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)

ANNOUNCEMENT IN RELATION TO THE REPLY TO THE SHENZHEN STOCK EXCHANGE'S INQUIRY LETTER FOR ANNUAL REPORT 2019

The Company and all members of the Board of Directors hereby guarantee that there is no false record, misleading statement or major omission in the contents of the announcement and they will undertake the individual and joint liabilities for the authenticity, accuracy and completeness of its contents.

Shandong Molong Petroleum Machinery Company Limited (hereinafter referred to as the "Company") received the SME Board Inquiry Letter for Annual Reports [2020] No. 13 Inquiry Letter for the annual report 2019 of Shandong Molong Petroleum Machinery Company Limited (hereinafter referred to as the "Inquiry Letter") from the Corporate Management Department of the SME Board of the Shenzhen Stock Exchange on 10 April 2020, pursuant to which the Company made the following reply to the relevant questions:

1. **According to the annual report, products of the Company, such as pipes for petroleum and gas extraction, fluid and structural pipes are mainly used in the exploitation of energy sources such as oil and natural gas, and are within the scope of energy equipment manufacturing industry. The development and prosperity of the industry of energy sources exploitation such as oil and natural gas are directly related to the development of the industry in which the Company operates. During the reporting period, operating revenue – pipe products and operating revenue – tube blanks of the Company were RMB3,457 million and RMB699 million respectively, representing a decrease of 11.8% and an increase of 136% year-on-year respectively. Gross profit margin of pipe products and tube blanks for the period were 10.03% and -2.1% respectively, representing a decrease of 7.02% and 4.15%. During the reporting period, sales and production volumes of special equipment manufacturing sector of the Company were 874,900 tons and 880,300 tons respectively, representing an increase of 12.82% and 9.74% year-on-year respectively.**

(1) In terms of sales and production volumes of the Company's pipe products and tube blanks for the period, illustrate the changes in average sales price and purchase price of the Company's pipe products and tube blanks in the last three years, and illustrate the rationality of the changes in the average sales price and purchase price of the pipe products and tube blanks in terms of the downstream demand analysis of the Company's products and the price analysis of similar products of peer companies:

Reply:

1) Analysis of changes in average sales price of pipe products and tube blanks:

During the reporting period, there were no significant changes in the total sales volume of the Company's pipe products as compared with the previous year, but the sales volume of casings decreased significantly by approximately 18.23% year-on-year. Affected by the volatility of international crude oil prices, prices of Brent crude oil futures increased from US$45.23/barrel in July 2017 to US$86.74/barrel in October 2018, representing a rapid growth of international crude oil prices. Oil and gas companies, under such influence, continued to increase oil and gas exploration and development inputs, resulting in an increase in demand for the Company's casing and its sales volume. Since November 2018, however, attributed to the commencement of international crude oil prices downward fluctuation and factors such as Sino-US economic and trade frictions, sluggish global economy, the Company has been facing an increasing downward pressure of the industry, resulting in a significant decrease in market demand for casing products. In addition, PetroChina Company Limited, the largest customer of the Company, began to perform centralized purchase in advance for winter storage and partial demand for 2019 in November 2018, resulting in a decrease in the demand for products during the reporting period. The above reasons led to a decline in the Company's sales volume of casing products during the reporting period and product prices fell by 2.04% compared with that of last year.

Market demand for general pipes and tube blanks was relatively large, and the sales volume of the Company's general pipe products during the reporting period recorded an increase of 25.28% year-on-year, while the sales volume of tube blanks increased by 148.12% year-on-year. The price of general pipe products, however, declined by 12.84% compared with that of last year as affected by the market situation of steel industry in 2019.

① Changes in average sales price of the Company's pipe products and tube blanks in the past three years are as follows:

Unit: RMB/ton

Product	**2019 Average sales price**	**2018 Average sales price**	**2019 increase/ decrease compared with 2018**	**2017 Average sales price**
Pipe products	5,180.37	5,665.35	–8.56%	4,542.53
Tube blanks	3,366.36	3,535.04	–4.77%	2,365.91

② Changes in average sales price of peer comparable's similar products in the past three years are as follows:

Unit: RMB/ton

Product	**2019 Average sales price**	**2018 Average sales price**	**2019 increase/ decrease compared with 2018**	**2017 Average sales price**
Seamless pipes	4,833.33	5,237.50	–7.72%	4,755.00
Hot rolling tube blanks	3,869.09	4,131.67	–6.36%	3,788.33

Note: Extracted from data published on www.mysteel.com.

As it is difficult to obtain the sales price data of similar products of peer listed companies, the Company inquired the sales data of similar products published on www.mysteel.com, and compared with the sales price of the Company's pipe products and tube blanks. The decrease in average sales price of the Company's pipe products and tube blanks is in line with the price change trend of similar products of peer comparables.

2) **Analysis of changes in average purchase price of raw materials:**

① Changes in average purchase price of the Company's main raw materials in the past three years are as follows:

Unit: RMB/ton

Raw materials	**2019 Average purchase price**	**2018 Average purchase price**	**2019 increase/ decrease compared with 2018**	**2017 Average purchase price**
Steel scrap	2,350.01	2,206.53	6.50%	1,540.50
Mineral dust	600.82	433.1	38.73%	412.14

Analysis of changes in market price of steel scrap: In 2019, the price of steel scrap in Shandong Province remained at a high level. The price of heavy scrap (excluding tax) fluctuated at RMB2,300 to RMB2,600/ton. In 2017 to 2019, the average sales prices of heavy steel scrap (excluding tax) in Shandong were RMB1,662/ton, RMB2,189/ton and RMB2,419/ton respectively, of which the price in 2019 increased by approximately 10.51% compared with 2018 and 45.55% compared with 2017. (source: www.mysteel.com)

Analysis of changes in market price of mineral dust: In 2019, affected by the collapse of tailings dam of Vale S.A. in Brazil and hurricane in Australia, the price of iron ores rose significantly compared with the previous year. According to the data of Lange Steel Information Research Center, from January to November 2019, the average price of iron ores imported through Chinese customs was $95.69/ton, representing an increase of 35.8% as compared with the corresponding period last year. (source: www.lgmi.com)

As it is difficult to obtain the purchase price data of the same kind of raw materials of peer listed companies, the Company compared the changes in the price of raw materials published by third parties for analysis. The change trend of the purchase price of the Company's main raw materials is basically in line with that of the market price.

(2) In terms of the development of the industry, analysis of competitors and changes in the gross profit margins of peer comparables during the reporting period, illustrate the reasons and rationality for the decrease in the gross profit margin of the Company during the reporting period. Annual audit accountant please verify and give clear opinion.

Reply:

① Changes in gross profit margin of the Company's pipe products and tube blanks in the past three years are as follows:

Items	2019 Gross profit margin	2018 Gross profit margin	2019 increase/ decrease compared with 2018	2017 Gross profit margin
Pipe products	10.03%	17.04%	–7.01%	7.55%
In which: Casings	15.36%	17.33%	–1.97%	21.89%
General	–0.28%	16.30%	–16.58%	–3.43%
Tube blanks	–2.10%	2.05%	–4.15%	4.49%

② Changes in gross profit margin of peer listed companies in 2019 are as follows:

	Shangdong Molong		Valin Steel		Daye Special Steel	
Items	Gross profit margin	YOY increase/ decrease	Gross profit margin	YOY increase/ decrease	Gross profit margin	YOY increase/ decrease
Casings (or similar products)	15.36%	–1.97%	17.76%	1.15%	19.21%	–0.50%

Note: There is no data from peer listed companies for general pipe products.

③ Changes in gross profit margin of peer listed companies in 2019 are as follows:

	Shandong Molong		Shandong Iron and Steel		Jiangsu Shagang	
Items	Gross profit margin	YOY increase/ decrease	Gross profit margin	YOY increase/ decrease	Gross profit margin	YOY increase/ decrease
Tube blanks (or similar products)	–2.10%	–4.15%	9.24%	–3.72%	8.24%	–13.55%

Through the comparative analysis of the changes in gross profit margin of similar products of peer listed companies, the changes in gross profit margin of the Company's products are basically in line with those of the peers.

Products of the Company are mainly used in the exploitation of energy sources such as oil and natural gas, and are within the scope of energy equipment manufacturing industry. In the long run, demand for oil and gas would be on the rise. Due to the increasing reliance on imported crude oil and natural gas as well as the prominent energy safety issues, there are urgent needs for importation instead of increasing the self-development rate. In recent years, the government has rolled out various policies to encourage exploration and development of oil and gas resources, and oil companies are required to fulfill their responsibilities of increasing reserves and production. Domestic oil companies have formulated their seven-year action plan to increase inputs to the exploration and development of oil and gas. With the acceleration of oil and gas production and the increasing oil and gas capital expenditures, the domestic energy equipment and oil service industry was expected to become more prosperous.

In 2019, after three years of "eliminating excess capacity" of the steel industry, the policy benefit brought by the supply-side structural reform has been gradually declining, the high supply pressure of the steel industry appears and the market price of steel is on its decline trend, coupled with the enterprises' profit compromised by the surge of iron ore price, the profitability of the industry drops significantly. Despite within the scope of energy equipment manufacturing industry, the Company is greatly affected by the material cost and product price of the steel industry. According to the comparative analysis of the data published by the peers and third parties, the changes in gross profit margin of the Company's pipe products and tube blanks in 2019 is basically in line with the change trend of the market price of the peers.

Verification opinion from accountant:

We have performed the relevant audit procedures and are of the view that the reasons for the changes in average sales price and purchase price of the Company's pipe products and tube blanks and for the decrease in the gross profit margin are rational.

For details, please refer to the Special Description of Inquiry Letter for the Annual Report 2019 of Shandong Molong Petroleum Machinery Company Limited issued by Shinewing Certified Public Accountants Ltd. (Special General Partner).

2. **During the reporting period, the aggregate sales to the Company's five largest customers accounted for 47.91% of the total sales for the year, while the aggregate purchases from the five largest suppliers accounted for 27.94% of the total purchases for the year.**

    (1) **Illustrate whether the internal control system and operating process related to the Company's customer and supplier management, sales and purchase are strictly implemented in accordance with the relevant system:**

    Reply:

    The Company's internal control system related to customer and supplier management, sales and purchase mainly includes "Material Procurement and Management System", "Supplier Management System", "Sales Business Management System", Customer Credit Management System", "Sales Contract, Order, Organization Production Management Measures", "accounts receivable Management System" and Contract Management System".

    In terms of sales, the Company first evaluates the qualification of new customers, understands their operation and assets and credit status through various ways, and fully evaluates their assets and credit status. The Company's sales operation process is: customer credit evaluation → sales negotiation → contract signing → order production → production complete and warehousing → delivery → examination and acceptance by customers → invoicing and payment → after sales service. In this operation process, the Company focuses on strengthening the review of relevant business contracts. Except for the oilfield customers with long-term cooperation are allowed sales on credit, sales to traders and other customers are settled by advance payment or cash on delivery. In order to further reduce the risk of accounts receivable management, the Company has established a specific accounts receivable management team to strengthen the collection and related management of accounts receivable.

    In terms of purchase, the Company first evaluates the qualification of new suppliers, and only qualified suppliers may carry out business with the Company. The Company's purchase control process is: supplier evaluation → supplier selection and pricing → contract signing → goods inspection and warehousing → payment settlement. In this operation process, the Company focuses on strengthening the control of goods transfer after payment. When making payment, the finance department shall strictly review the contract, invoice and integrity of approval process related to payment.

    The Company's customer and supplier management, sales and purchase operations have strictly implemented the Company's internal control system and relating operating process.

(2) Illustrate whether the business scope, business qualification and business and personnel scales of the five largest customers and suppliers of the Company correspond with the sales or purchase scale of the Company:

Reply:

① Basic information of the five largest customers of the Company in 2019 are as follows:

No.	Name of customer	Registered capital (RMB'0,000)	Nature of company	Business scope and nature	Number of staff
1	Petro China Company Limited	18,302,097	Large central government owned enterprise	Exploration and development of oil and natural gas etc.	700,000-800,000
2	Beijing Sanliyuanchen Steel Pipe Sale Center	1,000	Private Enterprise	Production and trading of metal materials etc.	40-50
3	Shaanxi Yanchang Petroleum (Group) Company Limited	1,000,000	Large state-owned enterprise	Exploration and development of oil and natural gas etc.	130,000-150,000
4	Shandong Tianbao Industry and Trade Company Limited	15,789.47	Private Enterprise	Trading of steel etc.	500-600
5	Tianjin Huayuan Xingye Steel Sales Company Limited	2,000.00	Private Enterprise	Trading of steel etc.	40-50

The Company is a listed company specializing in energy equipment design and research, processing and manufacturing, sales service and export trading. Its products are mainly petroleum machinery products, and its main customers are PetroChina, Yanchang Petroleum, Sinopec and CNOOC. Among them, PetroChina, Sinopec and CNOOC are central government owned enterprises, and Yanchang Petroleum is a large state-owned enterprise in Shaanxi Province. In addition to petroleum machinery products, the Company also produces fluid and structural pipes and tube blanks, and its main customers are large steel traders. Beijing Sanliyuanchen Steel Pipe Sale Center is the Beijing branch of Liaocheng Jialong Tube Industry Manufacture Company Limited, which is a large enterprise specializing in manufacturing seamless steel pipes. Shandong Tianbao Industry and Trade Company Limited is an outstanding agent of large steel companies such as Rizhao Steel Company Limited and Tianjin Steel Company Limited. Tianjin Huayuan Xingye Steel Sales Company Limited is a major trading company of mass materials, such as various kinds of pipe materials in North China.

In conclusion, the business scope, business qualification and personnel and business scales of the five largest customers of the Company in 2019 correspond with the sales scale of the Company.

② Basic information of the five largest suppliers of the Company in 2019 is as follows:

No.	Name of supplier	Registered capital (RMB'0,000)	Business scope and nature	Number of staff
1	Shandong Shouguang Juneng Thermoelectric Development Company Limited	30,000	Production and supply of electricity and heat etc.	600-700
2	Shouguang Sensheng Environmental Technology Company Limited	3,000	Wholesale of renewable resources etc.	50-60
3	Xuyang Beifang (Tianjin) Environmental Technology Company Limited	2,000	Recycle of productive metal scrap etc.	40-50
4	Shouguang Ruichuang Renewable Resource Company Limited	500	Recycle and wholesale of renewable resources etc.	30-40
5	Kangjia Huanjia Environmental Technology Company Limited	18,000	Recycle of waste material etc.	90-100

Among the above five largest suppliers, Shandong Shouguang Juneng Thermoelectric Development Company Limited is a thermal power generation enterprise in Shouguang City, providing electricity for various enterprises in Shouguang City, including the Company's subsidiary Shouguang Baolong Petroleum Equipment Company Limited. Steel scrap is one of the main raw materials of the Company's subsidiary Shouguang Baolong Petroleum Equipment Company Limited, which are mainly purchased from companies specializing in trading of metal scrap. Among the above suppliers, Shouguang Sensheng Environmental Technology Company Limited, Xuyang Beifang (Tianjin) Environmental Technology Company Limited, Shouguang Ruichuang Renewable Resource Company Limited and Kangjia Huanjia Environmental Technology Company Limited have steel scrap trading qualification, and their personnel and business scale can ensure the Company's demand for steel scrap purchase.

In conclusion, the business scope, business qualification and personnel and business scales of the five largest suppliers of the Company in 2019 correspond with the purchase scale of the Company.

(3) Illustrate whether the five largest customers and suppliers and their respective controlling shareholders and beneficial controllers are related to the Company, the Company's beneficial controllers, shareholders who own more than 5% of the Company and directors, supervisors and senior executives.

Reply:

It is verified that the above five largest customers and suppliers and their respective controlling shareholders and beneficial controllers are not related to the Company, the Company's beneficial controllers, shareholders who own more than 5% of the Company and directors, supervisors and senior executives.

The annual auditor please: (1) illustrate the specific external confirmation of the five largest customers and suppliers of the Company in the reporting period, including but not limited to the object and amount of the external confirmation, reply status and whether alternative tests have been carried out; (2) illustrate the specific internal control test carried out on the sales and revenue cycle and procurement and cost cycle, and whether they are aware of any unusual situation.

Verification opinion from accountant:

Accountants carried out external confirmation of the five largest customers and suppliers. Through internal control tests by means of interviews, observations, examination and re-exercise, Shandong Molong was regarded to keep an effective internal control on financial report in relation to sales and revenue cycle, procurement and cost cycle in accordance with General Rules on Internal Control for Enterprises and relevant requirements on 31 December 2019.

For details, please refer to the Special Description of Inquiry Letter for the Annual Report 2019 of Shandong Molong Petroleum Machinery Company Limited issued by Shinewing Certified Public Accountants Ltd. (Special General Partner).

3. **At the end of the reporting period, the book balance of the Company's inventory was RMB957 million, and the provision for impairment of inventory was RMB21.73 million. The gross profit margin of the Company's main products, tube blanks, for the period was -2.1%. Please illustrate the balance of inventory – tube blanks and the provision for impairment of inventory, and, in terms of the calculation process of net realisable value of inventory – tube blanks, illustrate whether the provision for impairment of inventory – tube blanks was sufficient and prudent. The annual audit accountant please verify and give clear opinion.**

Reply:

The Company's inventory at the end of the period is measured at the lower of cost and net realizable value. Net realizable value of inventory directly held for sale, such as goods-in-stock, work-in-progress and held-for-sale raw materials is determined by their estimated sales price less the estimated cost of sales and related selling expenses and taxes. Net realizable value of held-for-production raw materials is determined by the estimated sales price of finished products by which they produced less the estimated production cost, estimated cost of sales and related selling expenses and taxes.

At the end of the reporting period, the balance of "inventory – tube blanks" held-for-sale was RMB17.0476 million. The Company measures the above inventory at the lower of net realizable value and cost at the end of the period. The above tube blanks for external sales are mostly produced by order, and their net realizable value is determined by the signed contract price (or with reference to similar products) less estimated sales cost and related expenses and taxes. Provision for impairment of inventory is made for the part of net realizable value less than the inventory cost. At the end of the reporting period, RMB857,800 of provision for impairment of "inventory – pipe blanks" has been made. The above provision for impairment of pipe blanks accounted for 5.03% of the book balance of pipe blanks. Details are shown in the following table:

Types of inventory	Amount of inventory (tons)	Cost of inventory (RMB'0,000)	Net realizable value (RMB'0,000)	Provision for impairment of inventory (RMB'0,000)
Inventory – tube blanks	4,857.71	1,704.76	1,618.98	85.78

As analyzed above, the provision for impairment of "inventory – tube blanks" of the Company for the period was sufficient and prudent.

Verification opinion from accountant:

We have performed the relevant audit procedures and are of the view that the Company has made provision for impairment of tube blanks inventory at the end of the period in a sufficient and prudent way in accordance with the Accounting Standards for Business Enterprises.

For details, please refer to the Special Description of Inquiry Letter for the Annual Report 2019 of Shandong Molong Petroleum Machinery Company Limited issued by Shinewing Certified Public Accountants Ltd. (Special General Partner).

4. **At the end of the reporting period, the balance of other receivables of the Company from administrative units was RMB26.00 million, of which RMB14.53 million and RMB7.25 million were from Shouguang City Yang Kou Town Office of Finance and Shouguang City Yang Kou Town Statistic Center of Finance, Political, Economic and Management Affairs, with an aging of over 5 years and 3 years respectively, and the provision for bad debt at the end of the period was RMB2.6154 million and RMB2.1284 million respectively. During the reporting period, the Company has written off RMB35.87 million of other receivables from JESORO OIL LTD. As of the end of 2018, the Company has made provision for bad debt for these other receivables in full, for the reason that JESORO OIL LTD was deregistered.**

(1) **Illustrate the reasons for the generation and specific nature of other receivable balance of the Company from Shouguang City Yang Kou Town Office of Finance and Shouguang City Yang Kou Town Statistic Center of Finance, Political, Economic and Management Affairs, as well as whether the basis for the provision of bad debt is sufficient.**

Reply:

1) **Reasons for the generation and specific nature of other receivable – Shouguang City Yang Kou Town Office of Finance and Shouguang City Yang Kou Town Statistic Center of Finance, Political, Economic and Management Affairs**

On 24 March 2013, the Company entered into a project construction agreement with Shouguang City Yang Kou Town Office of Finance, pursuant to which the Company shall pay a construction deposit of RMB14.53 million prior to the commencement of the project construction, and such deposit shall be returned to the Company after the completion of the project construction which was in 2016. The Company paid the construction deposit to Shouguang City Yang Kou Town Office of Finance in accordance with the agreement on 1 April 2013.

On 10 June 2014, Shouguang City Yang Kou Town Statistic Center of Finance, Political, Economic and Management Affairs provisionally borrowed RMB10.10 million from the Company for a term of 3 years and agreed to repay one-third of the total principal of the loan and all interest from the previous year on 30 May every year. On 21 December 2015 and 27 February 2018, Shouguang City Yang Kou Town Statistic Center of Finance, Political, Economic and Management Affairs repaid RMB3.37 million and RMB1.00 million of the principal to the Company, with a balance of RMB5.73 million outstanding. On 31 December 2015 and 31 December 2016, the Company made provision for loan interest of RMB1.13 million and RMB0.39 million respectively as agreed. In consideration of Shouguang City Yang Kou Town Statistic Center of Finance, Political, Economic and Management Affairs has not repaid the loan since its two installments of loan principal, the Company no longer made provision for loan interest from 2017. As of the end of 2019, the book balance of other receivables was RMB7.25 million, in which: RMB5.73 million for principal and RMB1.52 million for interest.

Upon the maturity of the above two receivables, the Company has repeatedly negotiated with the people's government of Yangkou Town, Shouguang City. The people's government of Yangkou Town, Shouguang City confirmed the outstanding amount, stating that due to a current capital shortage, the amount shall be repaid once the funds are adequate. Regarding the construction deposit, the government of Yangkou Town pointed out that the local fiscal income decreased significantly due to the impact of the current coronavirus epidemic. A specific repayment time shall be negotiated upon the end of the epidemic. As of the date replying this letter, the government of Yangkou Town repaid RMB0.2 million upon negotiation, and promised to settle the outstanding amount by the end of this year.

2) Basis for the provision of bad debt of other receivable – Shouguang City Yang Kou Town Office of Finance and Shouguang City Yang Kou Town Statistic Center of Finance, Political, Economic and Management Affairs

According to the Accounting Standards for Business Enterprises and accounting policies of the Company, the Group measures other receivables loss provision in accordance with the following circumstances:

① For financial assets whose credit risk has not increased significantly since initial recognition, the Group measures the loss provision based on the expected credit loss in the next 12 months;

② For financial assets whose credit risk has significantly increased since initial recognition, the Group measures the loss provision at an amount equivalent to the expected credit loss over the life of the financial instrument;

③ For purchased or created financial assets that have suffered credit impairment, the Group measures the loss provision at an amount equivalent to the expected credit loss over the entire life of such assets.

Shouguang City Yang Kou Town Office of Finance and Shouguang City Yang Kou Town Statistic Center of Finance, Political, Economic and Management Affairs are subordinate to the people's government of Yangkou Town, Shouguang City. Although relevant amounts have overdue, the Company considers that the risk of bad debt loss from the government is low, and bad debt provision shall be made in accordance with the expected credit loss over the life of the financial instrument as phase two above. Bad debt provision proportion is determined with reference to 6% consolidated finance costs of the Company and the expected credit loss is calculated in accordance with the expected credit loss according to "overdue amount * 6% of capital cost * overdue period".

The construction deposit of Shouguang City Yang Kou Town Office of Finance is RMB14.53 million and shall be repaid upon the completion of project construction at the end of 2016. No bad debt provision shall be made during the construction period. The construction deposit, since 2017 until the end of the reporting period, has overdue 3 years with a provision for bad debt of RMB2.6154 million (RMB14.53 million*6%*3 years).

The balance of loan of Shougang City Yang Kou Town Statistic Center of Finance, Political, Economic and Management Affairs is RMB7.25 million, of which the Company made bad debt provision respectively based on the principal and interest combined with the overdue ageing. The provision for bad debt of other receivables is RMB2.1284 million (RMB5.73 million*6%*5 years+RMB1.13 million*6%*5 years+RMB0.39 million*6%*3 years).

As analyzed above, the Company has made provision for bad debt in full in accordance with prudential principle, which is in compliance with relevant requirements of Accounting Standard for Business Enterprises.

(2) Illustrate the specific time of deregistration of JESORO OIL LTD, the reason and rationality for writting off other receivables of RMB35.87 million from JESORO OIL LTD, and whether the Company has taken active and effective recovery measures.

Reply:

JESORO OIL LTD (hereinafter referred to as "JESORO OIL LTD") cooperated with the Company to explore the Uzbekistan market and has successfully assisted the Company to sign contracts with two customers, namely UNIX Technology Company Limited and Clarkson Company Limited(克松公司), and introduced pipe products into the Uzbekistan market. Upon the entrance of the Company's products into the Uzbekistan market, JESORO OIL LTD is responsible for technical services, inspection, and short-distance transportation of products. As of the end of 2015, the Company signed purchase contracts for an aggregate of 109,500 ton casings with UNIX Technology Company Limited and Clarkson Company Limited(克松公司). The total amount of which was US$151.5997 million. In order to help JESORO OIL LTD commence its business in Uzbekistan as soon as possible and expedite its performance of contracts with UNIX Technology Company Limited and Clarkson Company Limited (克松公司), the Company paid JESORO OIL LTD US$27.1244 million in advance for technical services, inspection, and short-distance transportation as agreed in the contracts. As of the end of 2015, actual contract performed was 70,500 tons of casings, representing a corresponding contract amount of US$96.0181 million. As of the end of 2015, due to a major personnel reshuffle of the Ministry of Oil of Uzbekistan, 39,000 tons of casings in the contracts entered into between UNIX Technology Company Limited and Clarkson Company Limited(克松公司) with Uzbekistan National Oil and Gas Company Limited were not performed, representing a corresponding contract amount of US$55.5816 million. Service fees corresponding to unperformed parts of the contract were US$9.8 million. The Company promptly required JESORO OIL LTD to return the above service fees. Upon negotiations with multiple parties, JESORO OIL LTD returned an aggregate of US$4.7 million during 2015 to 2016. As to date, an amount of US$5.1 million is still not recovered.

Regarding the amount, the Company established a special recovery team, in which the deputy general manager in marketing is the team leader and the export department manager is the deputy team leader, to recover the amount through various measures. Apart from proactive attempts to contact personnel of JESORO OIL LTD, the Company also coordinated with the aforementioned customers to contact and recover the amount for multiple times, and learned about the situation of JESORO OIL LTD through other foreign customers, but no substantial progress has been made.

In consideration of the difficulty in recovering the amount, the Company made bad debt provision of RMB10.6175 million, RMB10.6175 million, and RMB13.78 million from 2016 to 2018 respectively. As of the end of 2018, bad debt provision for such amount of other receivables was made in full. In October 2019, the Company learned through other foreign customers that the company was deregistered at the end of 2018.

In order to give a true picture of the Company's financial situation, on 26 February 2020, the Company held the second extraordinary meeting of the sixth session of the board of directors and the first extraordinary meeting of the sixth session of the board of supervisors, and the "proposal for the write-off of bad debts 2019" has been passed to write off the above receivables.

Verification opinion from accountant:

We have performed relevant audit procedures and are of the view that the provision for bad debt of the above other receivables of the Company is sufficient and the reasons for the write-off of the receivables from JESORO OIL LTD are rational.

For details, please refer to the Special Description of Inquiry Letter for the Annual Report 2019 of Shandong Molong Petroleum Machinery Company Limited issued by Shinewing Certified Public Accountants Ltd. (Special General Partner).

5. **At the end of the reporting period, fixed assets included in outstanding certificate of ownership were workshop plant, office building and staff canteen of Maolong New Materials with a book value balance of RMB253 million. Please explain the reasons for the outstanding of the certificate of ownership, the expected time of process and whether there are major obstacles. The annual audit accountant please verify and give clear opinion.**

Reply:

The area used by Shouguang Maolong New Materials Technology Development Company Limited currently is maritime area. The Company's project construction has applied for the use of maritime area in accordance with the "Maritime Area Use Management Law of the People's Republic of China" and the application has been approved. The project has been submitted to the Weifang Commission of Economy and Informatization for approval. It has passed the energy conservation examination, obtained the maritime area use right certificate, and was approved by the Shandong Provincial Oceanic and Fishery Department on environmental assessment. It has also obtained permits including the construction land planning permit, construction project planning permit and project construction permit. All formalities for construction have been completed. The project was completed, examined and accepted on 25 January 2019.

As the policies regarding the application of state-owned land use right certificate for maritime area are currently not certain, real estate certificates cannot be applied for the above plant and office building and other buildings in the meantime. The Company has been repeatedly communicating with relevant authorities, but the situation could only be solved upon the policies are determined. Besides, please note that the process of the certificate of ownership has no influence on the normal production and operation of Shouguang Maolong New Materials Technology Development Company Limited, and the Company will continue to communicate with relevant authorities to strive for a solution soon.

Verification opinion from accountant:

We have performed relevant audit procedures and are of the view that outstanding certificates of ownership are in line with actual circumstances.

For details, please refer to the Special Description of Inquiry Letter for the Annual Report 2019 of Shandong Molong Petroleum Machinery Company Limited issued by Shinewing Certified Public Accountants Ltd. (Special General Partner).

6. At the end of the reporting period, the closing balance of the Company's goodwill was RMB143 million, which was generated from the acquisition of equity interests of Maolong New Materials not under common control by the Company in 2007. The acquisition constituted a business combination not under common control. At the time of acquisition, Maolong New Materials held 95% equity interest of Weihai Baolong and 75% equity interest of Molong Electro-Mechanical, which in turn held 5% equity interest of Weihai Baolong. As the three newly acquired companies operated and commenced business independently, they formed three asset groups at the time of acquisition. During the reporting period, provision for impairment of goodwill of RMB17.29 million and RMB6.39 million were made by the Company for Weihai Baolong Asset Group and Molong Electro-Mechanical Asset Group respectively. Please illustrate the recognition method and specific test process of the above impairment loss of goodwill, including but not limited to the calculation process of the present value of the estimated future cashflow, forecast growth rate, steady growth rate, profit margin, discount rate, forecast period, etc., and whether the provision for impairment of goodwill in the report period was sufficient and prudent. The annual audit accountant please verify and give clear opinion.

Reply:

According to relevant requirements of the Accounting Standards for Business Enterprises, goodwill is tested at the end of each year for impairment, whether indication of impairment exist or not. When performing impairment test on goodwill that is separately presented in the financial statements, the carrying value of goodwill is allocated to the related asset groups or groups of asset groups which are expected to benefit from the synergies of the business combination. If the result of the test indicates that the recoverable amount of an asset group or group of asset groups to which the goodwill allocated is lower than its carrying amount, the corresponding impairment loss is recognised. The impairment loss is first deducted from the carrying amount of goodwill that is allocated to the asset group or group of asset groups, and then deducted from the carrying amounts of other assets within the asset groups or groups of asset groups in proportion to the carrying amounts of assets other than the goodwill.

(1) Background of the formation of goodwill

On 31 December 2007, the Company acquired Shouguang Maolong Machinery and Electric Co., Ltd. (renamed as "Shouguang Maolong New Material Technology Development Co., Ltd." in November 2013), which owned two controlling subsidiaries, of which it held 95% equity interest of Weihai Baolong Special Petroleum Materials Co., Ltd and 75% equity interest of Shouguang Molong Electro-mechanical Equipment Co., Ltd. The above three newly acquired companies formed three asset groups at the time of acquisition as they were independently operating and independently conducting business.

The acquisition is not under common control. According to Lu ZhengXin Ping Bao [2008] No. 3005 Asset Evaluation Report issued by Shandong Zhengyuan Hexin Asset Appraisal Co., Ltd., the fair value of identifiable assets of Shouguang Maolong Machinery Electric Co., Ltd. attributable to shareholders of the parent was lower than the part that constitutes purchase cost and goodwill of RMB142.9734 million was recognized as of the date of consolidation (31 December 2007).

In 2013, Maolong New Materials began to investigate, demonstrate and prepare for the foundry relocation technology transformation project, which was completed at the end of 2016. Assets and businesses involved in the project are not included in the asset group of the Company at the time of the above acquisition.

(2) Provision for goodwill impairment in 2019

The Company calculates the recoverable value of the asset group by the method of the present value of the estimated future cashflow, and calculates the recoverable value of the asset group that includes the goodwill based on future operation data approved by the Company. The estimated future cashflow is determined based on the cashflow forecast for the next five years approved by the management. The management prepares the pre tax cashflow forecasts for the next five years based on indicators such as historical actual operation data, industry development trend, expected income growth rate and gross profit margin. The growth rate of cashflow adopted beyond five years is expected to be 0. According to the principle consistent with cashflow and discount rate, weighted average capital cost is selected as the discount rate, which is used to discount the net cashflow of asset group related to goodwill in the future as the recoverable amount. The basis for determining the recoverable amount shall be consistent with that of the carrying amount, and the carrying amount of asset group including goodwill is compared with the recoverable amount of that asset group to determine whether the goodwill of the asset group is impaired.

The asset group that includes the goodwill being tested for impairment by the Company in the period is the same as the asset group recognised as at the date on which the goodwill was purchased. The scope included in the test includes asset group constituents: fixed assets, construction in progress, intangible assets and goodwill, etc.

As at 31 December 2019, the forecast period growth rate, steady growth rate, profit margin, discount rate and forecast period relating to asset groups that include goodwill of the Company are illustrated in the following table:

Unit: RMB0'000

Name of asset group	Forecast period	Forecast period operating revenue growth rate	Forecast period average profit margin	Forecast period average net profit	Steady period	Steady period operating revenue growth rate	Steady period profit margin	Steady period net profit	Discount rate	Present value of estimated future net cash flow
Weihai Baolong asset group	2020-2024	12.32%	1.68%	1,536.39	2025 onward	0%	1.71%	1,642.97	13.75%	8,488.86
Molong asset group portfolio	2020-2024	31.55%	16.94%	1,412.00	2025 onward	0%	16.86%	1,466.84	13.04%	5,275.31

In 2019, as affected by factors such as Sino-US economic and trade frictions, sluggish global economy, the sales and prices of products of the Company kept declining, and the profitability of asset group products in relation to goodwill decreased, showing signs of impairment. Weihai Baolong asset group recorded operating revenue of RMB567.3197 million and a net profit of RMB-25.6793 million. Molong asset group portfolio recorded operating revenue of RMB56.2512 million and a net profit of RMB2.0755 million. The Company conducted a preliminary impairment test on goodwill, and engaged Wanlong (Shanghai) Assets Valuation Co. Ltd. to conduct an assessment, and issued assessment reports (Wanlong Ping Bao Zi (2020) No. 10019 and Wanlong Ping Bao Zi (2020) No. 10018). According the results of the impairment test and the assessment which calculates the recoverable value of the asset groups based on the income approach, the Company made provision for goodwill impairment of RMB23.6834 million on the above two asset groups. The calculation process of impairment is as follows:

Unit: RMB0'000

Name of asset group A	Carrying amount of asset groups B	Original value of goodwill attributable to the parent C	Holding ratio of minority shareholders D	Unrecognised book value of goodwill attributable to minority shareholders E=C/(1-D)*D	Total book value of assets and the amount of goodwill F=B+C+E	Recoverable amount of asset groups G	Accrued provision for asset impairment H=B-G	Aggregate provision for goodwill impairment I=F-G-H	Accrued provision for goodwill impairment attributable to the parent J=I*(1-D)	Book value of goodwill impairment made for previous years K	Amount of provision for goodwill impairment to be made for the year L=J-K
Weihai Baolong asset group	8,510.66	10,007.81	1.25%	126.68	18,645.15	8,488.86	21.80	10,134.49	10,007.81	8,279.00	1,728.81
Molong asset group portfolio	5,285.80	2,789.53	25%	929.84	9,005.17	5,275.31	10.49	3,719.37	2,789.53	2,150.00	639.53
Total	13,796.46	12,797.34	–	1,056.52	27,650.32	13,764.17	32.29	13,853.86	12,797.34	10,429.00	2,368.34

Remarks:

① Upon testing, as the amount of the loss of accrued asset impairment was relatively small, no provision for asset impairment was made after provision for goodwill impairment;

② In 2019, some assets were added to Molong asset group portfolio, which increased the book value of the asset group.

(3) Provision for goodwill impairment from 2016 to 2018

① Provision for goodwill impairment in 2016

In 2016, due to the overcapacity of the steel industry, the market demand for the products of the Company and their prices continued to stay low. The results of the Company's goodwill-related asset groups declined significantly, showing signs of impairment. Weihai Baolong asset group recorded operating revenue of RMB169.7980 million and a net profit of RMB-72.1391 million in 2016. Molong asset group portfolio recorded operating revenue of RMB29.1251 million and a net profit of RMB-2.7666 million. The Company conducted a preliminary impairment test on goodwill and engaged Beijing North Asia Asset Assessment Firm to conduct an assessment, and issued assessment reports (Bei Fang Ya Shi Zi Ping Zi (2017) No. 01-022, Bei Fang Ya Shi Zi Ping Zi (2017) No. 01-023 and Bei Fang Ya Shi Zi Ping Zi (2017) No. 01-024). The recoverable value of the asset groups is determined based on the principle of the present value of the estimated future operating net cash flow and the assessed asset market value minus disposal costs and relevant taxes and fees, whichever is higher. According to the results of the impairment test and the assessment, the Company made provision for goodwill impairment of RMB41.8 million. The calculation process of impairment is as follows:

Unit: RMB0'000

Name of asset group A	Carrying amount of asset groups B	Original value of goodwill attributable to the parent C	Holding ratio of minority shareholders D	Unrecognised book value of goodwill attributable to minority shareholders E=C/(1-D)*D	Total book value of assets and the amount of goodwill F=B+C+E	Recoverable amount of asset groups G	Accrued provision for asset impairment H=F-G	Amount of impairment attributable to the parent I=H*(1-D)	Book value of goodwill impairment made for previous years J	Amount of provision for asset impairment to be made for the year K=I-J	Amount of provision for goodwill impairment for the year L
Weihai Baolong asset group	7,386.92	10,007.81	1.25%	126.68	17,521.41	9,136.88	8,384.53	8,279.72	4,629.00	3,650.72	3,650.00
Molong asset group portfolio	5,545.98	2,789.53	25%	929.84	9,265.35	6,411.42	2,853.93	2,140.45	1,620.00	520.45	530.00
Maolong New Materials asset group	358.61	1,500.00	0%	–	1,858.62	666.05	1,192.57	1,192.57	1,200.00	-7.43	
Total	13,291.51	14,297.34	–	1,056.52	28,645.38	16,214.35	12,431.03	11,612.74	7,449.00	4,163.74	4,180.00

② Provision for goodwill impairment in 2017

In 2017, the overall macro-economy showed a steady and good development trend. The downstream demand of the steel industry recovered and the Company's industry environment has undergone major changes, resulting in a significant increase in the market demand and prices of its products. The capacity utilization rate and the profitability of the Company's goodwill-related asset groups increased and there was no sign of impairment. Weihai Baolong asset group recorded operating revenue of RMB315.5202 million and a net profit of RMB11.0724 million in 2017. Molong assets group, located at the center of Shangkou Town, in response to the unified planning of the government department and the improvement of the residents' living environment, the Company planned to relocate its plants and update some of its equipment. Under such impact, Molong assets group's results in 2017 were unsatisfactory. Molong asset group recorded operating revenue of RMB29.9424 million yuan and a net profit of –RMB0.8715 million in 2017. The Company expected that its results in the future improve significantly by combining the equipment update plan of the asset group and the changes in the industry environment. The Company conducted a preliminary impairment test on goodwill and engaged Beijing North Asia Asset Assessment Firm to conduct an assessment, and issued assessment reports (Bei Fang Ya Shi Zi Ping Zi (2018) No. 01-031-01, Bei Fang Ya Shi Zi Ping Zi (2018) No. 01-031-02 and Bei Fang Ya Shi Zi Ping Zi (2018) No. 01-031-03). The recoverable value of the asset groups is determined based on the principle of the present value of the estimated future operating net cash flow and the assessed asset market value minus disposal costs and relevant taxes and fees, whichever is higher. According to the results of the impairment test and the assessment, it was unnecessary to make provision for goodwill impairment. The calculation process of impairment is as follows:

Unit: RMB0'000

Name of asset group A	Carrying amount of asset groups B	Original value of goodwill attributable to the parent C	Holding ratio of minority shareholders D	Unrecognised book value of goodwill attributable to minority shareholders E=C/(1-D)*D	Total book value of assets and the amount of goodwill F=B+C+E	Recoverable amount of asset groups G	Accrued provision for asset impairment H=F-G	Amount of impairment attributable to the parent I=H*(1-D)	Book value of goodwill impairment made for previous years J	Amount of provision for asset impairment to be made for the year K=I-J	Amount of provision for goodwill impairment for the year L
Weihai Baolong asset group	7,437.67	10,007.81	1.25%	126.68	17,572.16	12,445.24	5,126.92	5,062.83	8,279.00	-3,216.17	–
Molong asset group portfolio	5,439.94	2,789.53	25%	929.84	9,159.31	6,975.69	2,183.62	1,637.72	2,150.00	-512.28	–
Maolong New Materials asset group	358.61	1,500.00	0%	–	1,858.61	858.90	999.71	999.71	1,200.00	-200.29	–
Total	13,236.22	14,297.34	–	1,056.52	28,590.08	20,279.83	8,310.25	7,700.26	11,629.00	-3,928.74	–

③ Provision for goodwill impairment in 2018

In 2018, China's economy progressed steadily and the macro economy operated steadily, resulting in a steady increase in the product market demand and prices of the Company. Despite current results of Weihai Baolong asset group were affected by is technological reform in equipment, portfolio of Weihai Baolong asset group and Molong asset group portfolio had a promising prospect of future development without signs of impairment. Weihai Baolong asset group recorded operating revenue of RMB339.8047 million and a net profit of RMB0.2236 million in 2018. Molong asset group recorded operating revenue of RMB51.8407 million and a net profit of RMB2.5997 million in 2018. Main assets in Maolong New Materials asset group were equity interest of Yalong Oil Machinery Co. Ltd, a joint stock company. The Company conducted a preliminary impairment test on goodwill, and engaged Wanlong (Shanghai) Assets Valuation Co. Ltd. to conduct an assessment, and issue assessment reports (Wan Long Ping Bao Zi (2019) No. 10039, Wan Long Ping Bao Zi (2019) No. 10040 and Wan Long Ping Bao Zi (2019) No. 10041). The recoverable value of the asset groups is calculated based on the income approach. According to the results of the impairment test and the assessment, the Company only made provision for goodwill impairment of RMB3.0 million on Maolong New Materials asset group. The calculation process of impairment is as follows:

Unit: RMB0'000

Name of asset group A	Carrying amount of asset groups B	Original value of goodwill attributable to the parent C	Holding ratio of minority shareholders D	Unrecognised book value of goodwill attributable to minority shareholders E=C/(1-D)*D	Total book value of assets and the amount of goodwill F=B+C+E	Recoverable amount of asset groups G	Accrued provision for asset impairment H=F-G	Amount of impairment attributable to the parent I=H*(1-D)	Book value of goodwill impairment made for previous years J	Amount of provision for asset impairment to be made for the year K=I-J	Amount of provision for goodwill impairment for the year L
Weihai Baolong asset group	9,105.21	10,007.81	1.25%	126.68	19,239.70	12,794.99	6,444.71	6,364.15	8,279.00	-1,914.85	–
Molong asset group portfolio	2,116.15	2,789.53	25%	929.84	5,835.52	3,902.06	1,933.46	1,450.10	2,150.00	-699.90	–
Maolong New Materials asset group		1,500.00	0%	–	1,500.00	–	1,500.00	1,500.00	1,200.00	300.00	300.00
Total	11,221.36	14297.34	–	1,056.52	26,575.22	16,697.05	9,878.17	9,314.25	11,629.00	-2,314.75	300.00

Remark: In 2018, due to plant relocation and disposal of assets of Molong Electro-Mechanical, the carrying value of the asset group decreased.

As analyzed above, the Company considers that the provision for impairment of goodwill from 2016 to 2018 and in the reporting period was sufficient and prudent.

Verification opinion from accountant:

We have performed relevant audit procedures and are of the view that the Company has provided for goodwill impairment in the year in a sufficient and prudent way and complies with the Accounting Standards for Business Enterprises.

For details, please refer to the Special Description of Inquiry Letter for the Annual Report 2019 of Shandong Molong Petroleum Machinery Company Limited issued by Shinewing Certified Public Accountants Ltd. (Special General Partner).

7. **At the end of the reporting period, the Company had current liabilities of RMB3,869 million, including short-term loans of RMB1,930 million, long-term loans due within one year of RMB483 million and accounts payable of RMB924 million. The current ratio was 0.64 and gearing ratio was 68.81%. In terms of monetary funds at the end of the period, receivables collection plan and the repayment plan of the above liabilities subsequent to the end of the period, please illustrate whether the Company has any liquidity risk and overdue debt, and whether the Company has sufficient risk warning in this respect. The annual audit accountant please verify and give clear opinion.**

Reply:

At the end of 2019, the Company has short-term borrowings of RMB1.93 billion and long-term borrowings due within one year of RMB483 million. The following table illustrates the creditors, debt amount, maturity date, repayment plan and repayment status of the above short-term liabilities:

Unit: RMB0'000

Borrowing type	Name of creditor	Borrowing amount	Maturity date	Repayment plan	Repayment status
Short-term borrowings	Minsheng Bank, Shouguang sub-branch	10000.00	2020/1/7	–	Repaid and renewed
	CCB, Shouguang sub-branch	3488.00	2020/1/29	–	Repaid and renewed
	CCB, Shouguang sub-branch	10000.00	2020/2/13	–	Repaid and renewed
	Huaxia Bank, Weifang sub-branch	4000.00	2020/3/5	–	Repaid and renewed
	ICBC, Shouguang sub-branch	4100.00	2020/3/18	–	Repaid and renewed

Borrowing type	Name of creditor	Borrowing amount	Maturity date	Repayment plan	Repayment status
	ABC, Shouguang sub-branch	2000.00	2020/3/20	–	Repaid and renewed
	ABC, Shouguang sub-branch	3000.00	2020/3/20	–	Repaid and renewed
	Bank of Beijing, Weifang branch	10000.00	2020/3/20	–	Repaid and renewed
	BOC, Shouguang sub-branch	5400.00	2020/4/1	–	Repaid and renewed
	BOC, Shouguang sub-branch	4820.00	2020/4/4	–	Repaid and renewed
	ABC, Shouguang sub-branch	8000.00	2020/4/7	–	Repaid and renewed
	CCB, Shouguang sub-branch	14500.00	2020/4/7	–	Repaid and renewed
	Bank of Beijing, Weifang branch	8560.00	2020/1/30	–	Repaid and renewed
	Weifang China CITIC Bank	4000.00	2020/3/20	–	Repaid and renewed
	EPEC	1123.00	–	Recovery of loans for repayment, renewable	Partially repaid and renewed
	ABC, Shouguang sub-branch	6000.00	2020/4/16	–	Repaid and renewed
	ABC, Shouguang sub-branch	7000.00	2020/4/23	–	Repaid and renewed
	ICBC, Shouguang sub-branch	4300.00	2020/4/29	–	Repaid and renewed
	ABC, Shouguang sub-branch	3000.00	2020/5/12	–	Repaid and renewed
	ICBC, Shouguang sub-branch	9800.00	2020/5/22	–	Repaid and renewed
	ABC, Shouguang sub-branch	8000.00	2020/5/22	–	Repaid and renewed
	BOC, Shouguang sub-branch	4760.00	2020/6/14	Repay with internal resources and renew upon maturity	–
	ICBC, Shouguang sub-branch	5900.00	2020/6/24	Drawdown repay	–

Borrowing type	Name of creditor	Borrowing amount	Maturity date	Repayment plan	Repayment status
	Bank of Beijing, Weifang branch	5000.00	2020/6/24	Repay with internal resources and renew upon maturity	–
	ABC, Shouguang sub-branch	6000.00	2020/7/23	Repay with internal resources and renew upon maturity	–
	China CITIC Bank, Shouguang sub-branch	2000.00	2020/8/24	Repay with internal resources and renew upon maturity	–
	ABC, Shouguang sub-branch	3600.00	2020/9/9	Repay with internal resources and renew upon maturity	–
	ICBC, Shouguang sub-branch	7700.00	2020/9/9	Drawdown repay	–
	China CITIC Bank, Shouguang sub-branch	6000.00	2020/9/18	Repay with internal resources and renew upon maturity	–
	ABC, Shouguang sub-branch	6400.00	2020/10/14	Repay with internal resources and renew upon maturity	–
	CCB, Shouguang sub-branch	1000.00	2020/10/21	Repay with internal resources and renew upon maturity	–
	CCB, Shouguang sub-branch	5000.00	2020/10/29	Repay with internal resources and renew upon maturity	–
	BOC, Shouguang sub-branch	4700.00	2020/11/7	Repay with internal resources and renew upon maturity	–
	CMB, Shouguang sub-branch	3800.00	2020/5/8	–	Repaid and renewed
	Sub-total	**192,951.00**			

Borrowing type	Name of creditor	Borrowing amount	Maturity date	Repayment plan	Repayment status
Long-term borrowings due within one year	COSCO Leasing	1523.59	2020/1/11	–	Matured and repaid
	COSCO Leasing	1445.44	2020/4/11	–	Matured and repaid
	Great Wall Asset Management	1125.00	2020/2/29	–	Matured and repaid
	COSCO Leasing	1373.81	2020/7/11	Repay with internal resources	–
	COSCO Leasing	1375.71	2020/10/11	Repay with internal resources	–
	Great Wall Asset Management	7471.33	2020/5/30	Repay with internal resources, continue to cooperate	–
	Great Wall Asset Management	1126.19	2020/10/8	Repay with internal resources, continue to cooperate	–
	Great Wall Asset Management	7822.62	2020/11/30	Repay with internal resources, continue to cooperate	–
	Shandong Guohui	25000.00	2020/12/7	Repay with internal resources, financing replacement	–
	Sub-total	**48,263.69**			
Total		**241,214.69**			

The Company's bank borrowings are mainly concentrated in the four state-owned banks, namely ABC, CCB, ICBC and BOC. Since 2017, led by ABC, the bank creditors held several bank creditor meetings, and the banks promised not to rescind or reduce loans, and continue to support the development of enterprises. As of the date replying this letter, all the matured bank loans of the Company abovementioned have been repaid on time and renewed, and there is no overdue debt or interest default.

At the end of 2019, the Company's monetary funds balance was RMB539.9421 million, which is sufficient to meet the needs of the Company's daily production, operation and management of capital turnover. At the end of 2019, the Company's accounts receivable amounted to RMB507.559 million, of which PetroChina, Sinopec, CNOOC and Yanchang Petroleum, all of which are large state-owned enterprises, accounted for 84.63% of the total accounts receivable. These customers have good credit status, with stable and guaranteed repayment. At the end of 2019, the amount of goods delivered of the Company's inventory was RMB128.5009 million, and the amount of finished products was RMB286.4876 million, with a total of RMB414.9885 million. Such assets have strong liquidity. The Company has no major investment plan in 2020, and the cash outflow from investment activities will significantly reduce as compared with the previous year.

At the end of the reporting period, gearing ratio of the Company was 68.81%, which is a relatively high level. Apart from the impacts of domestic and foreign economic situations, volatility in crude oil prices and industry demand, the higher gearing ratio was also related to the industry, business model and production pattern of the Company:

(1) The Company mainly engages in the research and development, production and sales of products required by the energy equipment industry. It is an asset-intensive industry, and the gearing ratio of enterprises in the industry is generally relatively high. Valin Steel, a listed company which was operating in the industry similar to the Company, had a gearing ratio of 60.78%. At the end of 2019, the gearing ratio of Daye Special Steel was 65.18%.

(2) The Company is one of the few domestic manufacturers with complete industrial chain of casings. The production process is long and includes Hot Rolling, Heat Treatment, Pipe Processing, and Packaging by Maolong New Materials, Shouguang Baolong and Shandong Molong and other branches. Each process requires the use of available working capital, which in turn leads to relatively higher rate of spending of the working capital of the Company.

(3) Products of the Company are for the four largest oil companies in China. The sales model is on credit terms and the time for delivery, acceptance, and settlement of products is relatively long. The capital locked in product delivery and accounts receivable of the Company is relatively large.

(4) The largest customer of the Company is Petro China Company Limited, of which more than 60% of accounts receivable is settled by commercial acceptance bill. Upon receipt of commercial acceptance bills, the Company mainly pledged them through Kunlun Bank to issue bank acceptance bills for payments of accounts payable, which increased the Company's gearing ratio at the end of the reporting period by approximately 1.3 percentage points compared with wire transfers and bank settlements.

In view of the Company's high debt, unreasonable debt structure and other issues, the Company has implemented the following measures in order to further improve its solvency and debt structure:

(1) Mr. Zhang En Rong, the controlling shareholder and beneficial controller of the Company, has signed an irrevocable letter of commitment for financial support on 30 March 2017, committed to providing working capital to the Company in a reasonable way such as pledging the shares of Shandong Molong held by him at no consideration. Such supporting commitment remains effective.

(2) The Company will continue to strengthen its cooperation with banks and further expand its financing channels. At present, China CITIC Bank has increased the credit line of RMB20 million to the Company, Minsheng Bank has increased the credit line of RMB100 million to the Company, Kunlun bank has increased the order financing line of RMB200 million to the Company, and EPEC has provided an additional commercial factoring line of RMB40 million to the Company, and none of the above additional lines has been used at present. Other banks are also planning to increase the credit line to the Company. China Great Wall Asset Management Company Limited, Shandong Branch has completed internal approval to commence comprehensive financial business of approximately RMB200 million with a term of three years for the Company. In addition, the Company is also actively seeking other financing channels, such as financial leasing, to increase the proportion of long-term loans and improve the Company's debt structure.

(3) The Company has stepped up the development of new products. New products such as bimetal corrosion-resistant pipes and ML125V casings will be respectively introduced to the market. The Company will continue to develop new products according to the specific needs of customers, so as to improve the market competitiveness of the Company's products.

(4) With the technical advantages of the forging technology transformation project of Shouguang Maolong New Materials Technology Development Company Limited, a wholly-owned subsidiary of the Company, we shall further expand the market share of high-end products and improve the Company's profitability.

(5) The Company will continue to increase its market development efforts to improve the market position of the Company and diversify its income streams.

Taking into account of the above measures, the Company has adequate capital to maintain normal production and operation with basically smooth financing channels, and has the ability to repay its liabilities upon maturity. Therefore, the Company has a relatively low liquidity risk.

Verification opinion from accountant:

We have performed relevant audit procedures and are of the view that the Company has the ability to repay liabilities upon maturity and we are not aware of any overdue liabilities.

For details, please refer to the Special Description of Inquiry Letter for the Annual Report 2019 of Shandong Molong Petroleum Machinery Company Limited issued by Shinewing Certified Public Accountants Ltd. (Special General Partner).

8. **At the end of the reporting period, the Company had other payables – accrued energy charges of RMB35.88 million, representing a year-on-year increase of 58%. Please illustrate the reasons and rationality of the year-on-year increase in the accrued energy charges, and, in terms of accrued energy charges carried forward subsequent to the end of the period, illustrate whether the accrued amount at the end of the reporting period was reasonable and sufficient. The annual audit accountant please verify and give clear opinion.**

Reply:

At the end of the reporting period, the main reasons for the increase of other payables – accrued energy charges of the Company as compared with the corresponding period last year are as follows:

1. The accrued electricity tariff increased by RMB4.356 million. As the power company issues an invoice on the 18th day of each month for the electricity tariff in arrears, the Company accrued the electricity tariff according to the electricity consumption during the period of 18-31 December 2019 and included in the production cost of the month. In December 2019, the electric-arc furnace production line of the subsidiary Shouguang Baolong Petroleum Equipment Company Limited was in normal operation, while the production line was shut down for inspection and maintenance in the same period of last year, resulting in an increase in the accrued electric tariff at the end of 2019 as compared with the same period of last year.

2. The accrued guaranteed freight increased by RMB10.7739 million. It is mainly due to subsidiary Shouguang Baolong Petroleum Equipment Company Limited's outsourcing manufacturers, namely Zhejiang Hongfeng, Yingkou Dongli, Qingdao Zhengwang and Hebei Huarui, failed to issue invoices in time at the end of 2019 for the guaranteed freight, while the Company has accrued and recorded the corresponding expenses as production cost in the period, resulting in an increase of the accrued guaranteed freight in the current period on a year-on-year basis.

As of the date replying this letter, an invoice of RMB29.4129 million has been issued for accrued energy charges of RMB35.88 million, and the Company has urged the supplier to issue invoices for the remaining balance as soon as possible.

Verification opinion from accountant:

We have performed relevant audit procedures and are of the view that the amounts of the Company's accrued charges are rational and the reasons for the changes is in line with the Company's actual circumstances.

For details, please refer to the Special Description of Inquiry Letter for the Annual Report 2019 of Shandong Molong Petroleum Machinery Company Limited issued by Shinewing Certified Public Accountants Ltd. (Special General Partner).

9. According to the annual report, during the reporting period, administrative expenses – amortisation of intangible assets, depreciation expenses and utilities were RMB11.64 million, RMB47.82 million and RMB22.03 million respectively, representing a decrease of 62%, an increase of 75% and an increase of 164% year-on-year respectively. Please illustrate the reasons and rationality of the changes in the above expenses. The annual audit accountant please verify and give clear opinion.

Reply:

At the end of the reporting period, "management expenses – amortization of intangible assets" decreased by 62% year-on-year, mainly due to the fact that the amortization amount of the self-developed intangible assets of the enterprise was included in "research and development expenses" for the period according to the Notice on Revising and Issuing the Format of Financial Statements of General Enterprises for the Year 2019 (Cai Kuai [2019] No. 6), while the same was included in "management expenses – amortization of intangible assets" category in the same period of last year.

At the end of the reporting period, the "management expenses – depreciation expenses" increased by 75% year-on-year, mainly due to the depreciation expenses of RMB15.26 million incurred by the wholly-owned subsidiary Shouguang Maolong New Materials Technology Development Company Limited during the period of shutdown for inspection and maintenance and equipment technical transformation in 2019, which was included in this category.

At the end of the reporting period, the "management expenses – utilities" increased by 164% year on year, mainly due to the utilities of RMB14.68 million incurred by the wholly-owned subsidiary Shouguang Maolong New Materials Technology Development Company Limited during the period of shutdown for inspection and maintenance and equipment technical transformation in 2019, which was included in this item.

Verification opinion from accountant:

We have performed relevant audit procedures and are of the view that the changes in the above management expenses of the Company is in line with the Company's actual circumstances and the reasons for the changes are rational.

For details, please refer to the Special Description of Inquiry Letter for the Annual Report 2019 of Shandong Molong Petroleum Machinery Company Limited issued by Shinewing Certified Public Accountants Ltd. (Special General Partner).

10. At the end of the reporting period, net loans and advances of the Company was RMB17.05 million. As at 31 December 2019, the Company had overdue loans of RMB47.93 million in aggregate, which were overdue for over 360 days, and a loss provision for loans of RMB30.88 million has been made. Please provide details of the loans and advances, including whether they are related to the core business of the Company, the reasons and rationality for the overdue period of over 360 days, and whether the loss provision for loans was sufficient and prudent. The annual audit accountant please verify and give clear opinion.

Reply:

(1) Particulars of loans and advances of the Company

Loans and advances of the Company during the reporting period were the loans lent by the subsidiary Shouguang Maolong Micro-Credit Company Limited earlier. The business scope of the company is "to handle various loans in Shouguang City; to carry out consulting business regarding small enterprise development, management and finance". Since the second half of 2017, the company ceased to carry out external business. In September 2019, the company changed its name to Shouguang Baolong Management and Consultation Company Limited and changed its corporate type and business scope.

(2) Description of accounting policies on provision for loan losses

The Company has established an expected credit loss model. The Company, based on whether there have been significant changes in the credit risk of financial instruments and whether credit impairment has occurred, and taking into account the impact of forward-looking macroeconomic factors, made provision for expected credit loss of financial instruments in the next 12 months or over the remaining life. Expected credit loss = loan principal × expected loss given default.

In accordance with relevant regulations in the "Notice on Strengthening Loan Classification Management for Micro-Credit Company to Improve Risk Provision (Lujinbanfa [2013] No.11), the Company analyzes the recovery of loans case by case, and follows cautious and objective principles to classify loans into five categories: normal, special mention, sub-standard, doubtful, and loss. Among them: normal: the borrower can perform the contract without sufficient reasons to suspect that the principal and interest of the loan cannot be repaid on time and in full; special mention: the borrower is currently able to repay the principal and interest of the loan, but there are some factors that may have an adverse effect on the repayment; sub-standard: the borrower's repayment ability has obvious problems, and the principal and interest of the loan cannot be repaid based on his/her normal operating income. Even with execution of guarantee, it may incur certain losses; doubtful: the borrower cannot repay the principal and interest of the loan in full, and even with the execution of guarantee, it will definitely incur a large loss; loss: after taking all possible measures or all necessary legal procedures, the principal and interest still cannot be recovered, or only a small part can be recovered. The five risk classification portfolios have common credit risk characteristics, and provision for loan losses is calculated in accordance with corresponding credit risk characteristics × corresponding expected default loss given default.

① Normal loans

According to the requirements of <Lujinbanfa [2013] No.11>, the general provision for losses of normal loan is subject to not less than 1% of the loan balance. The Company adjusts the general provision ratio to 6% based on historical experience, factors of forward-looking adjustments and the time value of currency.

② Special mention loans

According to the requirements of <Lujinbanfa [2013] No.11>, special mention loans are subject to 1% provision for loan losses and 2% special provision for loan losses. The Company adjusts the general provision ratio to 6% and special provision ratio to 5% based on historical experience, factors of forward-looking adjustments and the time value of currency.

③ Sub-standard loans

According to the requirements of <Lujinbanfa [2013] No.11>, sub-standard loans are subject to 1% provision for loan losses and 25% special provision for loan losses. The Company adjusts the general provision ratio to 6% and special provision ratio to 28% based on historical experience, factors of forward-looking adjustments and the time value of currency.

④ Doubtful loans

According to the requirements of <Lujinbanfa [2013] No.11>, doubtful loans are subject to 1% provision for loan losses and 50% special provision for loan losses. The Company adjusts the general provision ratio to 6% and special provision ratio to 55% based on historical experience, factors of forward-looking adjustments and the time value of currency.

⑤ Loss loans

According to the requirements of <Lujinbanfa [2013] No.11>, loss loans are subject to 100% special provision for loan losses.

(3) Credit impairment losses for loans and advances of the Company

According to the above policies of provision for loan credit loss and combining the particulars of the collaterals and guarantee of the borrower, losses of provision for credit impairment are as follows:

Borrower	Balance	Five categories	Ratio of provision made	Amount of provision made	Overdue time (Months)	Collaterals and guarantee
Unit 1	6,000,000.00	Special mention	11.00%	660,000.00	48	The Company or subsidiary's accounts payable is pledged as a collateral guarantee, and it has been processed as of date of replying this letter after the Company won the litigation in the second instance
Unit 2	1,650,000.00	Special mention	11.00%	181,500.00	32	The Company or subsidiary's accounts payable is pledged as a collateral guarantee and the risk is lower because amount can be transferred by three parties upon completion of relevant procedures
Unit 3	2,403,579.00	Sub-standard	34.00%	817,216.86	40	The litigation has been won and the execution period has due, with collateralized real estate and continuous repayments
Unit 4	1,121,000.00	Doubtful	61.00%	683,810.00	73	The litigation has been won and the execution period has due, with properties and lands seized having monetization capabilities
Unit 5	6,505,822.15	Doubtful	61.00%	3,968,551.51	73	The litigation has been won, and the execution period has due, with properties and lands seized having monetization capabilities

Borrower	Balance	Five categories	Ratio of provision made	Amount of provision made	Overdue time (Months)	Collaterals and guarantee
Unit 6	4,700,000.00	Doubtful	61.00%	2,867,000.00	73	Litigation has been won and the execution period has due, with properties and lands seized having monetization capabilities
Unit 7	2,000,000.00	Doubtful	61.00%	1,220,000.00	20	Collateralized real estate with monetization capabilities
Unit 8	800,000.00	Doubtful	61.00%	488,000.00	43	Collateralized real estate with monetization capabilities
Unit 9	7,057,931.25	Doubtful	61.00%	4,305,338.06	55	Litigation filed, execution period entered, collateralized real estate with monetization capabilities
Unit 10	25,000.00	Loss	100.00%	25,000.00	69	Insolvency of the borrower and the guarantor
Unit 11	1,000,000.00	Loss	100.00%	1,000,000.00	74	Insolvency of the borrower and the guarantor
Unit 12	3,000,000.00	Loss	100.00%	3,000,000.00	68	Insolvency of the borrower and the guarantor
Unit 13	1,034,500.00	Loss	100.00%	1,034,500.00	67	Insolvency of the borrower and the guarantor
Unit 14	1,691,637.00	Loss	100.00%	1,691,637.00	53	Insolvency of the borrower and the guarantor
Unit 15	600,000.00	Loss	100.00%	600,000.00	48	Insolvency of the borrower and the guarantor
Unit 16	2,335,684.68	Loss	100.00%	2,335,684.68	60	Insolvency of the borrower and the guarantor
Unit 17	3,000,000.00	Loss	100.00%	3,000,000.00	46	Insolvency of the borrower and the guarantor
Unit 18	3,000,000.00	Loss	100.00%	3,000,000.00	45	Insolvency of the borrower and the guarantor
Total	47,925,154.08			30,878,238.11		

As analysed above, it is sufficient and prudent for the Company to make provision for loan loss with reference to the relevant provisions of the financial regulatory authorities after taking into account of the financial situation of the debtors and guarantors, the possibility of realization of the collaterals and the realizable amount.

Verification opinion from accountant:

We have performed relevant audit procedures and are of the view that the provision for loss of loans by the Company complies with relevant requirements of the Accounting Standards for Business Enterprises.

For details, please refer to the Special Description of Inquiry Letter for the Annual Report 2019 of Shandong Molong Petroleum Machinery Company Limited issued by Shinewing Certified Public Accountants Ltd. (Special General Partner).

11. **During the reporting period, research and development expenses – amortization of non-patented technology for the previous year of the Company was RMB7.48 million. Please provide details of the above expenses, and the rationality for the non-patented technology for last year was amortized in the current period. The annual audit accountant please verify and give clear opinion.**

Reply:

During the reporting period, the Company's "research and development expenses – amortization of non-patented technology for the previous year" presented was RMB7.48 million, which is the amount to be amortized in the current year of non-patented technology independently researched and developed by the Company in the previous year and the reporting period and recorded in intangible assets. According to relevant requirements of the Accounting Standards for Business Enterprises No. 6 – Intangible Assets, the Company adopts straight-line method to amortize self-developed non-patented technologies within their estimated useful life. The amortization of non-patented technologies during the reporting period is as follows:

Unit: RMB

Name of non-patented technology	Date of credit	Original value	Months of amortization	Amount of monthly amortization	Amortization in 2019	
					Months	Amortized amount
Non-patented technology 1	August 2014	5,423,681.59	60	90,394.69	7	632,762.85
Non-patented technology 2	September 2014	6,551,255.15	60	109,187.59	8	873,500.68
Non-patented technology 3	November 2015	1,113,496.38	60	18,558.27	12	222,699.28
Non-patented technology 4	October 2015	4,910,644.52	60	81,844.08	12	982,128.88
Non-patented technology 5	September 2017	4,681,188.03	60	78,019.80	12	936,237.61
Non-patented technology 6	December 2017	4,496,393.44	60	74,939.89	12	899,278.69
Non-patented technology 7	June 2018	4,014,109.52	60	66,901.83	12	802,821.90
Non-patented technology 8	June 2018	2,998,536.14	60	49,975.60	12	599,707.23
Non-patented technology 9	November 2018	3,943,426.86	60	66,222.59	12	794,671.08
Non-patented technology 10	June 2019	5,570,485.70	60	92,841.43	7	649,890.00
Non-patented technology 11	December 2019	5,293,962.59	60	88,232.71	1	88,232.71
Total						7,481,930.91

During the reporting period, the above non-patented technologies were within their useful life and were able to bring inflow of economic benefits to the Company. According to the relevant provisions of the Accounting Standards for Business Enterprises, the Company believes that it is reasonable to adopt straight-line method for amortization during the reporting period.

Verification opinion from accountant:

We have performed relevant audit procedures and are of the view that the accounting for research and development expenses – amortization of non-patented technology for the previous year of the Company complies with the requirements of the Accounting Standards for Business Enterprises.

For details, please refer to the Special Description of Inquiry Letter for the Annual Report 2019 of Shandong Molong Petroleum Machinery Company Limited issued by Shinewing Certified Public Accountants Ltd. (Special General Partner).

12. During the reporting period, loss on bad debts of bill receivables was RMB2.60 million. Please illustrate the reasons and rationality of the loss on bad debts of bill receivables, and, in terms of the collection of bill receivables subsequent to the end of the period, illustrate whether provision for bad debts of bill receivables is sufficient and prudent. The annual audit accountant please verify and give clear opinion.

Reply:

The business model of the Company's bills receivable is commercial acceptance bill for the purpose of collecting contractual cashflow. The provision for impairment of the bills receivable at the end of the year is made according to the expected credit impairment method of the accounts receivable.

As of the end of the reporting period, the balance of bills receivable of the Company was RMB260.2376 million, all of which was issued by PetroChina Company Limited through Kunlun Bank, with an ageing within one year. The Company has made bad debt provision of RMB2.6023 million at the expected credit loss rate of 1%. As of the date replying this letter, all matured bills receivable of the Company have been collected.

Description of provision not made for impairment of bill receivables in 2018: In 2017, the Ministry of Finance successively revised and issued "Accounting Standards for Business Enterprises No. 22-Recognition and Measurement of Financial Instruments", "Accounting Standards for Enterprises No. 23-Transfer of Financial Assets", "Accounting Standards for Enterprises No. 24-Hedge Accounting", "Accounting Standards for Business Enterprises No. 37-Presentation and Reporting of Financial Instrument" ("new financial instrument standards"). From 1 January 2018, the Company, as an A + H listed company, implemented the above new financial instrument standards and made provisions for expected credit loss for impairment of financial assets such as bill receivables in accordance with relevant requirements. At the end of 2018, the drawers of the Company's commercial acceptance receivables were PetroChina and Yanchang Petroleum. PetroChina is a central enterprise, and Yanchang Petroleum is a large provincial state-owned enterprise with a good credit status. Relevant commercial acceptance bills received by the Company in recent years have been paid on schedule, and there has been no incident that the drawer refused or failed to pay on time. Based on the judgment of the drawer's credit status and historical performance, the Company was of the view that the default probability of commercial acceptance bills not due at the end of 2018 was 0, resulting in the expected credit loss rate determined as 0 and no provision for impairment was made.

From January to March in 2019, most enterprises delayed their resumption of work and production as affected by downward fluctuations of international crude oil prices and the outbreak of coronavirus epidemic. In consideration of the macroeconomic environment, changes in the industry, and the impact of the epidemic, the Company made provisions for impairment of commercial acceptance bills in 2019, in accordance with the method of accruing bad debt provision for accounts receivable for prudent considerations.

As analysed above, taking into account of the historical bill collection record and situation subsequent to the end of the period, bills receivable upon maturity can all be collected. As such, the Company's provision for bad debts of bills receivable in 2019 is sufficient and prudent.

Verification opinion from accountant:

We have performed relevant audit procedures and are of the view that bad debt provision for commercial acceptance bills receivable by the Company complies with the requirements of the Accounting Standards for Business Enterprises.

For details, please refer to the Special Description of Inquiry Letter for the Annual Report 2019 of Shandong Molong Petroleum Machinery Company Limited issued by Shinewing Certified Public Accountants Ltd. (Special General Partner).

13. **Illustrate the collection of accounts receivable at the end of the reporting period and, in terms of collection, illustrate whether provision for bad debts of accounts receivable is sufficient. The annual audit accountant please verify and give clear opinion.**

Reply:

For accounts receivable, the Company adopts expected credit loss approach to provide allowances for bad debts. For accounts receivable which has significant different credit risk, expected credit loss is determined on an individual basis. Apart from determining expected credit loss of accounts receivable on individual basis, the Company also adopts expected credit loss model based on collective characteristics, and calculates the expected credit losses of accounts receivable through receivable default risk exposure and expected credit loss rate. Expected credit loss rate is determined based on the probability of default and the loss given default.

As of the end of the reporting period, the Company's accounts receivable amounted to RMB507.559 million, of which RMB429.5484 million was due from the four major petroleum companies PetroChina, Sinopec, CNOOC and Yanchang Petroleum, accounting for 84.63% of the total accounts receivable. All of the above customers are large state-owned enterprises with good credit status, and the risk of bad debts of accounts receivable is very low. In addition to petroleum machinery products, the Company also produces certain fluid and structural pipes and tube blanks, and its main customers are large steel traders. These customers are mainly settled by advance payment or cash on delivery to avoid the risk of bad debts to the greatest extent.

PetroChina, Sinopec, CNOOC and Yanchang oil usually repay within three months after the invoice is issued by the Company. According to the Company's policy of provision for credit impairment loss of accounts receivable, and based on the principle of prudence, accounts receivable with an aging within one year are provided for credit impairment loss on default loss rate of 1%. As of the date replying this letter, the Company has received a repayment subsequent to the end of the period of approximately RMB283 million, of which the repayment from four largest oil companies amounted to approximately RMB242 million. The ratio of repayment subsequent to the end of the period was approximately 56.40% while that of the same period of last year was 73%. The main reason for the decrease in ratio of repayment subsequent to the end of the period: The repayments from the four largest oil companies are mainly concentrated on the period subsequent to 25th of each month. In 2020, as affected by Lunar Chinese New Year holidays and the novel coronavirus epidemic, oilfield customers delayed their resumption of work, resulting in relatively fewer repayments for the first two months. Starting from March, the repayments from the four largest oil companies have been returning to normal. Taking account of the influence of the above matters, the repayment subsequent to the end of the period is normal and reasonable. In view of the collection subsequent to the end of the period and the composition of customers, the provision for bad debts of accounts receivable of the Company at the end of the reporting period is sufficient.

Verification opinion from accountant:

We have performed relevant audit procedures and are of the view that bad debt provision for the accounts receivable of the Company complies with relevant requirements of the Accounting Standards for Business Enterprises.

For details, please refer to the Special Description of Inquiry Letter for the Annual Report 2019 of Shandong Molong Petroleum Machinery Company Limited issued by Shinewing Certified Public Accountants Ltd. (Special General Partner).

14. **The Company has not paid any cash dividend for three years in a row. Could the Company please advise the reasons based on business development, and conduct self-examination as to whether it has complied with the No. 3 Guideline for the Supervision of Listed Companies – Cash Dividends of Listed Companies and the articles of association of the Company. Please advise the key work ideas about increasing investors' return.**

Reply:

In the recent three years (2017, 2018 and 2019), the Company achieved a net profit attributable to shareholders of the listed company of RMB38 million, RMB92 million and RMB-196 million respectively. Given the loss for 2016 has widen, despite the Company delivered better business results in 2017 and 2018, it still encountered difficulties such as great pressure from short-term debt repayment, high finance costs and relatively high gearing ratio. Under the Company's profit distribution principle of "emphasizing the reasonable return on investment of investors and taking into account the sustainable development of the Company while maintaining the continuity and stability of the profit distribution policy", and based on the Company's sustainable development and safeguarding long-term interests of shareholders, the fifth and sixth session of the board of directors of the Company considered at its eighth and second meeting respectively and decided not to pay any dividends, not to distribute any bonus shares, and not to increase any capital by transferring reserve funds, for 2017 and 2018 respectively, and such decisions were considered and passed at the 2017 and 2018 annual general meetings respectively. The retained undistributed profits of the Company are mainly used to supplement the liquidity required for daily operations to ensure steady development of the Company, and ultimately maximise the interests of shareholders. In 2019, the Company had a net profit attributable to shareholders of the listed company of RMB-196 million, which did not satisfy the conditions for payment of cash dividend. In order to ensure the Company's normal production and operation and future development, the Company intends not to pay any dividends, not to distribute any bonus shares, and not to increase any capital by transferring reserve funds for 2019. Such profit distribution proposal is subject to be considered and passed at the 2019 annual general meeting of the Company.

The Company has conducted self-examination and confirms that the formulation and review procedures of its annual profit distribution plan are in compliance with relevant provisions and requirements of the No. 3 Guideline for the Supervision of Listed Companies – Cash Dividends of Listed Companies and the Articles of Association. The board of directors has seriously studied and discussed the timing, conditions, decision-making procedures and other requirements of paying cash dividends, and also adequately considered and listened to the opinions of independent directors. The board of supervisors of the Company has also considered the annual profit distribution plan of the Company for the past three years and has formulated their opinion.

The board of directors and management of the Company have established a firm idea of rewarding shareholders, and have formulated a scientific, continuous and stable dividend policy to actively reward the investors, and guide investors to establish long-term investment and rational investment concepts. It is stipulated in the Articles of Association that the Company shall follow the profit distribution principle of "emphasizing the reasonable return on investment of investors and taking into account the sustainable development of the Company while maintaining the continuity and stability of profit distribution policy". The Company is also encouraged to take initiative in communicating and exchanging with shareholders (particularly the minority shareholders) through various channels, fully listening to their opinions and requests, and promptly addressing their concerns.

As the Company's business is making progress with an increasingly higher profitability, subject to relevant national laws and regulations and the Articles of Association, after comprehensively analyzing the Company's actual business development, shareholders' requirements and willingness, social capital costs, external financing environment and other factors by focusing on the long-term and sustainable development of the Company, and having adequate consideration of the Company's existing and future profit scale, cashflows, development status, capital requirements of project investment, bank credits and debt financing environment, the Company will establish a sustainable, stable and scientific return planning mechanism for investors, implement a proactive profit distribution policy, emphasize the reasonable return on investment of investors, actively implement profit distribution system prioritizing cash dividend, in order to share the Company's growth and development results with shareholders.

15. The Company's 2019 annual report does not provide an explanation for data with changes of more than 30%, e.g. non-recurring profit and loss items on page 7 – profit or loss arising from contingencies unrelated to the normal operation of the Company; there are calculation errors in some data contained in the 2019 annual report, e.g. the composition of operating cost on page 18, of which the year-on-year increase/decrease was miscalculated. Please make corrections to the above errors, and check whether there are other situations that require corrections in the 2019 annual report.

Reply:

It is verified that the Company's 2019 annual report does not provide an explanation for data with changes of more than 30% presented in "Extraordinary Gains or Losses Items and Amounts" in "II. Company Profile and Major Financial Indicators" and "XVIII. ADDITIONAL INFORMATION 1. NON-RECURRING PROFIT (LOSS) FOR THE PERIOD" in "XII FINANCIAL REPORT", for which additional disclosure is required; there are calculation errors in the year-on-year increase/decrease of the composition of operating cost contained in the 2019 annual report, for which revision is required. For detailed additional and revised information, please refer to the "2019 Annual Report" (Updated) and "Announcement on supplement and revision of 2019 annual report" published by the Company on the designated media for information disclosure on the date replying this letter.

Apart from the above supplement and revision, all other contents of the 2019 annual report remain unchanged. This supplement and revision have no impact on the Company's financial position and operating results in 2019. The Company would like to apologize for the inconvenience caused to investors by this supplement and revision. In the future, the Company will improve the audit of regular report data and strive to improve the quality of information disclosure.

Hereby announce the above.

By order of the Board
Shandong Molong Petroleum Machinery Company Limited*
Liu Yun Long
Chairman

Shandong, the PRC, 24 May 2020

As at the date of this announcement, the Board comprises the executive Directors, namely Mr. Liu Yun Long, Mr. Liu Min, Mr. Zhang Yu Zhi and Mr. Li Zhi Xin; the non-executive Directors, namely Mr. Yao You Ling and Mr. Wang Quan Hong; and the independent non-executive Directors, namely Mr. Tang Qing Bin, Mr. Song Zhi Wang and Mr. Cai Zhong Jie.

* *For identification purpose only*