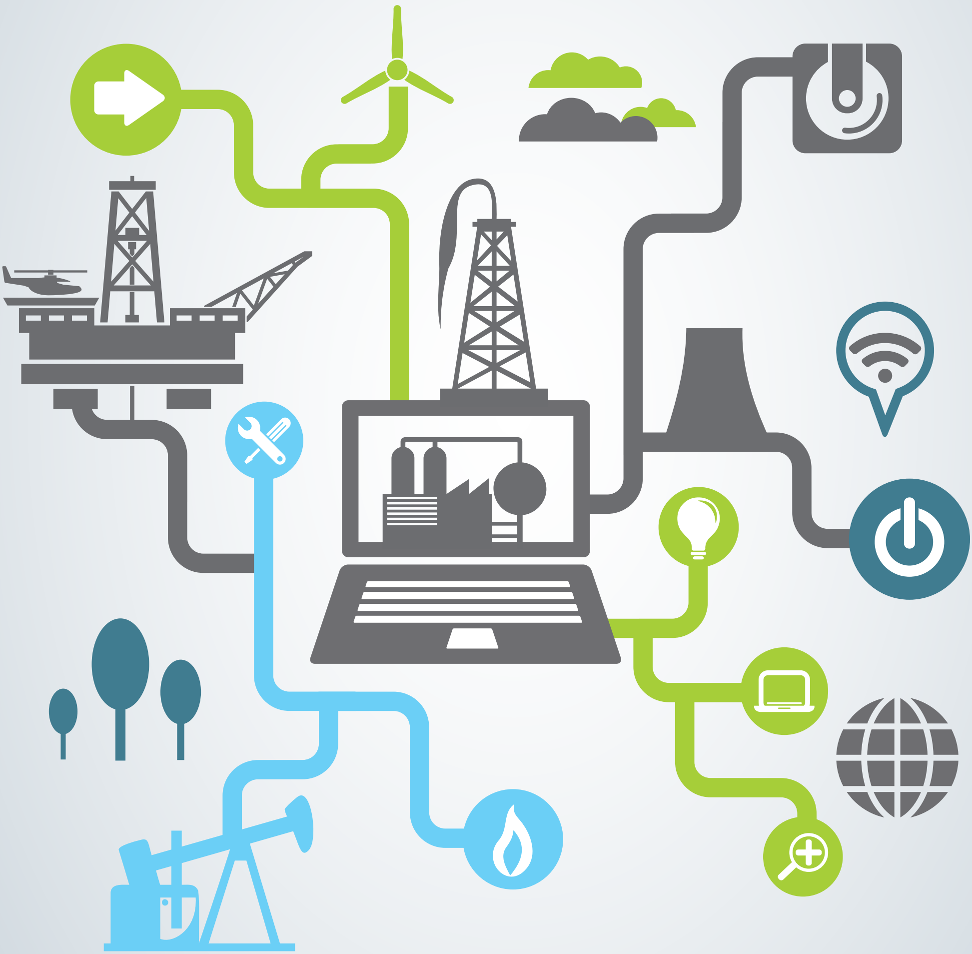
SSP 南海石油

# South Sea Petroleum Holdings Limited

Stock Code : 76



# INTERIM REPORT 2011

# Contents

The Board of Directors ("the Board") of South Sea Petroleum Holdings Limited ("the Company") is pleased to announce the unaudited condensed consolidated balance sheet as at 30 June 2011 of the Company and its subsidiaries ("the Group"), the unaudited condensed consolidated income statement, the unaudited condensed consolidated cash flow statement and the unaudited consolidated statement of changes in equity for the six months ended 30 June 2011 as follows:

## CONDENSED CONSOLIDATED INCOME STATEMENT

| | | Six months ended | |
|---|---|---|---|
| | | **30 June 2011** | 30 June 2010 |
| | | **Unaudited** | Unaudited |
| | *Notes* | ***US$'000*** | *US$'000* |
| **TURNOVER** | *3* | **32,152** | 22,892 |
| Cost of sales | | **(18,634)** | (16,166) |
| | | **13,518** | 6,726 |
| Other income | | **930** | 2,320 |
| Net gain (loss) in fair value of financial assets held for trading | | **44,648** | (5,010) |
| General and administrative expenses | | **(12,346)** | (10,080) |
| Drilling and operating expenses | | **(5,835)** | (4,177) |
| Other taxes | | **(248)** | (232) |
| **PROFIT (LOSS) FROM OPERATING ACTIVITIES** | *4* | **40,667** | (10,453) |
| Finance costs | | **(353)** | (510) |
| **PROFIT (LOSS) BEFORE TAX** | | **40,314** | (10,963) |
| Income tax | *5* | **(225)** | – |
| **PROFIT (LOSS) FOR THE PERIOD** | | **40,089** | (10,963) |
| Attributable to: | | | |
| Equity shareholders of the Company | | **40,040** | (10,910) |
| Non-controlling interests | | **49** | (53) |
| | | **40,089** | (10,963) |
| **EARNINGS (LOSS) PER SHARE (US Cents)** | *6* | | |
| **– Basic** | | **14.72** | (4.67) |
| **– Diluted** | | **14.69** | N/A |

## CONDENSED CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

| | Six months ended | |
|---|---|---|
| | **30 June 2011** | 30 June 2010 |
| | **Unaudited** | Unaudited |
| | ***US$'000*** | *US$'000* |
| **PROFIT (LOSS) FOR THE PERIOD** | **40,089** | (10,963) |
| **OTHER COMPREHENSIVE INCOME** | | |
| Exchange differences | **597** | (989) |
| Revaluation of land and buildings | **317** | – |
| **TOTAL COMPREHENSIVE INCOME FOR THE PERIOD** | **41,003** | (11,952) |
| Attributable to: | | |
| Equity shareholders of the Company | **40,871** | (11,862) |
| Non-controlling interests | **132** | (90) |
| | **41,003** | (11,952) |

## CONDENSED CONSOLIDATED BALANCE SHEET

| | Notes | 30 June 2011 Unaudited US$'000 | 31 December 2010 Audited US$'000 |
|---|---|---|---|
| **NON-CURRENT ASSETS** | | | |
| Fixed assets | 7 | **23,241** | 22,375 |
| Available-for-sale investment | | **771** | 771 |
| Deferred tax assets | | **379** | 368 |
| | | **24,391** | 23,514 |
| **CURRENT ASSETS** | | | |
| Cash and bank balances | | **22,013** | 22,682 |
| Financial assets at fair value held for trading | 8 | **60,387** | 16,798 |
| Trade and notes receivables | 9 | **14,215** | 8,550 |
| Inventories | | **11,019** | 10,747 |
| Prepayments, deposits and other receivables | | **77,042** | 56,360 |
| | | **184,676** | 115,137 |
| **CURRENT LIABILITIES** | | | |
| Trade payables | 10 | **5,726** | 5,035 |
| Other payables and accrued expenses | | **5,593** | 4,502 |
| Bank overdraft | | **2,891** | 1,091 |
| Bank loan on discounted debtors | | **1,382** | 104 |
| Finance lease – current portion | | **263** | 272 |
| Taxation | | **423** | 472 |
| | | **16,278** | 11,476 |

| | Notes | 30 June 2011 Unaudited US$'000 | 31 December 2010 Audited US$'000 |
|---|---|---|---|
| **NET CURRENT ASSETS** | | **168,398** | 103,661 |
| **TOTAL ASSETS LESS CURRENT LIABILITIES** | | **192,789** | 127,175 |
| **NON-CURRENT LIABILITIES** | | | |
| Finance leases | | **210** | 280 |
| Provision | | **2,724** | 1,909 |
| Convertible debentures | *11* | **3,368** | 3,650 |
| | | **6,302** | 5,839 |
| **NET ASSETS** | | **186,487** | 121,336 |
| **CAPITAL AND RESERVES** | | | |
| Share capital | *13* | **157,667** | 131,667 |
| Revaluation reserve | | **4,043** | 3,710 |
| Special capital reserve | | **12,037** | 12,037 |
| Share premium | | **197,560** | 198,851 |
| Convertible debenture equity reserve | | **917** | 1,478 |
| Translation reserve | | **6,397** | 5,899 |
| Accumulated losses | | **(195,420)** | (235,460) |
| Total equity attributable to equity shareholders of the Company | | **183,201** | 118,182 |
| Non-controlling interests | | **3,286** | 3,154 |
| | | **186,487** | 121,336 |

## CONDENSED CONSOLIDATED STATEMENT OF CASH FLOW

| | Six months ended | |
|---|---:|---:|
| | **30 June 2011** | 30 June 2010 |
| | **Unaudited** | Unaudited |
| | ***US$'000*** | *US$'000* |
| **NET CASH (USED IN) FROM OPERATING ACTIVITIES** | **(25,910)** | 865 |
| **NET CASH USED IN INVESTING ACTIVITIES** | **(1,787)** | (5,023) |
| **CASH FLOW FROM FINANCING ACTIVITIES** | **24,898** | 9,091 |
| **(DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS** | **(2,799)** | 4,933 |
| Cash and cash equivalents at 1 January | **21,591** | 19,814 |
| Effect of foreign exchange rates | **330** | (142) |
| **CASH AND CASH EQUIVALENTS AT 30 June** | **19,122** | 24,605 |
| **ANALYSIS OF THE BALANCES OF CASH AND CASH EQUIVALENTS** | | |
| Cash and bank balances | **22,013** | 26,227 |
| Bank overdraft | **(2,891)** | (1,622) |
| | **19,122** | 24,605 |

# CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN EQUITY (UNAUDITED)

*For the Six Months Ended 30 June 2011*

*(Expressed in US$'000)*

| | Attributable to equity holders of the Company | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | **Share capital** | **Share premium** | **Convertible debenture equity reserve** | **Special capital reserve** | **Translation reserve** | **Revaluation reserve** | **Accumulated losses** | **Total** | **Non-controlling interests** | **Total equity** |
| At 1.1.2011 | **131,667** | **198,851** | **1,478** | **12,037** | **5,899** | **3,710** | **(235,460)** | **118,182** | **3,154** | **121,336** |
| Total comprehensive income for the period | **–** | **–** | **–** | **–** | **498** | **333** | **40,040** | **40,871** | **132** | **41,003** |
| Issue of shares upon conversion of convertible debentures | **26,000** | **(1,291)** | **–** | **–** | **–** | **–** | **–** | **24,709** | **–** | **24,709** |
| Convertible debenture – equity component | **–** | **–** | **(561)** | **–** | **–** | **–** | **–** | **(561)** | **–** | **(561)** |
| At 30.6.2011 | **157,667** | **197,560** | **917** | **12,037** | **6,397** | **4,043** | **(195,420)** | **183,201** | **3,286** | **186,487** |

| | Attributable to equity holders of the Company | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | Share capital | Share premium | Convertible debenture equity reserve | Special capital reserve | Translation reserve | Revaluation reserve | Accumulated losses | Total | Non-controlling interests | Total equity |
| At 1.1.2010 | 109,722 | 199,947 | 2,253 | 12,037 | 5,918 | 3,843 | (216,777) | 116,943 | 2,823 | 119,766 |
| Total comprehensive income for the period | – | – | – | – | (663) | (289) | (10,910) | (11,862) | (90) | (11,952) |
| Issue of shares upon conversion of convertible debentures | 21,804 | (1,096) | (2,253) | – | – | – | – | 18,455 | – | 18,455 |
| At 30.6.2010 | 131,526 | 198,851 | – | 12,037 | 5,255 | 3,554 | (227,687) | 123,536 | 2,733 | 126,269 |

# NOTES TO THE FINANCIAL STATEMENTS

## 1. Basis of preparation and significant accounting policies

These unaudited consolidated interim financial statements of the Group ("Interim Accounts") have been prepared in accordance with Hong Kong Accounting Standard 34, "Interim Financial Reporting" issued by the Hong Kong Institute of Certified Public Accountants ("HKICPA"), and Appendix 16 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited.

These Interim Accounts should be read in conjunction with the annual financial statements for the year ended 31 December 2010, which have been prepared in accordance with Hong Kong Financial Reporting Standards ("HKFRS").

Except as described in note 2 below, the accounting policies applied are consistent with those of the annual financial statements for the year ended 31 December 2010, as described in those annual financial statements.

## 2. Adoption of new or amended HKFRSs

In the current period, the Group has applied for the first time the following new and revised HKFRSs issued by the HKICPA, which are relevant to and effective for the Group's financial statements for the annual financial period beginning on 1 January 2011.

| | |
|---|---|
| HKAS 24 (Revised) | Related Party Disclosures |
| HKAS 34 (Amendment) | Interim Financial Reporting |
| HKFRSs (Amendments) | Third improvements to HKFRSs |

The effect of the adoption of the above amendments to standards beginning 1 January 2011 is not material to the Group's results of operations or financial position and only results in additional disclosures.

## 3. Turnover and segment information

Turnover represents oil revenue from the sale of crude oil, assembly of electronic components for the contract electronics manufacturer and sales of mineral products.

An analysis of the Group's turnover and results for the period by business segments is as follows:

**For the six months ended 30 June 2011**
*(Expressed in US$'000)*

| | **Oil** | **Sale of minerals** | **Contract electronic manufacturing** | **Trading securities** | **Others** | **Total** |
|---|---|---|---|---|---|---|
| Revenue from external customers | **7,883** | **9,265** | **14,950** | **–** | **54** | **32,152** |
| Segment results | **(1,330)** | **(91)** | **545** | **44,730** | | **43,854** |
| Unallocated income and expenses | | | | | | **(3,187)** |
| Profit from operating activities | | | | | | **40,667** |
| Finance costs | | | **(22)** | | **(331)** | **(353)** |
| Taxation | | **(225)** | | | | **(225)** |
| Profit for the period | | | | | | **40,089** |

For the six months ended 30 June 2010

| | Oil | Sale of minerals | Contract electronic manufacturing | Trading securities | Others | Total |
|---|---|---|---|---|---|---|
| Revenue from external customers | 4,930 | 5,710 | 12,213 | – | 39 | 22,892 |
| Segment results | (2,395) | (779) | 221 | (3,812) | – | (6,765) |
| Unallocated income and expenses | | | | | | (3,688) |
| Loss from operating activities | | | | | | (10,453) |
| Finance costs | | | (189) | | (321) | (510) |
| Loss for the period | | | | | | (10,963) |

## 4. Profit (loss) from operating activities

Profit (loss) from operating activities is arrived at after charging (crediting):

| | Six months ended | |
|---|---|---|
| | **30 June 2011** | 30 June 2010 |
| | **Unaudited** | Unaudited |
| | ***US$'000*** | *US$'000* |
| Depreciation on fixed assets | **1,513** | 1,476 |
| Net gain (loss) in fair value of financial assets held for trading | | |
| – realized | **731** | 1,597 |
| – unrealised | **(45,379)** | 3,413 |

## 5. Income tax

No provision for Hong Kong profits tax has been made as, in the opinion of the Company's directors. The Group did not have any estimated assessable profits in Hong Kong for the period.

Taxation for overseas subsidiaries is charged at the appropriate current rates of taxation ruling in the relevant countries.

## 6. Earnings (loss) per share

The calculation of basic earnings (loss) per share is based on the net profit attributable to equity shareholders for the period of US$40,040,000 (2010: loss of US$10,910,000), and weighted average of 272,024,352 (2010: 233,647,186) ordinary shares in issue during the period.

The diluted earnings per share for the period is calculated by adjusting the weighted average number of ordinary shares outstanding to assume conversion of dilutive potential ordinary shares arising from the convertible debentures to 272,595,041; and the adjusted profit attributable to shareholders of the Company of US$40,047,000, being the profit attributable to the shareholders of the Company of US$40,040,000 adjusted to eliminate the interest expense of US$7,000.

## 7. Fixed assets

During the six months ended 30 June 2011 the Group acquired approximately US$2,046,000 (2010: US$5,040,000) of fixed assets.

## 8. Financial assets at fair value held for trading

| | **30 June 2011** | 31 December 2010 |
|---|---|---|
| | **Unaudited** | Audited |
| | ***US$'000*** | *US$'000* |
| Hong Kong listed shares | **15,387** | 16,798 |
| Shares traded on the OTC Bulletin Board in the United States | **45,000** | – |
| | **60,387** | 16,798 |

The Group is exposed to equity price risk through its investment in these equity securities.

## 9. Trade and note receivables

The ageing analysis of the trade and note receivables is as follows:

| | **30 June 2011** | 31 December 2010 |
|---|---|---|
| | **Unaudited** | Audited |
| | ***US$'000*** | *US$'000* |
| 0-30 days | **8,118** | 4,424 |
| 31-60 days | **1,687** | 1,997 |
| 61-90 days | **4,369** | 1,518 |
| Over 90 days | **41** | 611 |
| | **14,215** | 8,550 |

Included in trade receivables an amount of USD3,924,000 (31.12.2010: USD1,631,000) which was due from non-controlling interest.

## 10. Trade payables

The ageing analysis of the trade payables is as follows:

| | **30 June 2011** | 31 December 2010 |
|---|---|---|
| | **Unaudited** | Audited |
| | ***US$'000*** | *US$'000* |
| 0-30 days | **3,520** | 1,714 |
| 31-60 days | **1,238** | 2,156 |
| 61-90 days | **353** | 969 |
| Over 90 days | **615** | 196 |
| | **5,726** | 5,035 |

## 11. Convertible debentures

During the six-month period ended 30 June 2011, the Company issued the convertible debentures for approximately US$24,946,000. Finder's fee of US$1,247,000 have been paid to Kelton Capital Group Limited. Conversion right was exercised to convert US$25,833,000 of the convertible debentures for 52,000,000 shares of US$0.50 each.

On 4 April 2011, the Company entered into a subscription agreement with a U.S. based institutional investor for an aggregate of US$250 million 3% interest convertible debentures due April 2021.

## 12. Dividend

The Directors have decided not to declare any interim dividend for the six months ended 30 June 2011 (2010: Nil).

## 13. Share capital

| | **30 June 2011**<br>**Unaudited**<br>***US$'000*** | 31 December 2010<br>Audited<br>*US$'000* |
|---|---|---|
| Authorised: | | |
| 1,000,000,000 ordinary shares of US$0.50 each | **500,000** | 500,000 |
| Issued and fully paid: | | |
| 315,333,744 shares of US$0.50 each (31.12.2010: 263,333,744 ordinary shares of US$0.50 each) | **157,667** | 131,667 |

During the period, 52,000,000 ordinary shares of US$0.5 each were issued by exercising the convertible debentures for an aggregate consideration of approximately US$25,833,000.

## 14. Related party transactions

During the period, the Group entered into the following transactions with related party:

| | **Six months ended** | |
|---|---|---|
| | **30 June 2011**<br>**Unaudited**<br>***US$'000*** | 30 June 2010<br>Unaudited<br>*US$'000* |
| Sales to non-controlling interest | **4,384** | 5,710 |

At 31 December 2010, included in other payables and accrued expenses an amount of US$302,000 which was due to non-controlling interest.

## 15. Capital commitment

| | **30 June 2011**<br>**Unaudited**<br>***US$'000*** | 31 December 2010<br>Audited<br>*US$'000* |
|---|---|---|
| Acquisition for fixed assets | | |
| – Contracted but not provided for | **620** | – |

## 16. Comparative figures

Certain comparative figures have been reclassified to conform with current period's presentation.

## 17. Approval of the Interim Accounts

The Board of Directors of the Company approved the Interim Accounts on 30 August 2011.

# MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

(In this review, all references to "$" are to the legal currency of the United States of America, unless otherwise specified.)

For the six months ended 30 June 2011, the Group's turnover was $32.152 million as compared to $22.892 million for the same period of the prior year. The net income attributable to shareholders was $40.040 million, or $14.72 cents per share, as compared to net loss of $10.910 million, or $4.67 cents per share for the same period of 2010. On the balance sheet, the total assets of the Group as at 30 June 2011 were $209.067 million, as compared to $138.651 million at 31 December 2010, and the net assets of the Group were $186.487 million at 30 June 2011, as compared to $121.336 million at 31 December 2010.

## BUSINESS DEVELOPMENT

The Group has two principal lines of business. The first line of business is to develop and produce crude oil and minerals, such as graphite, in Asia. The second line of business is to provide electronic manufacturing services in the United Kingdom.

Through its wholly-owned subsidiary, Kalrez Petroleum (Seram) Limited, the Company operates oilfields in Indonesia under the Bula Petroleum Production Sharing Contract ("Bula PSC"), which the Group entered into with BPMIGAS, Department of Petroleum of Indonesia, on 22 May 2000. The Bula PSC will expire in 2019.

Through its wholly-owned subsidiary, South Sea Graphite (Luobei) Co., Limited ("SSG"), the Company is engaged in the business of production and sale of graphite products in Luobei, Heilongjiang Province of China. Through its wholly-owned subsidiary, Axiom Manufacturing Services Ltd. ("Axiom") in the United Kingdom, the Company provides electronics manufacturing services in the business-to-business or business-to-industry sectors and to original equipment manufacturers in the following market sectors:

- Medical devices
- Industrial control equipment
- Domestic appliances
- Computer and related products
- Testing and instrumentation products
- Ministry of Defense products

As a result of efficiently managing costs and assets, Axiom is able to offer its customers an outsourcing solution that represents a lower total cost of acquisition than that typically provided by the OEM's own manufacturing operation. OEMs contract with Axiom to build their products or to obtain services related to product development and prototyping, volume manufacturing or aftermarket support.

In many cases Axiom builds products that carry the brand names of its customers and substantially all of Axiom's manufacturing services are provided on a turnkey basis whereby Axiom purchases customer specific components from suppliers, assembles the components onto printed circuit boards, performs post production testing and provides customers with production process and test documentation. Axiom also provides manufacturing services on a consignment basis whereby materials are provided by the customers for Axiom to build into finished printed circuit boards or products. Axiom offers its customers flexible just-in-time delivery programs which allow product shipments to be closely coordinated with the customers' inventory requirements. Additionally, Axiom completes the assembly of final products for its customers by integrating the manufactured printed circuit boards into the customers' finished products. Most of Axiom's customers are located within the United Kingdom.

## Prospects

The Company believes that mineral resources are strategically valuable and worth investment over the long term. Since 2010, the price of graphite products has increased significantly in the global market. The Company deems it strategically important to procure a steady supply of graphite raw materials to ensure sustainable operation and growth of its graphite business. If financing is available on terms acceptable to the Company, the Company intends to acquire additional graphite mineral resources, increase oil production, and develop or acquire hi-technology to support and complement its existing electronics hardware business in the UK, thereby enhancing high-tech contents in its electronics products. The Company believes that these endeavors will enable it to strengthen earnings and profitability, and deliver more value to its shareholders.

On 20 June 2011, Heilongjiang South Sea Graphite Ltd ("HSSG") and RHI AG ("RHI"), a leading refractories company in the world, entered into a five-year supply agreement. Within the five-year contract period from 1 June 2011 through 30 June 2016, RHI agreed to purchase from HSSG a minimum of 80,000 metric tons ("MT") of graphite. For the first contract year ended 30 June 2012, RHI will purchase 22,000 MT of graphite from HSSG, and the total selling price is estimated to be RMB113.8 million, approximately HK$137.1 million.

## Results of Operations

For the six months ended 30 June 2011, the Group's turnover was $32.152 million, an increase of $9.260 million, or 40.5%, as compared to $22.892 million for the same period of the prior year. Specifically, for the six months ended 30 June 2011, the turnover of the Group's crude oil operation was $7.88 million as compared to $4.93 million in the same period of 2010, representing an increase of 59.8%. The increase in oil revenue was primarily due to increased production and increased average sales price of crude oil. For the same period, the Group's graphite operation generated revenues of $9.265 million, or an increase of 62.26%, as compared to $5.71 million for the six months ended 30 June 2010. The increase in the Group's graphite operation revenue was primarily due to an increase in customer orders, increase in sales price, and attaining additional new customers. For the six months ended 30 June 2011, the turnover of the Group's electronics manufacturing service operation was $14.95 million, representing an increase of $2.737 million, or 22.41%, as compared to $12.21 million for the same period of the prior year. The turnover increase in the Group's electronics manufacturing service operation was largely due to an increase in sales orders and new customers. The increase in profit for the period was mainly due to the gain in fair value of a financial asset held for trading which is traded on the OTC Bulletin Board in the United States.

## Liquidity and Capital Resources

The Group's operations are primarily funded by cash flows from its operations, and to a certain extent, from issuance of the Company's ordinary shares and convertible debentures.

At 30 June 2011, the Group's cash and cash equivalents were $19.122 million as compared to $21.591 million as at 31 December 2010. For the six months ended 30 June 2011, the Group's operating activities used net cash of $25.91 million. During the same period, the Group's investing activities used net cash of $1.787 million, primarily due to purchase of property and equipment. By comparison, net cash provided by the Group's operating activities in the same period of 2010 was $0.865 million, and net cash used in its investing activities in 2010 was $5.023 million. For the six months ended 30 June 2011, the Group's financing activities generated net cash of $24.898 million, primarily from issuance of convertible debentures of the Company.

On 4 April 2011, the Company entered into a subscription agreement with a US based institutional investor for an aggregate of US$250 million 3% interest convertible debentures due April 2021. The net proceeds were intended to be used as funding for potential acquisitions of graphite mineral resources and capital reserve to increase oil production in the Bula Oilfields, Indonesia, and to develop or acquire hi-technology to support and complement its existing electronics hardware business in the UK, thereby enhancing high-tech contents in its electronics products. The subscription agreement was approved by the majority shareholders of the Company at its annual general meeting held on 11 May 2011.

At 30 June 2011, the Group had no contingent liabilities. The Group believes that its cash balance and the cash generated from operations are adequate to meet its operating expenses and capital expenditure for the next twelve months. However, the Group's continuing operating and investing activities may require it to obtain additional sources of financing. In that case, the Group may seek financing from institutional investors, banks, or other sources of financing. There can be no assurance that any necessary additional financing will be available to the Group at that time.

## OFF BALANCE SHEET ARRANGEMENTS

At 30 June 2011, the Group had no off balance sheet arrangements.

## EMPLOYEES AND REMUNERATION POLICIES

At 30 June 2011, the Group had a total of approximately 905 employees in Indonesia, the United Kingdom, China and Hong Kong. The Group believes that its relationship with its employees is satisfactory.

From time to time, the Group may also use the services of independent consultants and contractors to perform various professional services. The remuneration of each employee of the Group is determined on the basis of his or her performance and responsibility.

## MATERIAL UNCERTAINTIES

There are no material uncertainties relating to events or conditions that may cast significant doubt upon the Company's ability to continue as a going concern.

## FOREIGN EXCHANGE EXPOSURE

The Group's principal operating subsidiaries earn revenues and incur costs in US dollars, Chinese Renminbi and British pounds, respectively. During the six-month period ended 30 June 2011, the Group did not engage in any hedging activities. The Group will continue to monitor the risk of foreign exchange fluctuation on the Group's results of operations, financial conditions and cash flow.

## LEGAL PROCEEDINGS

The Group is not aware of any pending or threatened legal proceeding that, if determined in a manner adverse to us, could have a material adverse effect on the business and operations of the Group.

## RESIGNATION AND APPOINTMENT OF AN EXECUTIVE DIRECTOR

On 8 July 2011, Mr. Zhou Ling resigned as the executive director and the chairman of the Board of the Company, and Mr. Guan Xinmin was appointed as an executive director and the chairman of the Board of the Company, both effective on 08 July 2011.

The reason for Mr. Zhou's resignation was that he desired to focus more on his personal business. He confirmed to the Board that he had no disagreement with the Board and there was no matter in respect of his resignation that needs to be brought to the attention of the shareholders of the Company.

Mr. Guan, aged 48, received his baccalaureate degree in Russian language and Russian affairs from Heilongjiangin University in 1984. Mr. Guan worked in both governmental sector and private companies, with nearly 30 years' experiences in trading mineral products in China and European countries. He has established broad mineral products procurement and marketing channels in the Chinese and Russian markets.

Before being appointed as an executive director, Mr. Guan had been our General Purchasing Manager since 2009. He does not hold any other directorship in the last three years in any public companies listed in Hong Kong or overseas. Mr. Guan does not have any relationship with any other directors, senior management, substantial shareholders or controlling shareholders. As at the date of this report, Mr. Guan does not have any interests in shares of the Company within the meaning of Part XV of the Securities and Futures Ordinance (Chapter 571 of the Laws of Hong Kong).

## ESTABLISHMENT OF A WHOLLY-OWNED SUBSIDIARY

On 19 May 2011, a memorandum has been reached between the Company and Beijing Dance Theater ("BDT"), a not-for-profit organization in Beijing, China, and the Company decided to establish a wholly owned subsidiary in Hong Kong, Unicorn Arts Limited ("Unicorn"), to promote arts and enhance its corporate social responsibility.

Under the memorandum, Unicorn and BDT will cooperate with each other in the production of artistic and cultural events to be held in China and overseas. Both Unicorn and BDT agreed to donate part of the income from such events to charitable organizations in China, including Hong Kong, which will be earmarked for natural disaster relief. The Company will invest HK$500,000 in Unicorn as its working capital.

## MAJOR CUSTOMERS AND SUPPLIERS

During the six-month period ended 30 June 2011, the Group's purchases from the five largest suppliers accounted for approximately 37.35% of the Group's total purchases and purchases from the largest supplier included therein accounted for approximately 10.89% of the Group's total purchases.

During this period under review, the Group's sales to the five largest customers accounted for approximately 65.87% of the Group's total turnover and sales to the largest customer included therein accounted for approximately 19.39% of the Group's total sales.

None of the directors of the Company, their associates, nor any shareholders which to the best knowledge of the directors own more than 5% of the Company's issued share capital, had any beneficial interests in the Group's five largest customers and suppliers for the period under review.

## DIRECTORS' AND CHIEF EXECUTIVE'S INTERESTS AND SHORT POSITIONS IN SHARES, UNDERLYING SHARES AND DEBENTURES

Save as disclosed in the section "Substantial Shareholders" as set forth in the Company's Corporate Governance Report stated below, at 30 June 2011, none of the directors or chief executives of the Company or any of their associates had any interests and short positions in the shares, underlying shares and debentures of the Company or any of its associated corporations as recorded in the registers maintained by the Company pursuant to Section 352 of the Securities and Futures Ordinance (Chapter 571, Laws of Hong Kong) (the "SFO"), or as otherwise notified to the Company and The Stock Exchange of Hong Kong Limited (the "Stock Exchange") pursuant to the Model Code for Securities Transactions by Directors of Listed Issuers.

All directors have confirmed that they complied with the required standards set out in the Model Code for Securities Transactions by Directors of Listed Issuers as set out in Appendix 10 to the Listing Rules throughout the review period.

At 30 June 2011, former director and chief executive officer of the Company, who was resigned on 8 July, 2011, held following long positions in the ordinary share of the Company:

| | Number of Ordinary Shares held | | Approximate % |
|---|---|---|---|
| **Name** | **Personal Interests** | **Corporate Interests** | **of shareholding** |
| Zhou Ling | – | 640,000 | 0.29% |

Save as disclosed above, as at the date of this report, none of the directors and executive officers of the Company and their respective associates had any interest or short position in the shares, underlying shares and debentures of the Company or any of its associated corporations that were required, pursuant to Section 352 of the Securities and Futures Ordinance ("SFO"), to be entered in the register referred to therein or which were required, pursuant to the Model Code contained in the Listing Rules, to be notified to the Company and the Stock Exchange.

## DIRECTORS' INTERESTS IN CONTRACTS

For the six months ended 30 June 2011, none of the Company's directors had a material interest, either direct or indirect, in any contract of significance to the business of the Company to which the Company or any of its subsidiaries was a party.

At no time during the year was the Company or any of the Company's subsidiaries a party to any arrangements to enable the directors of the Company to acquire benefits by means of the acquisition of shares, or debentures of, the Company or any other body corporate.

## ARRANGEMENT TO PURCHASE SHARES OR DEBENTURES

At no time during the period under review was the Company or any of its subsidiaries, a party to any arrangements to enable the Company's directors or chief executives to acquire benefits by means of the acquisition of shares in or debentures of the Company or any other body corporate.

## SUBSTANTIAL SHAREHOLDERS' AND OTHER PERSONS' INTERESTS AND SHORT POSITIONS IN SHARES AND UNDERLYING SHARES

At 30 June 2011, no person, other than a director or chief executive's interests which are disclosed in the section "Directors' and Chief Executive's Interests and Short Positions in Shares, Underlying Shares and Debentures" above, had registered an interest, short position, or lending poor in the shares or underlying shares or debentures of the Company that was required to be kept by the Company pursuant to Section 336 of the SFO.

## DIVIDENDS

The Directors have decided not to declare any interim dividend for the six months ended 30 June 2011 (2010: Nil).

## COMPLIANCE WITH THE CODE ON CORPORATE GOVERNANCE PRACTICES

The Company has complied with the all the code provisions as set forth in the Code on Corporate Governance Practices contained in Appendix 14 to the Rules Governing the Listing of Securities ("Listing Rules") on The Stock Exchange of Hong Kong Limited throughout the accounting period covered by the interim report.

## COMPLIANCE WITH THE MODE CODE

The Company has adopted the Model Code for Securities Transactions by Directors by Listed Issuers (the "Model Code") set out in Appendix 10 of the Listing Rules. Upon enquiry by the Company, all directors of the Company have confirmed that they have complied with the required standards set out in the Model Code throughout the six months ended 30 June 2011.

## REVIEW BY THE AUDIT COMMITTEE

The Audit Committee has reviewed with management the accounting principles and practices adopted by the Company and discussed auditing, internal controls and financial reporting matters, including a review of the Unaudited Interim Accounts of the Group for the six months ended 30 June 2011.

## PUBLICATION OF REPORT

The interim report will be published on website of the Stock Exchange of Hong Kong Limited (http://www.hkex.com.hk) and website of the Company (http://www.southseapetro.com.hk).

On behalf of the Board

**Guan Xinmin**
*Chairman*

Hong Kong, 30 August 2011