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宏華集團有限公司

Honghua Group Limited

(a company incorporated in the Cayman Islands with limited liability)

(Stock code: 0196)

ANNOUNCEMENT OF INTERIM RESULTS FOR THE SIX MONTHS ENDED 30 JUNE 2011

FINANCIAL HIGHLIGHT

The Company's Shares were listed on the Main Board of The Stock Exchange on 7 March 2008

	Six months ended 30 June		
	2011	2010	% change
	(Unaudited)	(Unaudited)	
Revenue (<i>RMB'000</i>)	1,295,290	685,596	88.9%
Gross profit (<i>RMB'000</i>)	330,025	161,667	104.1%
Gross profit margin (%)	25.5%	23.6%	
Profit/(loss) from operations (<i>RMB'000</i>)	83,850	(54,095)	
Earnings/(loss) attributable to equity shareholders of the Company (<i>RMB'000</i>)	52,774	(89,458)	
Earnings/(loss) per share — Basic and diluted (<i>RMB cents</i>)	1.64	(2.77)	

The Board does not recommend payment of interim dividend for the six months ended 30 June 2011.

INTERIM RESULTS

The Board of the Company is pleased to announce the unaudited interim financial results of the Group for the six months ended 30 June 2011, together with the comparative figures for the corresponding period in 2010.

The interim financial report for the six months ended 30 June 2011 is unaudited, but has been reviewed by KPMG, in accordance with Hong Kong Standard on Review Engagements 2410 "Review of interim financial information performed by the independent auditor of the entity", issued by the Hong Kong Institute of Certified Public Accountants whose unmodified review report is included in the interim financial report to be sent to shareholders. These interim results have also

been reviewed by the Audit Committee, comprising solely the independent non-executive Directors, one of whom chairs the Audit Committee.

CONSOLIDATED INCOME STATEMENT

for the six months ended 30 June 2011 — unaudited

(Expressed in Renminbi)

		Six months ended 30 June	
		2011	2010
	<i>Note</i>	RMB'000	RMB'000
Revenue	3, 4	1,295,290	685,596
Cost of sales		<u>(965,265)</u>	<u>(523,929)</u>
Gross profit		330,025	161,667
Other revenue	5	2,417	3,193
Other net (loss)/income		(71)	1,253
Other operating expenses		(560)	(1,227)
Selling expenses		(75,945)	(69,984)
General and administrative expenses		<u>(172,016)</u>	<u>(148,997)</u>
Profit/(loss) from operations		83,850	(54,095)
Finance income		10,840	8,755
Finance expenses		<u>(16,623)</u>	<u>(54,526)</u>
Net finance expenses	6(a)	(5,783)	(45,771)
Share of profit from an associate		1,757	—
Share of loss from jointly controlled entities		(4,537)	(1,484)
Profit/(loss) before taxation	6	75,287	(101,350)
Income tax (expenses)/credit	7	<u>(15,059)</u>	12,176
Profit/(loss) for the period		<u>60,228</u>	<u>(89,174)</u>
Attributable to:			
Equity shareholders of the Company		52,774	(89,458)
Non-controlling interests		7,454	284
Profit/(loss) for the period		<u>60,228</u>	<u>(89,174)</u>
Earnings/(loss) per share — Basic and diluted <i>(RMB cents)</i>	9	<u>1.64</u>	<u>(2.77)</u>

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

for the six months ended 30 June 2011 — unaudited

(Expressed in Renminbi)

	Six months ended 30 June	
	2011	2010
	RMB'000	RMB'000
Profit/(loss) for the period	60,228	(89,174)
Other comprehensive income for the period, net of tax:		
Exchange differences on translation of financial statements of operations outside the PRC	<u>(10,872)</u>	<u>(18,504)</u>
Total comprehensive income for the period	<u>49,356</u>	<u>(107,678)</u>
Attributable to:		
Equity shareholders of the Company	<u>41,957</u>	<u>(107,969)</u>
Non-controlling interests	<u>7,399</u>	<u>291</u>
Total comprehensive income for the period	<u>49,356</u>	<u>(107,678)</u>

CONSOLIDATED BALANCE SHEET

at 30 June 2011 — unaudited

(Expressed in Renminbi)

		30 June 2011 <i>RMB'000</i>	31 December 2010 <i>RMB'000</i>
	<i>Note</i>		
Non-current assets			
Fixed assets			
— Property, plant and equipment		657,339	529,574
— Interests in leasehold land held for own use under operating leases		139,699	140,058
— Freehold land		5,217	5,339
		<u>802,255</u>	<u>674,971</u>
Deposits paid for acquisition of leasehold land		223,972	218,984
Construction in progress		187,986	77,144
Intangible assets		249,028	272,585
Interest in an associate		61,335	—
Interests in jointly controlled entities		29,634	41,868
Deferred tax assets		71,389	69,341
		<u>1,625,599</u>	<u>1,354,893</u>
Current assets			
Inventories	10	1,767,113	1,859,897
Trade and other receivables	11	1,330,099	1,217,108
Amounts due from related companies		61,373	25,749
Amount due from immediate holding company		6	6
Amount due from ultimate holding company		6	6
Current tax recoverable		23,420	27,508
Other financial assets		—	473,680
Pledged bank deposits		76,475	29,072
Bank deposits maturing over three months		6,600	4,000
Cash and cash equivalents		1,421,490	1,002,727
		<u>4,686,582</u>	<u>4,639,753</u>
Total current assets		<u>4,686,582</u>	<u>4,639,753</u>
Total assets		<u>6,312,181</u>	<u>5,994,646</u>

CONSOLIDATED BALANCE SHEET (continued)

at 30 June 2011 — unaudited

(Expressed in Renminbi)

		30 June 2011	31 December 2010
	<i>Note</i>	<i>RMB'000</i>	<i>RMB'000</i>
Current liabilities			
Interest-bearing borrowings		769,950	444,000
Amounts due to related companies		28,810	48,206
Trade and other payables	12	1,101,341	1,209,911
Current tax payable		11,826	11,196
Provision for product warranties		19,885	15,738
Total current liabilities		<u>1,931,812</u>	<u>1,729,051</u>
Net current assets		<u>2,754,770</u>	<u>2,910,702</u>
Total assets less current liabilities		<u>4,380,369</u>	<u>4,265,595</u>
Non-current liabilities			
Interest-bearing borrowings		242,265	182,318
Deferred tax liabilities		13,645	12,486
Total non-current liabilities		<u>255,910</u>	<u>194,804</u>
Total liabilities		<u>2,187,722</u>	<u>1,923,855</u>
Equity			
Share capital		299,593	299,593
Reserves		3,710,206	3,663,937
Total equity attributable to equity shareholders of the Company		4,009,799	3,963,530
Non-controlling interests		114,660	107,261
Total equity		<u>4,124,459</u>	<u>4,070,791</u>
Total liabilities and equity		<u>6,312,181</u>	<u>5,994,646</u>

1 BASIS OF PREPARATION

The interim financial report has been prepared in accordance with the applicable disclosure provisions of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited, including compliance with International Accounting Standard (“IAS”) 34, *Interim financial reporting*, adopted by the International Accounting Standards Board (“IASB”). It was authorised for issuance on 24 August 2011.

The interim financial report has also been prepared in accordance with the same accounting policies adopted by the Group in the 2010 annual financial statements, except for the accounting policy changes that are expected to be reflected in the 2011 annual financial statements. Details of these changes in accounting policies are set out in note 2.

2 CHANGES IN ACCOUNTING POLICIES

The IASB has issued a number of amendments to IFRSs and one new Interpretation that are first effective for the current accounting period of the Group and the Company. Of these, the following developments are relevant to the Group’s financial statements.

- IAS 24 (revised 2009), *Related party disclosures*
- Improvements to IFRSs (2010)

The Group has not applied any new standard or interpretation that is not yet effective for the current accounting period.

These developments related primarily to clarification of certain disclosure requirements applicable to the Group’s financial statements. These developments have had no material impact on the contents of the interim financial report.

3 SEGMENT REPORTING

Information regarding the Group's reportable segments as provided to the Group's most senior executive management for the purposes of resource allocation and assessment of segment performance for the period is set out below.

For the six months ended 30 June	Land drilling rigs		Parts, components and others		Offshore drilling rigs		Total	
	2011	2010	2011	2010	2011	2010	2011	2010
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
Revenue from external customers	907,454	466,642	387,836	218,954	—	—	1,295,290	685,596
Inter-segment revenue	—	—	312,184	139,423	—	—	312,184	139,423
Reportable segment revenue	<u>907,454</u>	<u>466,642</u>	<u>700,020</u>	<u>358,377</u>	<u>—</u>	<u>—</u>	<u>1,607,474</u>	<u>825,019</u>
Reportable segment profit/(loss)	<u>89,776</u>	<u>(27,501)</u>	<u>36,165</u>	<u>20,859</u>	<u>(22,295)</u>	<u>(10,761)</u>	<u>103,646</u>	<u>(17,403)</u>
As at 30 June/31 December	2011	2010	2011	2010	2011	2010	2011	2010
	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000	RMB'000
Reportable segment assets	<u>2,393,920</u>	<u>2,667,836</u>	<u>1,313,918</u>	<u>1,442,078</u>	<u>414,886</u>	<u>329,878</u>	<u>4,122,724</u>	<u>4,439,792</u>

(a) Reconciliation of reportable segment profit or loss

	Six months ended 30 June	
	2011	2010
	RMB'000	RMB'000
Profit/(loss)		
Reportable segment profit/(loss)	103,646	(17,403)
Elimination of inter-segment profits	(19,707)	(35,179)
Reportable segment profit/(loss)		
derived from Group's external customers	83,939	(52,582)
Share of profit from an associate	1,757	—
Share of loss from jointly controlled entities	(4,537)	(1,484)
Other revenue, expenses and net (loss)/income	1,786	3,219
Net finance expenses	(5,783)	(45,771)
Unallocated head office and corporate expenses	(1,875)	(4,732)
Consolidated profit/(loss) before taxation	<u>75,287</u>	<u>(101,350)</u>

(b) Change in reportable segments

The major change in segment information during the period is the addition of a new offshore drilling rigs segment. Due to the expansion of Group's operation, the internal reporting to the Group's chief operating decision maker include a new reportable segment on offshore drilling rigs. The offshore drilling rigs segment is engaged in the manufacturing and sales of offshore drilling rigs.

(c) Seasonality of operations

The group experiences higher sales in the second half of the year compared to the first half of the year. It is the general practice for the Group's customers, engaging in oil and gas drilling industry, to place larger amounts of purchase orders at the beginning of the year. Having considered the production and delivery schedule, the finished goods related to these purchase orders are delivered in the second half of the year. Revenue from the sale of finished goods is recognised when the customer has accepted the related risks and rewards of ownership. Accordingly, the Group anticipates the inventories would gradually build up before the delivery of finished goods in the second half of the year. As a result, the first half year typically reports lower revenues and results, than the second half.

4 REVENUE

The principal activities of the Group are manufacturing, sale and trading of drilling rigs and related parts and components. Revenue represents the sales value of goods supplied to customers less value-added tax, returns and trade discounts.

For the six months ended 30 June 2011, the Group's customer base include four customers (six months ended 30 June 2010: three customers) with whom transactions representing 16%, 15%, 12% and 12% (six months ended 30 June 2010: 29%, 24% and 22%) of the Group's revenue respectively. For the six months ended 30 June 2011, revenues from sales of drilling rigs and related parts and components to these customers, amounted to approximately RMB211 million, RMB193 million, RMB157 million and RMB157 million (six months ended 30 June 2010: RMB198 million, RMB166 million and RMB151 million) respectively which arose in Middle East region, Europe and Central Asia region, North America region, and Europe and Central Asia region, respectively (six months ended 30 June 2010: North America region, Europe and Central Asia region, and South Asia region respectively).

5 OTHER REVENUE

	Six months ended 30 June	
	2011	2010
	RMB'000	RMB'000
Rendering of repairing services	688	2,834
Others	1,729	359
	<u>2,417</u>	<u>3,193</u>

6 PROFIT/(LOSS) BEFORE TAXATION

Profit/(loss) before taxation is arrived at after charging/(crediting):

	Six months ended 30 June	
	2011	2010
	RMB'000	RMB'000
(a) Net finance expenses		
Bank interest income	(3,963)	(8,755)
Interest income on available-for-sale investments	(6,877)	—
Finance income	<u>(10,840)</u>	<u>(8,755)</u>
Foreign exchange loss, net	1,517	30,703
Interest on interest-bearing borrowings wholly repayable within five years	19,904	26,712
Bank charges	<u>2,536</u>	<u>1,935</u>
	23,957	59,350
Less: interest expense capitalised into assets under construction*	<u>(7,334)</u>	<u>(4,824)</u>
Finance expenses	<u><u>16,623</u></u>	<u><u>54,526</u></u>
Net finance expenses	<u><u>5,783</u></u>	<u><u>45,771</u></u>
* The borrowing costs have been capitalised at a rate of 2.29%–6.97% (six months ended 30 June 2010: 0.68%–6.50%) per annum.		
(b) Staff costs		
Contributions to defined contribution retirement schemes	23,316	19,931
Equity-settled share based payment expenses	4,312	10,482
Salaries, wages and other benefits	<u>134,320</u>	<u>106,098</u>
	<u><u>161,948</u></u>	<u><u>136,511</u></u>
(c) Other items		
Amortisation and depreciation		
— leasehold land held for use under operating leases	1,433	886
— other fixed assets	30,220	23,736
— intangible assets	17,560	18,350
Impairment losses on trade and other receivables	13,712	681
Operating lease charges in respect of properties	2,033	2,839
Provision for product warranties	19,130	13,663
Research and development costs (Note)	<u>22,286</u>	<u>18,888</u>

Note: The amounts included staff costs of employees in the Research and Development Department, which are also included in the total staff costs as disclosed in note 6(b).

7 INCOME TAX IN THE CONSOLIDATED INCOME STATEMENT

(a) Taxation in the consolidated income statement represents:

	Six months ended 30 June	
	2011	2010
	RMB'000	RMB'000
Current tax — outside Hong Kong		
Provision for the period	15,426	2,234
Under/(over) provision in respect of prior years	<u>523</u>	<u>(1,113)</u>
	15,949	1,121
Deferred tax		
Origination and reversal of temporary differences	<u>(890)</u>	<u>(13,297)</u>
	<u>15,059</u>	<u>(12,176)</u>

(i) Hong Kong

No provision for Hong Kong Profits Tax has been made as the Group did not have assessable profits subject to Hong Kong Profits Tax during the six months ended 30 June 2010 and 2011.

(ii) PRC

Pursuant to the income tax rules and regulations of the PRC, the companies comprising the Group in the PRC are liable to PRC enterprise income tax at a rate of 25% during the six months ended 30 June 2011 and 2010, except for the following companies:

(a) Sichuan Honghua Petroleum Equipment Co., Ltd (“Honghua Company”)

Honghua Company is a wholly foreign-owned enterprise, and is entitled to a reduced tax rate of 12.5% during the six months ended 30 June 2010. During the six months ended 30 June 2011, income tax is accrued at a tax rate of 15% applicable for Hi-Tech Enterprises pursuant to the relevant PRC tax rules and regulations.

(b) Chengdu Hongtian Electric Drive Engineering Co., Ltd (“Hongtian Company”) and Sichuan Honghua Youxin Petroleum Machinery Co., Ltd (“Youxin Company”).

Hongtian Company and Youxin Company are recognised as entities established in the western regions of the PRC with principal revenue of over 70% generated from the encouraged business activities. These companies are entitled to a preferential income tax rate of 15% during six months ended 30 June 2010. Effective from 1 January 2011, the applicable tax rate for Hongtian Company and Youxin Company is 25%.

On 27 July 2011, the Ministry of Finance, the General Administration of Customs and the State Administration of Taxation jointly issued CaiShui [2011] No.58 which states that enterprises within encouraged industries and located in the Western Region are entitled to a preferential tax rate of 15% for the period from 1 January 2011 to 31 December 2020 (“Tax Concession”). Hongtian Company and Youxin Company will apply for the Tax Concession in order to continue to enjoy the 15% preferential income tax rate from 2011 to 2020.

(iii) Others

The provision for taxation for other entities is based on the estimated assemble income of those entities and their respective applicable tax rates ruling in the relevant jurisdictions.

(b) Withholding tax

Under the PRC tax law and its Implementation Rules, dividends receivable by non-PRC resident enterprises from PRC enterprises on earnings earned since 1 January 2008 are subject to withholding tax at a rate of 10%. Deferred tax liabilities have been recognised for undistributed retained profits of its subsidiaries established in the PRC earned since 1 January 2008 to the extent that profits are likely to be distributed in the foreseeable future.

8 DIVIDENDS

The Board does not recommend the payment of dividends attributable to the six months ended 30 June 2011 (six months ended 30 June 2010: Nil).

9 EARNINGS/(LOSS) PER SHARE

(a) Basic earnings/(loss) per share

The calculation of basic earnings/(loss) per share for the six months ended 30 June 2011 is based on the profit attributable to ordinary equity shareholders of the Company for the period of RMB52,774,000 (six months ended 30 June 2010: loss of RMB89,458,000) and the weighted average number of shares of 3,223,798,400 (six months ended 30 June 2010: 3,223,782,961) in issue during the interim period.

(b) Diluted earnings/(loss) per share

The share options are anti-dilutive. Therefore, diluted earnings/(loss) per share are the same as the basic earnings/(loss) per share for each of the six months ended 30 June 2010 and 2011.

10 INVENTORIES

(a) Inventories in the balance sheet comprise:

	30 June 2011 RMB'000	31 December 2010 RMB'000
Raw materials	603,554	826,226
Work in progress	830,189	606,555
Finished goods	328,046	422,624
Goods in transit	5,324	4,492
	<u>1,767,113</u>	<u>1,859,897</u>

(b) An analysis of the amount of inventories recognised as an expense is as follows:

	Six months ended 30 June	
	2011 RMB'000	2010 RMB'000
Carrying amount of inventories sold	941,659	500,801
Write-down of inventories	4,501	9,702
Reversal of write-down of inventories	—	(237)
	<u>946,160</u>	<u>510,266</u>

11 TRADE AND OTHER RECEIVABLES

	30 June 2011 RMB'000	31 December 2010 RMB'000
Trade receivables	1,045,424	1,018,668
Bills receivable	4,000	4,000
Less: Allowance for doubtful debts	(139,985)	(126,273)
	909,439	896,395
Value-added tax recoverable	181,671	102,348
Prepayments	138,491	125,406
Other receivables	100,498	92,959
	<u>1,330,099</u>	<u>1,217,108</u>

All of the trade receivables are expected to be recovered within one year and all of the other receivables are expected to be recovered or recognised as expense within one year.

Ageing analysis

Included in trade and other receivables are trade receivables and bills receivable (net of allowance for doubtful debts) with the following ageing analysis as of the balance sheet date:

	30 June 2011 RMB'000	31 December 2010 RMB'000
Current	556,883	704,274
Less than 1 month past due	14,283	7,407
1 to 3 months past due	11,012	16,707
More than 3 months but less than 12 months past due	169,487	40,132
More than 1 year past due	157,774	127,875
	<u>909,439</u>	<u>896,395</u>

The Group normally grants an average credit period of 30 to 90 days to its trade customers.

12 Trade and other payables

	30 June 2011 RMB'000	31 December 2010 RMB'000
Trade payables	631,389	492,616
Bills payable	89,884	181,425
Receipts in advance	258,004	399,612
Other payables	122,064	136,258
	<u>1,101,341</u>	<u>1,209,911</u>

Bills payable as at 30 June 2011 and at 31 December 2010 were secured by pledged bank deposits. All of the trade and other payables are expected to be settled or recognised as income within one year or are repayable on demand.

An ageing analysis of the trade and bills payable based on the invoice date is as follows:

	30 June 2011 RMB'000	31 December 2010 RMB'000
Within 3 months	433,684	373,363
3 months to 6 months	126,318	138,841
6 months to 1 year	70,044	39,751
Over 1 year	91,227	122,086
	<u>721,273</u>	<u>674,041</u>

MANAGEMENT DISCUSSION AND ANALYSIS

During the Period, the Group recorded a turnover of approximately RMB1,295 million, an increase of 88.9% as compared to RMB686 million recorded during the same period last year. Gross profit was RMB330 million and profit attributable to equity shareholders of the Company was RMB53 million.

INDUSTRY REVIEW

During the Period, the global economy continued the recovery trend since 2010 and the emerging and developing economies still maintained strong growth. During the Period, global demand for crude oil rebounded while the international crude oil price fluctuated wildly. Benefiting from lower cost of oil exploitation, oil and gas exploration companies gradually increased their investment in exploration and exploitation activities. The increasing global oil and gas exploration and exploitation activities led to an increase in demand for oil drilling equipment and therefore created a relatively favorable business environment for the industry. According to Baker Hughes research, the average number of operating rigs worldwide during the Period increased by 17.6% as compared to the same period last year.

Meanwhile, some developed economies were reviewing their nuclear power policies and intended to further facilitate and promote clean energy as well as renewable energy subsequent to the radiation leak accident which occurred in Japan. Following the deployment in exploration and utilisation of coalbed methane and shale gas by various countries in Europe, America, the PRC and other emerging economies which possess abundant reserves of such gas resources, the exploration and utilisation of these resources was proactively promoted. During the Period, the PRC successfully carried out the first tender for the exploitation right of shale gas fields.

BUSINESS REVIEW

During the Period, to tackle the intensifying competition in the market, the Group stressed on optimising its product structure, enhancing market layout and achieving product and service differentiation, so as to facilitate its positive development in the aspects of manufacturing operations, market development, strategic cooperation and sustainable development, in order to capture the opportunities arising from the full recovery of the global economy and the oil and gas drilling industry.

Land Drilling Rigs and Parts, Components and Others Business

During the Period, the Group focused on strengthening sales of its core drilling rig products and achieved satisfactory results in the sales of land drilling rigs and parts and components. Meanwhile, the Group continued to obtain orders from Central Asian, North American and South East Asian markets and successfully promoted its high performance-to-cost land drilling rig products to domestic customers in these regions, consolidating the Group's leading position in the market. During the Period, the Group invested in Chengdu Jinkong Financial Leasing Co., Ltd with an aim to provide a financial leasing platform to address customers' financing needs in order to promote sales of drilling rigs and propel development of the Group's core business.

To improve market share and brand recognition, the Group intensified efforts in marketing and participated in 8 exhibitions, including the China International Petroleum & Petrochemical Technology and Equipment Exhibition, the Russian Petroleum and Gas Exhibition and the U.S. Offshore Petroleum Exhibition to promote sales of its core drilling products. At the same time, the Group continued to enhance its production capacity. During the Period, the Group substantially completed the construction and final inspection of the main plant in Dubai which has obtained completion certification awarded by Jebel Ali Free Zone Authority. The Group's U.S. assembly base has also completed restructuring and has been put into operation, which will further enhance the Group's capacity in the market promotion.

Development in Offshore Equipment Business

During the Period, the Group obtained administration approval for its offshore equipment production base in Qidong, Jiangsu Province, the PRC and methodically carried out construction work according to plan. The Group was also proactive in searching for strategic cooperation to enhance the competitiveness and productivity of its offshore production base. In July 2011, the Group announced that it would set up a joint venture with SBI Offshore Limited, an offshore equipment manufacturer in Singapore. Taking advantage of the two companies' competitive edges in production capability and market development, the joint venture will provide contract production services in the global offshore drilling market.

Oil and Gas Engineering Services

During the Period, the Group successfully implemented its diversification strategy and extended its production chain to the oil and gas engineering field. The Group's oil and gas engineering project in Kazakhstan commenced during the Period. The Group not only provided a self-manufactured 7000-meter drilling rig and an expert engineering team for the project, but also provided a one-stop drilling rig solution package according to the drilling requirements of the project. In addition, the Group's oil and gas engineering project in Xinjiang Province, the PRC also commenced drilling and the first drilling well was completed by the end of July 2011.

Research and Development of Products

The Group has always been devoted to the research and development of new products and market promotion so as to efficiently combine its efforts in product R&D and marketing. As at 30 June 2011, the Group had accumulated 123 patent applications and 76 of them have been approved by the authority. During the Period, the Group had 6 new patent applications and 3 of them were new inventions. The in-house designed products including direct top drives and direct-driven pumps have been successfully launched and are constantly modified to meet the demands of customers in different regions. In regard to products for non-conventional gas drilling equipment, the Group has designed the super single pipe rigs, coiled tubing rigs, rack and pinion rigs and fracturing pumps. Regarding the offshore oil and gas equipment segment, the basic design of "Honghua No.1" jack-up drilling rig perform has been completed and obtained the approval of the American Bureau of Shipping (the "ABS"). Its detailed designs and working drawings are under progress. The lift system and locking system design of the jack-up platform have also been submitted to the ABS for approval.

Optimisation in Corporate Governance

While developing its business, the Group was also devoted to building up a robust and efficient management system in quality, environment and safety. During the Period, the Group also obtained the OHSAS18001:2007 Occupational Health and Safety Management Certificate and Dutch National Environmental Management System Accreditation Board (RvA) Certification, after the API Certification and the ISO9001 Certification. During the Period, the Group implemented structure reorganisation and optimisation to enhance its operational efficiency. The Group also developed a systematic training program which integrated the internal and external training to enhance the working skills and overall strengths of staffs. During the Period, 258 sessions of training courses have been completed.

PROSPECTS

In the second half of 2011, the emerging markets are expected to maintain stable growth and lead to increasing crude oil demand. However, the market anticipates that oil price will remain volatile and bring uncertainties to the oil and gas market due to the uncertain political status in the Middle-East and North Africa as well as the European and U.S. debt crisis. In the long run, oil and natural gas still have an irreplaceable position in the global energy structure. It is expected that global demand for oil and gas will constantly increase in the future and lead to increase in global oil and gas exploration and exploitation expenditure, creating a relatively stable business environment for the oil and gas manufacturing industry.

Meanwhile, as growth in the onshore conventional oil and gas supply is limited, non-conventional and offshore oil and gas resources will gradually become the main sources of growth in oil and gas production in the future. The exploration and exploitation of non-conventional gas has become increasingly important in the PRC and other countries and is expected to bring enormous business opportunities to the oil and gas equipment manufacturing industry. The Group will continue to focus on enhancing its technical and equipment reserves in the field of non-conventional oil and gas exploration. The Group will also push ahead with the construction of its offshore production base and propel the research and development in offshore engineering equipment, so as to capture the business opportunities arising from the growing market demand for the related drilling equipment.

Looking forward, the Group will endeavor to capture opportunities arising from the steady development of the industry. The Group will further its input in research and development of products and convert its technical advantages into market advantages. It will promote new products addressing the changing market needs in a timely manner, reinforce the diversification and differentiation in products, and constantly improve its technical services so as to consolidate and enlarge its market share. The Group will further develop the oil and gas engineering business and proactively search for opportunities in investment and partnership with growth prospects along the upstream and downstream production chain.

Leveraging on the strong in-house research and development capability, technical competitiveness, excellent sales network and profound experience in the drilling equipment manufacturing industry, the Group will steadily promote the strategy of interactive development with equipment production as its core business and engineering services and resource exploration as supporting businesses, so as to bring maximised returns to the shareholders.

FINANCIAL REVIEW

During the Period, the Group's gross profit and profit attributable to equity shareholders of the Company amounted to approximately RMB330 million and RMB53 million respectively, while the gross profit and loss attributable to equity shareholders of the Company amounted to approximately RMB162 million and RMB89 million respectively in the same period last year. Gross margin and net margin were 25.5% and 4.1% respectively. During the Period, the increase in gross profit and profit attributable to equity shareholders was mainly due to the significant increase of revenue.

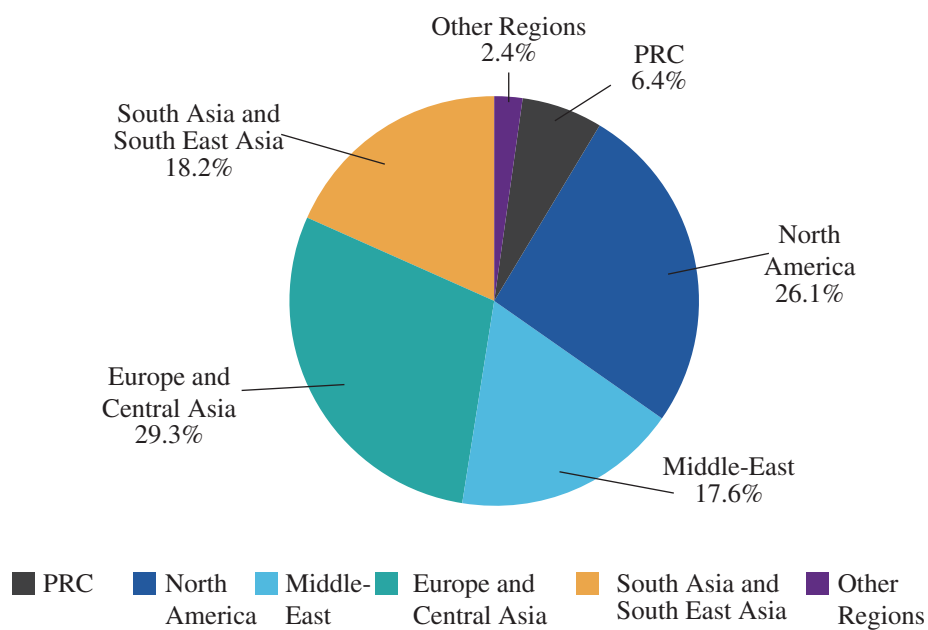
Revenue

During the Period, the Group's revenue amounted to approximately RMB1,295 million, representing an increase of approximately RMB609 million or 88.9% as compared to approximately RMB686 million in the same period last year. The increase in revenue was mainly due to the gradual recovery in the global land drilling rig market which led to growing market demand for land drilling rigs. During the Period, total number of rigs sold increased to 19 units from 9 units in the same period last year.

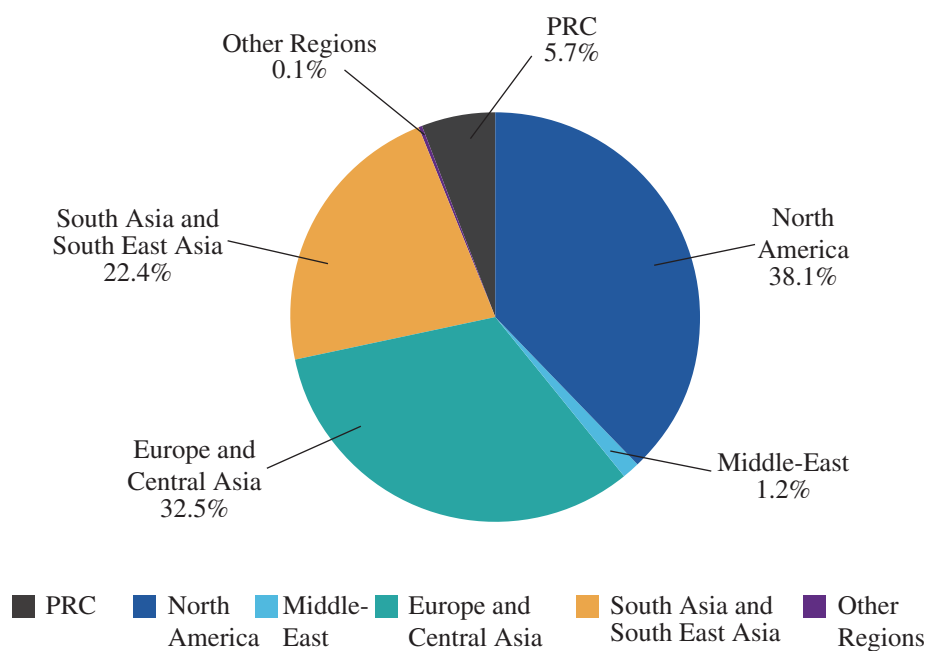
During the Period, revenue by geographical area was as follows: revenue from exports amounted to approximately RMB1,213 million, accounting for approximately 93.6% of the Group's total revenue, representing an increase of RMB566 million as compared to the same period last year. Among which, revenue from the South-Asian and South East-Asian and Middle-Eastern markets increased significantly. During the Period, the sales volume of the said markets increased to 5 and 3 units respectively, as compared to 1 and 0 unit respectively in the same period last year. The European and Central Asian market and the North American market were further penetrated. The sales volume of the said markets increased to 5 and 4 units respectively, as compared to 3 and 3 units respectively in the same period last year. Revenue from other regions and the PRC was roughly equal to that in the same period last year.

Revenue by Geographical Areas

For the six months ended 30 June 2011



For the six months ended 30 June 2010



During the Period, revenue by product categories was as follows:

Revenue by product categories	For the six months ended 30 June 2011			For the six months ended 30 June 2010			2011.1-6 vs 2010.1-6	
	Revenue <i>RMB'000</i>	Proportion (%)	Quantity (unit)	Revenue <i>RMB'000</i>	Proportion (%)	Quantity (unit)	Change <i>RMB'000</i>	Change (%)
Digitally-controlled rigs	846,419	65.4%	15	466,642	68.1%	9	379,777	81.4%
Conventional rigs	61,035	4.7%	4	—	—	—	61,035	
Subtotal	907,454	70.1%	19	466,642	68.1%	9	440,812	94.5%
Parts, components and others	387,836	29.9%		218,954	31.9%		168,882	77.1%
Total	<u>1,295,290</u>	<u>100.0%</u>		<u>685,596</u>	<u>100.0%</u>		<u>609,694</u>	88.9%

During the Period, revenue from drilling rigs and parts, components and others were RMB907 million and RMB388 million respectively, representing an increase of 94.5% and 77.1% as compared to RMB467 million and RMB219 million in the same period last year.

Drilling rigs comprised of digitally-controlled land rigs and conventional land rigs, revenue from which amounted to RMB846 million and RMB61 million respectively during the Period. The increase in revenue from drilling rigs was mainly due to the increase in sales volume of drilling rigs from 9 units in the same period last year to 19 units during the Period, while the average unit price declined to RMB48 million during the Period from RMB52 million in the same period last year. During the Period, the Group recorded sales of 4 heavy 7000-meter drilling rig, 1 heavy 9000-meter drilling rigs, 10 medium 5000-meter drilling rigs, 3 light 3000-meter drilling rigs and 1 light 1000-meter drilling rig.

The increase in revenue from parts, components and others was mainly due to sales of 3 self-manufactured top drives, compared to zero in the same period last year.

Cost of Sales

During the Period, the Group's cost of sales amounted to approximately RMB965 million, representing an increase of approximately RMB441 million or 84.2% as compared to the same period last year. The increase was mainly due to the increase in the Group's revenue.

Gross Profit and Gross Margin

During the Period, the Group's gross profit recorded approximately RMB330 million, representing an increase of RMB168 million as compared to the same period last year. Among which, gross profit from drilling rigs amounted to approximately RMB228 million, representing an increase of 135.1% as compared to the same period last year; gross profit from parts, components and others amounted to approximately RMB102 million, representing an increase of 59.4% as compared to the same period last year.

During the Period, the Group's overall gross margin was 25.5%, representing an increase of 1.9 percentage points as compared to 23.6% in the same period last year.

The gross margin for drilling rigs was approximately 25.1%, representing an increase of 4.3 percentage points as compared to 20.8% in the same period last year. The increase in gross margin was mainly due to the decline of manufacturing expense per drilling rig with the marked increase of revenue during the Period.

Gross margin of parts, components and others was 26.3%, representing a decrease of 3.1 percentage points as compared to the same period last year. The decrease was mainly due to the depreciation of the US dollars against RMB and the decline of average unit price of mud pumps.

Expenses in the Period

During the Period, the Group's selling expenses amounted to approximately RMB76 million, representing an increase of RMB6 million or 8.6% as compared to RMB70 million in the same period last year. The increase was mainly attributable to an increase of approximately RMB10 million in transportation costs due to sales increase, partly offset by the decrease of other selling expenses during the Period.

During the Period, the Group's general and administration expenses amounted to approximately RMB172 million, representing an increase of RMB23 million or 15.4% as compared to RMB149 million in the same period last year. The increase was mainly due to a provision of approximately RMB14 million made for long-aged trade receivables during the Period, while only RMB0.7 million provision for doubtful debts was made in the same period last year, and other general and administration expenses reasonably increased accordingly with the increase of revenue and stricter expense control. For the trade receivables already accrued provision, the Group is actively requesting the settlement.

During the Period, the Group's net financing expenses amounted to approximately RMB6 million, as compared to net financing expenses of RMB46 million in the same period last year. The decrease in net finance expenses was mainly attributable to ups and downs in the exchange rate of the US dollars and Euro against RMB and the Group's strengthened exchange rate risk management, approximately RMB2 million of net exchange loss recorded during the Period, while the relatively large depreciation of Euro against RMB caused a net exchange loss of approximately RMB31 million in the Group's related contract in the same period last year.

Share of Loss from Jointly Controlled Entities

During the Period, the Group's share of loss from jointly controlled entities amounted to approximately RMB5 million, representing an increase of RMB4 million as compared to share of loss of approximately RMB1 million in the same period last year.

Share of Profit from an Associate

During the Period, the Group's share of profit from an associate amounted to approximately RMB2 million, while there was no such investment in the same period last year.

Profit/Loss before Taxation

During the Period, profit before taxation of the Group amounted to approximately RMB75 million, whereas loss before taxation was approximately RMB101 million in the same period last year. The profit was mainly attributable to significant increase in revenue and gross margin.

Income Tax Expenses/Credit

During the Period, the Group's income tax expenses amounted to approximately RMB15 million, as compared to the income tax credit of approximately RMB12 million in the same period last year. The expense was mainly attributable to the profit before taxation of the Group. In addition, the equity-settled share-based payment expenses of RMB4 million (the same period of 2010: RMB10 million) were not deductible from income tax calculation during the Period.

Profit/Loss for the Period

During the Period, the Group's profit amounted to approximately RMB60 million, as compared to a loss of approximately RMB89 million in the same period last year. Among which, profit attributable to equity shareholders of the Company was approximately RMB53 million, while earnings attributable to non-controlling interest was approximately RMB7 million. During the Period, net profit margin was 4.1%, as compared to a net loss margin of 13.0% in the same period last year, which was mainly attributable to the significant decrease in the ratio of expenses to sales due to the marked increase in revenue during the Period.

Earnings before Interest, Taxes, Depreciation and Amortisation ("EBITDA") and EBITDA Margin

During the Period, EBITDA amounted to RMB130 million, as compared to an EBITDA loss of approximately RMB13 million in the same period last year, which was mainly due to the marked increase in operating profit for the increase in revenue. The EBITDA margin was 10.1%, as compared to a loss margin of 1.8% in the same period last year, which was mainly attributable to the increase of gross margin and the significant decrease in the ratio of expenses to sales as compared to the same period last year due to the significant increase in revenue during the Period.

Dividend

For the period ended at 30 June 2011, the Board does not recommend the payment of interim dividend.

Source of Capital and Borrowings

The Group's principal sources of capital include listing proceeds, cash from operations, and bank borrowings.

At 30 June 2011, the Group's bank borrowings amounted to approximately RMB1,012 million, representing an increase of approximately RMB386 million as compared to 31 December 2010. Among which, borrowings repayable within one year amounted to approximately RMB770 million, representing an increase of RMB326 million as compared to 31 December 2010. The increase of borrowings are mainly due to the increase of capital requirement accordingly with the increase of business.

Deposit and Cash Flow

At 30 June 2011, the Group's cash and cash equivalents amounted to approximately RMB1,421 million, representing an increase of approximately RMB418 million as compared to 31 December 2010.

During the Period, the Group's net operating cash outflow amounted to approximately RMB226 million; net cash inflow from investing activities amounted to approximately RMB285 million, which was due to the proceeds from sales of other financial assets during the period; net cash inflow from financing activities amounted to approximately RMB367 million, which was mainly for the proceeds from new bank loans; and net cash outflow for the effect of foreign exchange rates changes amounted to approximately RMB8 million.

Assets Structure and Changes Thereof

At 30 June 2011, the Group's total assets amounted to approximately RMB6,312 million, representing an increase of approximately RMB318 million or 5.3% as compared to 31 December 2010. Among which, current assets amounted to approximately RMB4,686 million, which were mainly listing proceeds, inventories and trade receivables and accounted for approximately 74.3% of total assets. Non-current assets amounted to approximately RMB1,626 million, accounting for approximately 25.7% of total assets.

Liabilities

At 30 June 2011, the Group's total liabilities amounted to approximately RMB2,188 million, representing an increase of approximately RMB264 million as compared to 31 December 2010. Among which, current liabilities amounted to approximately RMB1,932 million, accounting for approximately 88.3% of total liabilities. Non-current liabilities amounted to approximately RMB256 million, accounting for approximately 11.7% of total liabilities. At 30 June 2011, the Group's gearing ratio was approximately 34.7%, representing an increase of 2.6 percentage points as compared to 31 December 2010.

Total Equity

At 30 June 2011, total equity amounted to RMB4,124 million, representing an increase of RMB54 million as compared to 31 December 2010. Total equity attributable to equity shareholders of the Company amounted to approximately RMB4,010 million, representing an increase of RMB46 million as compared to 31 December 2010. Non-controlling interests totaled to approximately RMB115 million, representing an increase of RMB7 million as compared to 31 December 2010. Net asset value reached approximately RMB1.24 per share, representing an increase of RMB0.01 as compared to RMB1.23 at 31 December 2010. During the Period, the Group's earnings per share was approximately RMB1.64 cents, representing an increase of RMB4.41 cents as compared to loss per Share of RMB2.77 cents in the same period last year.

Contingent Liabilities and Pledge

As at 30 June 2011, the Group's contingent liabilities was mainly due to the disputes with 64 natural persons. Based on the PRC legal advisor's opinion, these 64 original investors had never been properly registered as shareholders of Honghua Company with the competent PRC government authority, there is no legal basis under the PRC law for them to be regarded as shareholders of Honghua Company. In addition, the Group considered that sufficient provision in legal costs in respect of the dispute has been made at 30 June 2011.

The Group has pledged bank deposits of approximately RMB76 million, representing an increase of approximately RMB47 million as compared with that at 31 December 2010.

Capital Expenditure, Major Investment and Capital Commitments

During the Period, capital expenditure of the Group on infrastructure and technical improvements amounted to approximately RMB273 million, representing an increase of approximately RMB198 million as compared to the same period last year. This was mainly due to the development of offshore construction projects and input of drilling rigs for oil & gas engineering services.

At 30 June 2011, the Group had capital commitments of approximately RMB1,903 million, which will be used for the construction of Jiangsu Qidong offshore manufacturing base and expand the Group's business as well as its production capacity.

Foreign Currency Risk

The Group has certain foreign currency deposits. At 30 June 2011, the Group's foreign currency deposits were equivalent to approximately RMB62 million, trade receivables and other receivables denominated in foreign currency were equivalent to approximately RMB711 million. Exports and foreign currencies settled business exposed the Group to exchange risk.

Use of Proceeds from the Initial Public Offerings

The net proceeds after the deduction of the related expenses from the initial public offering were approximately HK\$2,958 million. The Group has used the net proceeds obtained from initial public offerings in accordance with the “Use of Proceeds” in the prospectus of the Company issued at 25 February 2008. As at 30 June 2011, the use of the net proceeds was as follows: proceeds of HK\$975 million to be used for the offshore project, among which HK\$535 million has been incurred; proceeds of HK\$592 million to be used for the enlargement of oil and gas exploration, provision of products and services, oil and gas engineering services and oil and gas resources exploration, as well as other businesses which can create profitability for the Group, among which HK\$72 million has been incurred; proceeds of HK\$354 million to be used for production capacity expansion and research and development expenses, among which all has been incurred; proceeds of HK\$1,037 million to be used as working capital and day to day expenses, all has been incurred.

Employee Remuneration and Benefits

During the Period, the average number of the Group’s employees was 3,997. The total remuneration and benefit amounted to approximately RMB162 million, representing an increase of RMB25 million or approximately 18.2% as compared to the same period last year. It was mainly attributable to further development in the new offshore engineering business and penetration into the oil and gas drilling market. During the Period, 403 additional personnel were employed and approximately RMB13 million labor cost was added as compared to the same period last year.

The Group continuously optimised its organisational and workforce structure, as well as made adjustments to roles and responsibilities according to its human resources planning. The Group continued to take efficient measures in reducing staff costs and proactively introduced strategic talents. According to its remuneration policy, the Group offered remuneration based on employees’ job duties and individual capability in order to establish a competitive and fair system. The Group also emphasised on team work and individual work performance, as well as clearly established rewards and penalties, and delivered the Group’s organisation goals to the staff, allowing them to achieve them through team work. The Group strives to enhance the remuneration and benefits system, so as to achieve its goals and promote its teams to improve performance, and enhance the working ability, job satisfaction and sense of accomplishment of its employees.

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

Neither the Company nor any of its subsidiaries has purchased, sold or redeemed any of the Company’s Shares during the six months ended 30 June 2011.

AUDIT COMMITTEE

The Audit Committee comprises all the Independent Non-executive Directors with written terms of reference in compliance with the Listing Rules. The Audit Committee is responsible for reviewing and supervising financial reporting process and internal control systems of the Group and providing advices and recommendations to the Board. The Audit Committee shall hold at least two meetings a year and review opinions of internal auditors, matters in respects of internal control, risk management and financial reporting. The Audit Committee has reviewed the interim results of the Group for the six months ended 30 June 2011.

COMPLIANCE WITH THE CODE ON CORPORATE GOVERNANCE PRACTICES

The Company has complied with the principles as set out in the CG Code throughout the six months ended 30 June 2011, except the following deviations:

Based on the Rule A.2.1 of CG Code, the positions of Chairman and President (Chief Executive Officer) should be separated and should not be performed by the same individual. However, Mr. Zhang Mi is the Chairman of the Board and President (Chief Executive Officer) of the Company. Mr. Zhang Mi is the main founder of the Group and has extensive experiences in the industry and related industries. In the opinion of the Board, the vesting of duties of Chairman of the Board and President (Chief Executive Officer) of the Company to Mr. Zhang Mi would provide a strong and consistent leadership and allow effective planning and executing business decisions and strategies, as well as ensure the interests of the shareholders as a whole. On the other hand, the balance between powers and duties could be ensured through the operation of the Board and the committees under it. The Company will continue to review the effectiveness of the Group's corporate governance structure and consider whether it needs to make any changes, including the separation of duties of Chairman of the Board and President (Chief Executive Officer) of the Company.

MODEL CODE FOR SECURITIES TRANSACTIONS BY DIRECTORS

The Company has adopted a set of Code for Securities Trading, the strict level of which is no less exacting than that of the Model Code. After the specific enquiry by the Company, all the Directors have confirmed that they have complied with the standards specified in both of the Code for Securities Trading and the Model Code throughout the six months ended 30 June 2011.

PUBLICATION OF INTERIM RESULTS ANNOUNCEMENT AND INTERIM REPORT FOR THE SIX MONTHS ENDED 30 JUNE 2011

This announcement will be published on both the websites of the Company (www.hh-gltd.com) and of the Stock Exchange (www.hkexnew.hk). The interim report of the Company for the six months ended 30 June 2011 will be dispatched to shareholders and published on the aforesaid websites in due course.

DEFINITION

“Audit Committee”	:	the audit committee of the Company
“Board”	:	the Board of Directors of the Company
“Code for Securities Trading”	:	code for securities trading adopted by the Company since 21 January 2008
“Company” or “Honghua Group”	:	Honghua Group Limited
“CG Code”	:	Code on Corporate Governance Practices set out in Appendix 14 to the Listing Rules
“Directors”	:	directors of the Company
“Group”	:	the Company and its subsidiaries, its associate and its jointly controlled entities
“HK\$” or “HK dollars”	:	Hong Kong dollars, the lawful currency of Hong Kong
“Hong Kong”	:	the Hong Kong Special Administrative Region of the PRC
“Listing Rules”	:	the Rules Governing the Listing of Securities on The Stock Exchange (as amended from time to time)
“Model Code”	:	Model Code for Securities Transactions by Directors of Listed Issuers set out in Appendix 10 to the Listing Rules
“Period”	:	the six months ended 30 June 2011
“PRC” or “China”	:	the People’s Republic of China, unless the context requires otherwise, reference in this announcement of the PRC or China excludes Hong Kong, the Macau Special Administrative Region of the PRC and Taiwan
“RMB”	:	Renminbi, the lawful currency of the PRC

“same period last year”	:	the six months ended 30 June 2010
“Share(s)”	:	ordinary shares issued by the Company, with a nominal value of HK\$0.10 each
“Stock Exchange”	:	The Stock Exchange of Hong Kong Limited
“US\$”	:	United States of America dollars, the lawful currency of the United States of America

APPRECIATION

On behalf of the Board, I would like to take this opportunity to express heartfelt thanks to management and all employees for their hard work in the past and thanks to the shareholders, business partners and investors for their continuous support.

On behalf of the Board of
Honghua Group Limited
Zhang Mi
Chairman

Hong Kong, 24 August 2011

As at the date of this announcement, our directors are Mr. Zhang Mi (Chairman), Mr. Ren Jie and Mr. Liu Zhi as executive Directors, Mr. Huang Dongyang and Mr. Siegfried Meissner, as non-executive Directors, and Mr. Liu Xiaofeng, Mr. Qi Daqing, Mr. Tai Kwok Leung Alexander, Mr. Chen Guoming, Mr. Shi Xingquan and Mr. Guo Yanjun as independent non-executive Directors.