Weihai Baolong Special Petroleum Materials Co., Ltd. ("Weihai Baolong") of RMB213,526,000 (2006: RMB68,070,000) and Shouguang Molong Electro-mechanical Equipment Company Limited ("Molong Equipment") of RMB39,510,000 (2006: 38,426,000).

The purchase of raw materials from Weihai Baolong were made by the prevailing market price less an agreed discount of not more than RMB100 per ton. In addition, Weihai Baolong undertook that the supply price offered to the Company would not be higher than the supply price of the same goods offered to independent third parties over the same time.

The purchases of raw materials from Molong Equipment were made at the fixed rates prescribed by relevant authorities of the PRC (if any). If no fixed rates are prescribed by the relevant authorities of the PRC, the purchase price will be negotiated and agreed to by both parties with reference to the then prevailing market price. (subject to adjustment)

- (ii) The sales of scrap and raw materials were made at the fixed rates prescribed by relevant authorities of the PRC (if any). If no fixed rates are prescribed by the relevant authorities of the PRC, the selling price will be negotiated and agreed to by both parties with reference to the then prevailing market price. (subject to adjustments)
- (iii) These transactions were determined at rates mutually agreed between the Group and the related parties, which were lower than the market rates of the properties of similar locations.
- (iv), (vi) These transactions were determined upon normal commercial terms on an arm's length basis between the Group and connected parties.
- (v) These transactions were determined at rates mutually agreed between the Group and the related parties, which were set at cost incurred plus a margin of 5%.

The purchase transactions were made at cost. The related party transactions in respect of items (i), (ii), (iii), (iv), (v) and (vi) also constitute connected transactions or continuing connected transactions as defined in Chapter 14A of the Listing Rules.

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16. **Comparative Amounts**

Certain comparative amounts have been reclassified to conform with the current year's presentation.

17. **Post Reporting Period Event**

- (1) Pursuant to the resolutions of the 2006 Annual General Meeting and the first Class Meetings of 2007 held on 25 May 2007 and the resolutions of the Board Meeting held on 24 July 2007, 1,606,888,000 domestic shares and 985,104,000 H shares (i.e. an aggregate of 2,591,992,000 ordinary shares) were issued, on 24 July 2007, as bonus shares at the ratio of 4 new ordinary shares for each ordinary share to all shareholders registered on the Company's register of members on 25 April 2007, and the shares issued to shareholders of H shares were listed for trading on the Stock Exchange starting from 27 July 2007.

Assuming the above new issue of 2,591,992,000 ordinary shares at the par value of RMB0.1 per share was completed on 30 June 2007, calculated on the total outstanding share capital of 3,239,990,000 shares, the earnings per share was approximately RMB2.79 cents (2006: RMB1.56 cents).

- (2) According to the Ministry of Finance and the "Notice on the Promotion of Employment Taxation Benefits for the Handicapped" Cai Shui (2007) No.92 issued by the State Administration of Taxation (Note 6), the original taxation policy benefits enjoyed by Weifang Molong Drilling Equipment Company Limited have changed to actual value-added tax rebates capped at the ceiling of no more than RMB35,000 per year for each handicapped person with effect from 1 July 2007. And 100% of the actual amount of wages paid to handicapped staff members will be included and deducted before corporate income tax was levied.

MANAGEMENT DISCUSSION AND ANALYSIS

Financial Review

The Group has achieved a satisfactory result during the period under review. For the six months ended 30 June 2007, the Group recorded an unaudited revenue of approximately RMB806,411,000 (2006: RMB443,398,000) and an unaudited net profit of approximately RMB90,532,000 (2006: RMB50,424,000). Compared to the corresponding period in the previous year, the revenue has a growth of approximately RMB363,013,000 or 81.9%, and the net profit has a growth of approximately RMB40,108,000 or 79.5%.

Business Review

During the period under review, the Group was engaged in the design, manufacture and sale of petroleum drilling and extraction machinery and related accessories. Its major products can be grouped into six categories, namely oil well pipes, casing, oil well sucker rods, oil well pumps, oil well pumping machines and other petroleum drilling and extraction machinery accessories. These products are primarily used in petroleum drilling and extraction and are necessary equipments of the industry.

The Company's migration from the GEM to the Main Board of the Stock Exchange on 7 February 2007 has enhanced its image and recognition in the international market, and was favorable to the Company in terms of its efforts in expanding the market and facilitating international cooperation, so as to enable the Company stable development.

Following the implementation of the Group's strategies such as enhancement in the research and development capabilities, improvement to the existing products, expansion of sales networks, and along with the Group's excellent quality products and services, the Group has established a strong competitive position in the market and has recorded a steady increase in domestic sales, the revenue increased 31.4% compared with the same period of the previous year. The Group has also achieved a significant increase in its overseas sales, the sales revenue of which increased 1.8 times as compared with the same period of 2006. In particular the revenue of its sales to Europe and other countries recorded an outstanding increase of 2.8 times as comparable period of 2006.

As for the domestic market development, the Group's current customers are still mainly oil fields operated by PetroChina Company Limited and its subsidiaries (collectively "PetroChina Group"), including Xinjiang Oil Field (新疆油田), Daqing Oil Field (大庆油田), Changqing Oil Field (长庆油田), Liaohe Oil Field (辽河油田), Qinghai Oil Field (青海油田), Huabei Oil Field

(華北油田) and Jilin Oil Field (吉林油田), and China Petroleum & Chemical Corporation and its subsidiaries (collectively “Sinopec Group”), including Shengli Oil Field (勝利油田), Zhongyuan Oil Field (中原油田), Jiangnan Oil Field (江漢油田) and etc. Sales to the above oil fields under PetroChina Group and Sinopec Group accounted for approximately 47.1% of the Group’s total Sales revenue. Meanwhile, the Group is actively exploring cooperation opportunities with CNOOC Limited and its subsidiaries (collectively “CNOOC Group”) and carrying out a comprehensive and detailed survey research on the Jidong Oil Field striving to launch our Group’s products into the Jidong Oilfield during the second half of the year. In addition, the Group has begun to cooperate with Shanxi Yanchang Petroleum (Group) Co., Ltd. (i.e. Yanchang Petroleum, 延長石油).

Owing to our long standing good track record in the provision of supplies, the Group was named one of the top four outstanding suppliers of petroleum special piping products by the E-Business Department of PetroChina Company Limited.

Apart from its continued efforts in consolidating relationships with the existing customers and securing new ones, the Group has also placed great emphasis on further exploring overseas markets. Currently, apart from maintaining the scale of growth in our export business to such regions as North America, Europe, Russia, Southeast Asia, the Group also secures new clients in the Middle East, Africa and etc. And the sales growth contributed to the Group will be reflected in the annual report. The Group has established and maintained good cooperative relationships with several international oil companies, which in turn boosted the sales of its products in the overseas markets.

During the period under review, the Group’s sales to overseas markets were mainly priced in US dollars. The Group monitored closely the exchange rate changes between RMB and US dollars as well as the state taxation policy changes regarding export tax rebates. And corresponding strategies were formulated in respect of the pricing of export products, trade receivables, etc. in order to reduce the impact of the above changes on the Company’s business. In future, the Group will further enhance the quality and market positioning of export products, increase the proportion of high value-added products in exports and enhance efficiency by improving technology and reducing wastage to achieve the objective of cost reduction, in order to maintain the gross profit margin of exports products at a relatively stable level.

The 250,000-tonne casing production line has commenced its production in the fourth quarter of 2006 and is expected to demonstrate more of its importance this year. Commencement of this production line helped to enhance the Group’s production capabilities that favoured rapid growth of our business for the Group.

Comprehensive Development of New Products

The Group is proactively engaged in the R&D of new products. Also, the Group has successfully engaged suitable R&D and quality control experts in the industry and keeps abreast of the latest information and technology in the world, in order to maintain its leading position in the industry.

The development of high-pressure and corrosion resistant casings, special path casings, drilling rods and in-line pipes has been completed. The performance tests administered by authoritative national laboratories were passed and were ready for small batch production. Casings of the H₂S corrosion resistant series and low-temperature resistant casings entered into the experimental phase. A special type of buckle with proprietary intellectual property rights had also completed its initial design work and technical exchange.

Enhancement of Market Promotion and Development of Domestic and Overseas Markets

In respect of the domestic market, the Group considers that such on-site offices at oil fields allow the Group to make timely visits to its customers to listen to their opinions and collect the latest market information, which enables the Group to better understand customer needs, strengthen after-sales services and develop the domestic market. Meanwhile, the Group also puts effort in gaining potential new customers.

Products such as oil well pumps, oil well pipes, casings, etc. attained a breakthrough in the development of the coal gas drilling and extraction equipment market. The Group will continue to increase its efforts and the depth of developing the coal gas segment in future in order to facilitate the products such as oil well pipes, casings, oil well pumps, oil well pumping machines, etc. to expand the sales market of the coal gas drilling and extraction equipment market segment gradually.

In respect of the overseas markets, during the first half of 2007, the demand of Russian market recorded high growth and the Group, by grasping the opportunities and strengthening market development, has now become the largest Chinese supplier of oil well pipes and casing products in Russia; other foreign new markets which are being developed include Turkey, Libya, India, Vietnam and Columbia.

Major Acquisitions/Disposals and Significant Investment

During the period under review, the Company established a limited liability company, Shouguang Baolong Petroleum Equipment Company Limited (“Shouguang Baolong”) with an independent third party, Weifang Shengcheng Investment Management Company Limited, on 30 April 2007, in order to provide casting parts for our petroleum machinery products for cost reduction of purchases and optimization of our ancillary facilities. The business scope of Shouguang Baolong includes manufacturing and sales of petroleum equipment. The registered capital of Shouguang Baolong is RMB150 million. After the relevant capital has been fully contributed, the Company shall hold 70% of the equity interests.

As Shouguang Maolong Machinery Company Limited, the 10% shareholder of MPM (MPM International Limited), a subsidiary of the Company, had reached an agreement with Shengcheng Investment to transfer the above shareholding, approval was obtained from the Ministry of Commerce of the PRC in compliance with the relevant laws and regulations of the PRC. The transaction is in the process of arranging for the transfer.

The Acquisition of Minority Interests

Based on the actual operations of the subsidiary, Weifang Molong Drilling Equipment Company Limited (“Molong Drilling Equipment”), the Company had acquired the 10% shareholding held by the People’s Government of Shangkou Township being the minority shareholder of Molong Drilling Equipment for a total consideration of RMB7,340,000 on 28 June 2007. Molong Drilling Equipment had a registered capital of RMB6,000,000 and the Company was controlling 90% shareholding. The registration procedure for modification of shareholding ownership pursuant to the acquisition was completed on 10 July 2007 at the Bureau of Administration for Industry and Commerce in Shouguang City, Shangdong Province.

Outlook

With the development of the global economy, the continuous keen demand in crude oil from various countries and the steady growth of market demand in petroleum drilling and extraction machinery resulting from the exploitation of oil fields to increase output, which increases the usage and consumption of petroleum drilling and extraction machinery, the Group is highly confident in the future of the petroleum machinery industry.

The Group will continue to capture opportunities, and further enhance its competitive capability through various strategies, including expansion of the production volume of new products and high value-added products, improvement of product quality, strengthening of its research and development capability, enhancement of market promotion and effective cost control. Meanwhile, the Group will continue to develop domestic and overseas markets in order to increase its market share in the industry.

The future investments will concentrate on further increasing the scale of the production of oil well pipes and casings with a concentration on the petroleum machinery business, keep expanding the petroleum machinery business and improving the quality of mainstay products, stepping into foundry and band processing manufacturing and also keep researching and developing in the Coal Mine Methane drilling and extraction equipment industry.

Enhancement of Casing Production Capacity

The Group's 250,000-tonne casing production line has been put into production, and installation of the ancillary thermal treatment and processing production line has also been put into production. And they will form a casing production line with an annual capacity of 250,000 tonnes. With the enhancement of production technologies and skills, and the familiarization of the staff, the Group expects the production volume will meet the target in the next 3 years.

Bank Facilities and Pledge of Assets

As at 30 June 2007, the Group had bank credit loans amounting to RMB356,500,000 and US dollar short term deposits US\$3,300,000. In addition, ten banks, including the Agricultural Bank of China (Shandong Branch), have granted credit facilities totaling RMB680,000,000 to the Group. None of these credit facilities have been utilized.

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Employees

For the period under review, the breakdown of the number of employees of the Group is set out below:

	Six months ended 30 June	
	2007	2006
Research and development	58	57
Production	1,708	1,324
Quality control	97	92
Sales and marketing	65	63
Administration	166	168
	<hr/>	<hr/>
Total	2,094	1,704
	<hr/> <hr/>	<hr/> <hr/>

The Group keeps a close watch on the levels of employees' remuneration and benefits, and rewards staff according to the results of the Group's operating achievement. Furthermore, the Group also offers training and development opportunities to employees.

CORPORATE GOVERNANCE

The Company has complied throughout the period under review with the code provisions set out in the "Code on Corporate Governance" contained in Appendix 14 of the Listing Rules.

Re-election of the Board

Pursuant to the relevant provisions of the Articles of Association of the Company, a motion to re-elect the Board of Directors was tabled at the 22nd Meeting of the First Board of Directors held on 29 March 2007 by the Nomination Committee, and it was passed by a resolution at the Annual General Meeting for the year 2006 held on 25 May. All nine members of the first Board of Directors were re-elected as members of the new Board. Five of the new members, Mr. Zhang En Rong, Mr. Zhang Yun San, Mr. Lin Fu Long, Mr. Xie Xin Cang and Mr. Loke Yu alias Loke Hoi Lam, were appointed to the Second Board of Directors for an appointment period from 26 May 2007 to 25 May 2010; while Mr. Yan Yi Zhuang, Mr. Chan Jianxiong, Mr. Qin Xue Chang and Mr. Wang Ping would continue to act as directors pursuant to their original service contracts.

During the current period under review, Mr. Zhang En Rong, Mr. Zhang Yun San, Mr. Lin Fu Long and Mr. Xie Xin Cang were re-elected as executive Directors upon renewal of the Board of Directors; while Mr. Wang Ping and Mr. Chen Jian Xiong were re-elected as non-executive Directors; and Mr. Loke Yu alias Loke Hoi Lam, Mr. Yan Yi Zhuang and Mr. Qin Xue Chang were re-elected as independent non-executive Directors upon renewal of the Board.

Audit Committee

The Company formulated written terms of reference for the Audit Committee in accordance with requirements of the Listing Rules. The Audit Committee consists of three independent non-executive Directors. As a result of the election held at the first meeting on 28 May 2007 by the Second Board of Directors, the three independent non-executive Directors, Mr. Qin Xue Chang, Mr. Yan Yi Zhuang and Mr. Loke Yu alias Loke Hoi Lam, continued to form the Audit Committee under the Second Board of Directors. Mr. Qin Xue Chang was appointed as Chairman of the new Audit Committee. The Audit Committee held one meeting during the period under review with an attendance rate of 100%.

The Audit Committee is mainly responsible for monitoring the integrity of the Company's financial statements, reviewing the Company's internal control system and its execution ,through review of work undertaken by the internal and external auditors, evaluating financial information and related disclosure and receiving connected transactions..

The Group's unaudited financial information and related disclosure and receiving connected transactions for the six months ended 30 June 2007 have been reviewed by the Audit Committee.

Remuneration and Evaluation Committee

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The Company set up a remuneration and evaluation committee (the "Remuneration Committee") on 18 January 2005. The primary duties of the Remuneration Committee is to make proposals to the Board on the remuneration adjustment policy and structure in respect of the Directors and senior management of the Company and to determine the designated remuneration for all the executive Directors and senior management.

As a result of the election held at the first meeting on 28 May 2007 by the Second Board of Directors, the Remuneration Committee under the Second Board of Directors continued to be formed by the three independent non-executive Directors, Mr. Qin Xue Chang, Mr. Yan Yi Zhuang and Mr. Loke Yue alias Loke Hoi Lam, and one executive Director, Mr. Zhang Yun San. Mr. Loke Yu alias Loke Hoi Lam was appointed as Chairman of the new Remuneration Committee.

The Remuneration Committee held one meeting during the period under review with an attendance rate of 100%.

Nomination Committee

The Company set up a nomination committee (the "Nomination Committee") on 18 January 2005, which aims to ensure the procedures for the appointment of Directors to comply with the principle of fairness and transparency. The principal rights and duties of the Nomination Committee are to regularly review the structure, number and composition (including skill, knowledge and experience) of the Board and to make recommendations to the Board on any intended change.

As a result of the election held at the first meeting on 28 May 2007 by the Second Board of Directors, the Nomination Committee under the Second Board of Directors continued to be formed by the three independent non-executive Directors, Mr. Qin Xue Chang, Mr. Yan Yi Zhuang and Mr. Loke Yue alias Loke Hoi Lam, and one executive Director, Mr. Zhang Yun San. Mr. Yan Yi Zhuang was appointed as Chairman of the new Nomination Committee.

The Nomination Committee held one meeting during the period under review with an attendance rate of 100%.

Model Code for Securities Transaction by Directors

The Company has adopted a model code of practice with standards not lower than those as required under Appendix 10 of the Listing Rules for securities transactions by Directors. The Company has confirmed after making due enquiries with all the Directors in accordance with the code of practice that all the Directors have complied with the standard of dealings and model code of practice in relation to the securities transaction by Directors.

DISCLOSURE OF DIRECTORS', SUPERVISORS' AND CHIEF EXECUTIVES' INTERESTS IN SHARES, UNDERLYING SHARES AND DEBENTURES

As at 30 June 2007, the interest and short positions of the Directors, supervisors (the "Supervisors") and chief executives of the Company in the shares, debentures or underlying shares of the Company or any of its associated corporations (within the meaning of Part XV of the Securities and Futures Ordinance (the "SFO")) which were required to be notified to the Company and 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 were required, pursuant to section 352 of the SFO, to be entered in the register referred to therein, or which were required pursuant to the required standard of dealings by Directors as set out to in Appendix 10 of the Listing Rules, to be notified to the Company and the Stock Exchange, were as follows:

Long positions in the domestic shares of the Company:

	Type of Interest	Number of domestic shares <i>(Note 2)</i>	Percentage of domestic shares <i>(%)</i>	Percentage of total registered share capital <i>(%)</i>
Zhang En Rong <i>(Executive Director)</i>	Beneficial	279,517,000	69.58	43.14
Lin Fu Long <i>(Executive Director)</i>	Beneficial	34,216,000	8.52	5.28
Zhang Yun San <i>(Executive Director)</i>	Beneficial	30,608,000	7.62	4.72
Xie Xin Cang <i>(Executive Director)</i>	Beneficial	21,410,000	5.33	3.30
Li Bao Hui <i>(Supervisor) (Note 1)</i>	Interests of spouse	21,410,000	5.33	3.30

Notes:

1. Ms. Li Bao Hui is the wife of Mr. Xie Xin Cang and is taken to be interested in the 21,410,000 domestic shares held by Mr. Xie Xin Cang under SFO.
2. Refer to 17th of Notes of the unaudited condensed consolidated financial statements: Post Reporting Period Event (1). After the bonus shares were issued, long positions in the domestic shares of the Company for each of Mr. Zhang En Rong, Mr. Lin Fu Long, Mr. Zhang Yun San, Mr. Xie Xin Cang and Ms. Li Bao Hui had become as follows, but the capacity in which he/she holds the interests in the Company and the percentages of his/her interests against the total issued domestic share capital and the total issued share capital remain the same:

**Number of Shares (After the issuance of
bonus share on 24 July 2007)**

Zhang En Rong (<i>Executive Director</i>)	1,397,585,000
Lin Fu Long (<i>Executive Director</i>)	171,080,000
Zhang Yun San (<i>Executive Director</i>)	153,040,000
Xie Xin Cang (<i>Executive Director</i>)	107,050,000
Li Bao Hui (<i>Supervisor</i>)	107,050,000

Save as disclosed above, as at 30 June 2007 to the best knowledge of the Directors, none of the Directors, the Supervisors or chief executives of the Company had any interests or short positions 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), were required be notified to the Company and the Stock Exchange under Divisions 7 and 8 of Part XV of the SFO (including interests and short positions which they are taken or deemed to have under the SFO) or were required, pursuant to section 352 of the SFO to be entered in the register referred to therein, or which were required, pursuant to the requirements as set out in Appendix 10 of the Listing Rules, to be notified to the Company and the Stock Exchange.

OTHER DISCLOSURE INFORMATION

Directors' and Supervisors' Rights to Acquire Shares or Debentures

None of the Directors or Supervisors or their respective associates (as defined under the Listing Rules) was granted by the Company or its subsidiaries any rights or options to acquire any shares in or debentures of the Company or had exercised any such rights as at 30 June 2007.

Share Option Scheme

The Company does not have any share option scheme.

Substantial Shareholders

As at 30 June 2007, so far as known to the Directors, Supervisors or chief executives of the Company, the following persons (other than Directors, Supervisors or chief executives of the Company) had, or were deemed or taken to have interests or short positions in the shares and underlying shares and debentures of the Company which would fall to be disclosed to the Company and the Stock Exchange under the provisions of Divisions 2 and 3 of Part XV of the SFO and required to be recorded in the register to be kept under section 336 of the SFO:

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Long positions in the H Shares of the Company:

	Capacity	Number of H shares	Approximate percentage of total issued H Shares capital (%)	Approximate percentage of total issued Share capital (%)
Paul G. Desmarais (<i>Note 2</i>)	Interest of controlled corporation	270,702,000 (<i>Note 1</i>)	21.98	8.36
Nordex Inc. (<i>Note 2</i>)	Interest of controlled corporation	270,702,000 (<i>Note 1</i>)	21.98	8.36
Gelco Enterprises Ltd. (<i>Note 2</i>)	Interest of controlled corporation	270,702,000 (<i>Note 1</i>)	21.98	8.36

	Capacity	Number of H shares	Approximate percentage of total issued H Shares capital (%)	Approximate percentage of total issued Share capital (%)
Power Corporation of Canada (Note 2)	Interest of controlled corporation	270,702,000 (Note 1)	21.98	8.36
Power Financial Corporation (Note 2)	Interest of controlled corporation	270,702,000 (Note 1)	21.98	8.36
IGM Financial Incorporation (Note 2)	Interest of controlled corporation	270,702,000 (Note 1)	21.98	8.36
Commonwealth bank of Australia (Note 3)	Interest of controlled corporation	17,050,000	6.92	2.63

Notes:

1. Refer to 17th of Notes of the unaudited condensed consolidated financial statements: Post Report Period Event (1). According to the disclosure of interest notices filed by Desmarais Paul G., Gelco Enterprises Ltd., IGM Financial Inc., Nordex Inc., Power Corporation of Canada and Power Financial Corporation, each of these companies is interested in 270,702,000 H shares of the Company as at 30 June 2007, this figure has taken into account the effect of the issuance of bonus shares. Among these 270,702,000 H Shares in which these companies are deemed to have interest, 255,122,000 H Shares were directly held by Mackenzie Cundill Investment Management Ltd. and 15,580,000 H Shares were directly held by Mackenzie Cundill Investment MGMT (Bermuda) Ltd. (Please refer to Note 2).

If the issuance of bonus shares had not been taken into account, Desmarais Paul G., Gelco Enterprises Ltd., IGM Financial Inc., Nordex Inc., Power Corporation of Canada and Power Financial Corporation should each be interested in 54,140,400 H shares of the Company as at 30 June 2007. Among these 54,140,400 H Shares, 51,024,400 were directly held by Mackenzie Cundill Investment Management Ltd. and 311,600 H Shares were directly held by Mackenzie Cundill Investment MGMT (Bermuda) Ltd. (Please refer to Note 2).

2. Mackenzie Cundill Investment Management Ltd. is a wholly-owned subsidiary of Mackenzie Financial Corporation, which in turn is a wholly-owned subsidiary of Mackenzie Inc. Mackenzie Inc. is a wholly-owned subsidiary of IGM Financial Inc., which in turn is owned as to 55.99% by Power Financial Corporation, Power Financial Corporation is owned as to 66.40% by 171263 Canada Inc, which in turn is a wholly-owned subsidiary of 2795957 Canada Inc. 2795957 Canada Inc is a wholly-owned subsidiary of Power Corporation of Canada, which in turn is owned as to 54.18% by Gelco Enterprise Ltd., Gelco Enterprise Ltd. is owned as to 94.95% by Nordex Inc., which in turn is owned as to 68% by Paul G. Desmarais.

Mackenzie Cundill Investment MGMT (Bermuda) Ltd, is a wholly-owned subsidiary of Mackenzie (Rockies) Corp. which in turn is a wholly-owned subsidiary of Mackenzie Financial Corporation.

3. The H Shares in which Commonwealth Bank of Australia was deemed interested in under SFO were held by a corporation it controlled indirectly. The 17,050,000 H Shares are directly held by First State Investments (Hong Kong) Ltd, which was a wholly-owned subsidiary of First State (Hong Kong) LLC, which was in turn wholly-owned by First State Investments (Bermuda) Ltd., First State Investments (Bermuda) Ltd. was wholly owned by First State Investment Managers (Asia) Ltd. which was wholly owned by Colonial First State Group Ltd. Colonial First State Group Ltd. was wholly owned by Commonwealth Insurance Holdings Ltd. which was wholly owned by Colonial Holding Company Pty. Ltd. Commonwealth Bank of Australia wholly and directly owns the interests in Colonial Holding Company Pty. Ltd..

Save as disclosed above, as at 30 June 2007 so far as is known to the Directors, Supervisors or chief executive, there are no other persons (not being a Director, Supervisor or chief executive of the Company) who had interests or short positions in the shares, underlying shares and debentures of the Company which would fall to be disclosed to the Company under the provisions of Divisions 2 and 3 of Part XV of the SFO and required to be 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 Listing Rules) had any interest in a business which competes or may compete with the business of the Group.

Compliance Adviser's Interest

As updated and notified by the Company's compliance adviser, Guotai Junan Capital Limited (the "Compliance Adviser"), neither the Compliance Adviser, nor its directors, employees or associates (as defined under the Listing Rules) had any interest in the share capital of the Company as at 30 June 2007 pursuant to Rule 3A.19 of the Listing Rules.

Pursuant to an agreement dated 31 October 2005 between the Company and the Compliance Adviser, the Compliance Adviser will provide the Company with compliance advisory services during the first 12 months from the date of successful conversion to the Main Board on 7 February 2007 in accordance with the terms of the agreement.

Purchase, Sale Or Redemption Of Securities

Neither the Company nor its subsidiaries has purchased, sold or redeemed any listed securities of the Company during the six months ended 30 June 2007.

Directors

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

By order of the Board of Directors

Zhang En Rong

Chairman

Shandong, the PRC
17 August 2007